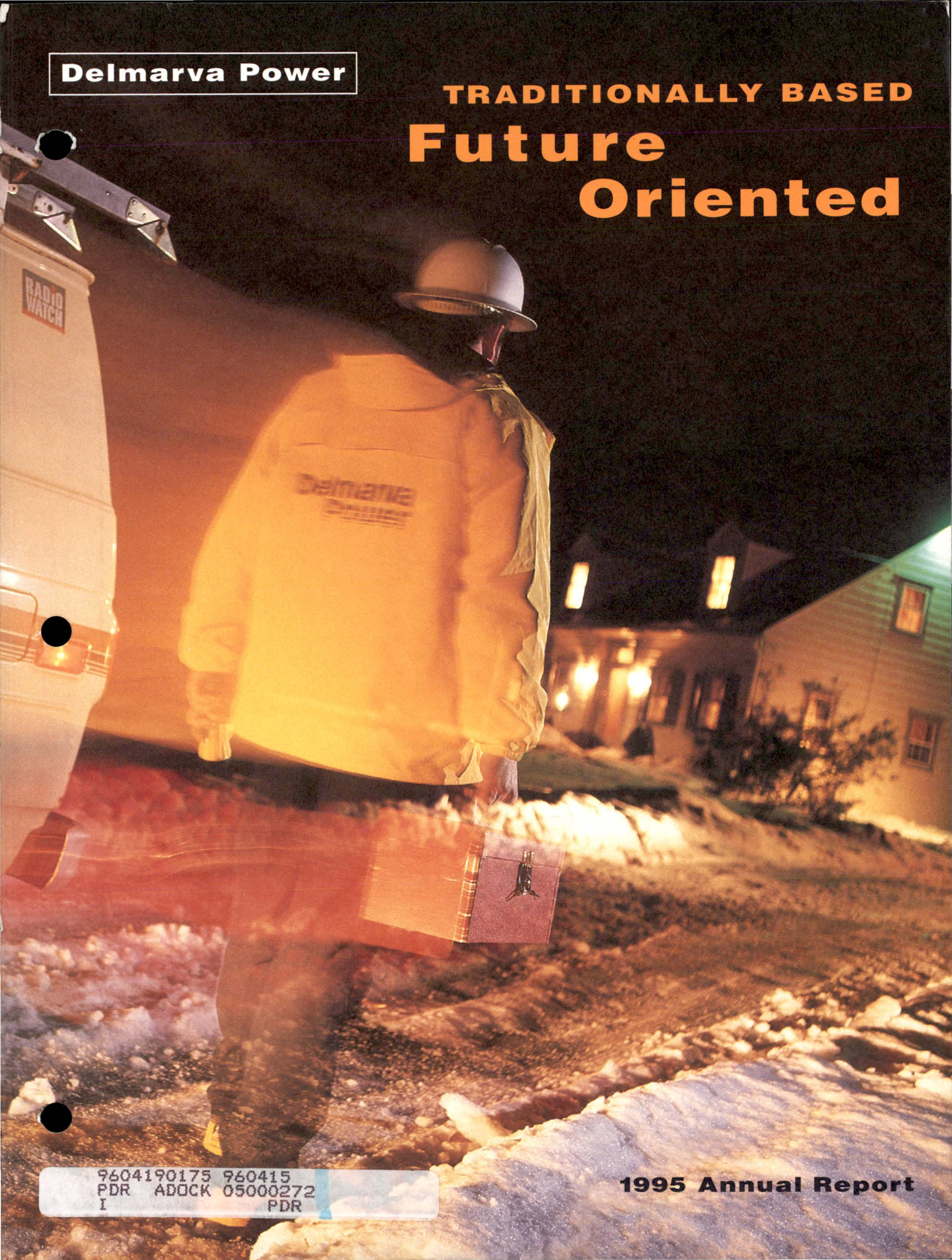
Delmarva Power

TRADITIONALLY BASED
Future Oriented



1995 Annual Report

HIGHLIGHTS

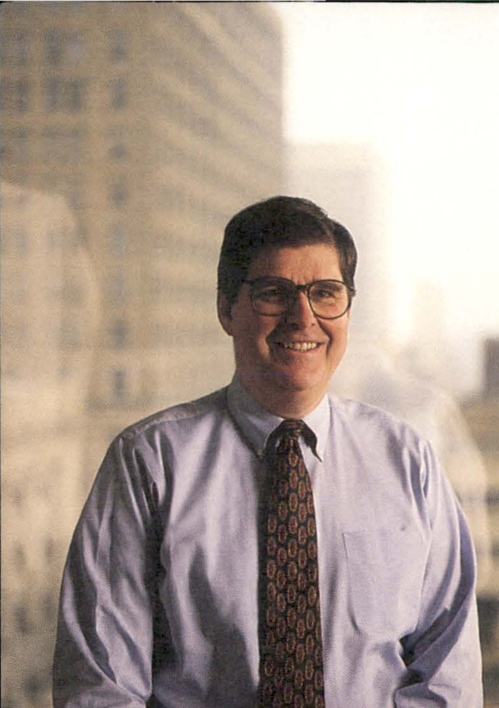
	1995	1994	% Increase (Decrease)
Revenues	$995,103,000	$991,021,000	0.4%
Net Income	$117,488,000	$108,310,000	8.5%
Earnings per Share	$1.79	$1.67 (1)	7.2%
Dividends Declared per Share	$1.54	$1.54	—
Electric Sales	12,310,921 mWh	12,505,082 mWh	(1.6)%
Gas Sales & Transportation	21.37 million mcf	20.34 million mcf	5.1%
Electric Customers	436,650	393,372	11.0%
Gas Customers	98,417	95,662	2.9%

(1) Reduced by an $0.18 per share charge for an early retirement offer.

An expanded version of the Company's financial highlights can be found on pages 20 to 48.

Our success will be built on our traditional base of reliable service, competitive prices, and customer satisfaction.

Our orientation in the future is to expand our customer relationships and seize opportunities for growth in the region.



"As our industry moves from a regulated to a competitive environment, electric utilities must change the way they do business. My message to you is that Delmarva Power is changing and prospering in this new competitive arena."

— Howard E. Cosgrove
Chairman, President, and
Chief Executive Officer

Dear Fellow Shareholder,

Our company is in the midst of an exciting industry transition. Examples of changing utility business are reported almost daily and include extensive bidding for wholesale contracts, regulatory changes, proposed state and federal legislation, power pool restructuring, and planned mergers and acquisitions.

The message is clear: As our industry moves from a regulated to a competitive environment, electric utilities must change the way they do business. My message to you is that Delmarva Power is changing and prospering in this new competitive arena.

Across the company, we are working to satisfy our customers, increase efficiency, and deliver shareholder value. In the future, our success depends on our ability to retain and attract new customers, market new energy-related services and products, and continuously improve efficiency.

Performing in a Competitive Environment

Delmarva Power performed well in 1995. We remain the low-cost energy provider in the Mid-Atlantic region. We successfully integrated former Conowingo Power customers and employees into the company. We met an ambitious earnings target, maintained our current dividend, and remain a solid investment for our shareholders, providing an above-average total return on your investment.

In addition, Delmarva Power demonstrated an ability to compete in a changing business environment. Our wholesale customers now have the option choosing their energy supplier, which made this segment of the business fiercely competitive last year. Our company made significant progress in this new environment. Despite widespread bidding from other energy suppliers, we retained all of our municipal customers by signing long-term energy sales agreements.

Increasing Efficiency

We serve 125,000 more customers today than we did ten years ago with fewer employees. Our energy prices are less today than they were ten years ago. And today, our customer favorability ratings are higher than a decade ago and are among the highest in the country. More than eight out of ten customers tell us that we deliver quality service in a timely manner.

I applaud our employees for their cost control activities, which continue to keep operating and maintenance expenses well below the regional average. Teams of Delmarva Power employees are improving the way we work throughout the company—from purchasing to fleet management—to increase efficiency and improve service to our customers. In addition, we are revamping our information technology systems so that employees at all levels have immediate access to key information needed in a competitive business environment.

We serve 125,000 more customers today than we did ten years ago with fewer employees. Our energy prices are less today than they were ten years ago. And today, our customer favorability ratings are higher than a decade ago and are among the highest in the country.

While we work to increase revenue and reduce expenses, we continue to be negatively affected by costs related to the outage of the Salem Nuclear Generating Station. As this report goes to press, Public Service Electric and Gas Company (PSE&G) has announced that the outage of Unit 1 will be extended for an indefinite period while they assess the condition of the unit's four steam generators. Unit 2 is scheduled to return to service in the third quarter of 1996. Last year, we were able to absorb Delmarva Power's share of the outage-related costs as a 7.41% owner of Salem. I am concerned about the implications of the extended outage at Unit 1, increasing costs, and the possibility of adverse regulatory treatment. We will pursue other avenues of recovery this year to mitigate the financial impact of the Salem situation.

Changing to Meet Customer Needs

Providing quality customer service has traditionally been a top priority and a strength for Delmarva Power. As customer needs evolve, we will continue to redefine our relationships with those we serve. The needs of our generation customers are different today than in the past. Our transmission and distribution customers have increasing needs and expanded options. At the same time, we continue to extend our relationships with our customers by providing energy service beyond the meter.

In order to meet these changing customer needs, we are functionally organizing our business into three strategic business units—energy supply, regulated delivery services, and energy services—focused on customers and supported by internal administrative services. Dividing our business functions into separate groups will allow us to strengthen our ability to deliver profitable, customized energy service to those we serve.

Developing New Products and Services

This past year we expanded and redirected our marketing team to enhance our ability to reach out to customers in our service territory and throughout the region. We now offer new energy products and services and will continue to build on our traditional values—reliable service, customer satisfaction, and competitive prices.

- We are leveraging our core operating and engineering expertise by offering design, construction, operating, and maintenance consulting services to municipal, cooperative, commercial, and industrial customers.
- We launched Surge Solution℠, our first new offering in a growing line of energy products for our residential customers. Surge Solution protects sensitive electronic appliances from damage caused by lightning-related power surges.
- We are working closely with neighboring communities, governments, and businesses to attract new customers and new jobs to our area.
- We are also exploring exciting new opportunities to use our engineering expertise and energy delivery infrastructure to provide services to the telecommunications industry, whose infrastructure needs are similar to our own.

Delmarva Power will face new challenges and exciting opportunities to build on our foundation of reliable service, customer satisfaction, and competitive prices.

Focusing on the Future

Our overall strategy to remain a top financial performer emphasizes the retail side of our business, where face-to-face contact with individual customers adds value to our energy service. We will also take advantage of new growth opportunities and continue to grow earnings by aligning our business with others, and by working with communities to bring new businesses and jobs to our area.

We will manage our wholesale portfolio by strengthening our ties with the customers who value the services we provide and by changing our relationships with the customers who have a different emphasis or focus. In the meantime, we know that industrial and commercial customers will be the next groups to be able to choose their energy supplier. We have already signed long-term agreements with several key industrial customers. Our goal is to establish similar alliances with other commercial and industrial customers throughout our region.

We support choice for all of our energy customers. In February 1996, we presented to the Delaware and Maryland Public Service Commissions a proposal to enter into a collaborative process to foster the change from a regulated to a competitive energy market. Our objective is to work together to develop solutions to key issues, including retail wheeling, functional unbundling, performance-based pricing, and expanded options for our customers.

As we move forward through 1996 and beyond, Delmarva Power will face new challenges and exciting opportunities to build on our tradition of reliable service, customer satisfaction, and competitive prices. Our company will continue to take steps to exceed customer expectations and provide an above-average total return on your investment. We are committed to directing industry change to your advantage. I am confident we are up to the task.

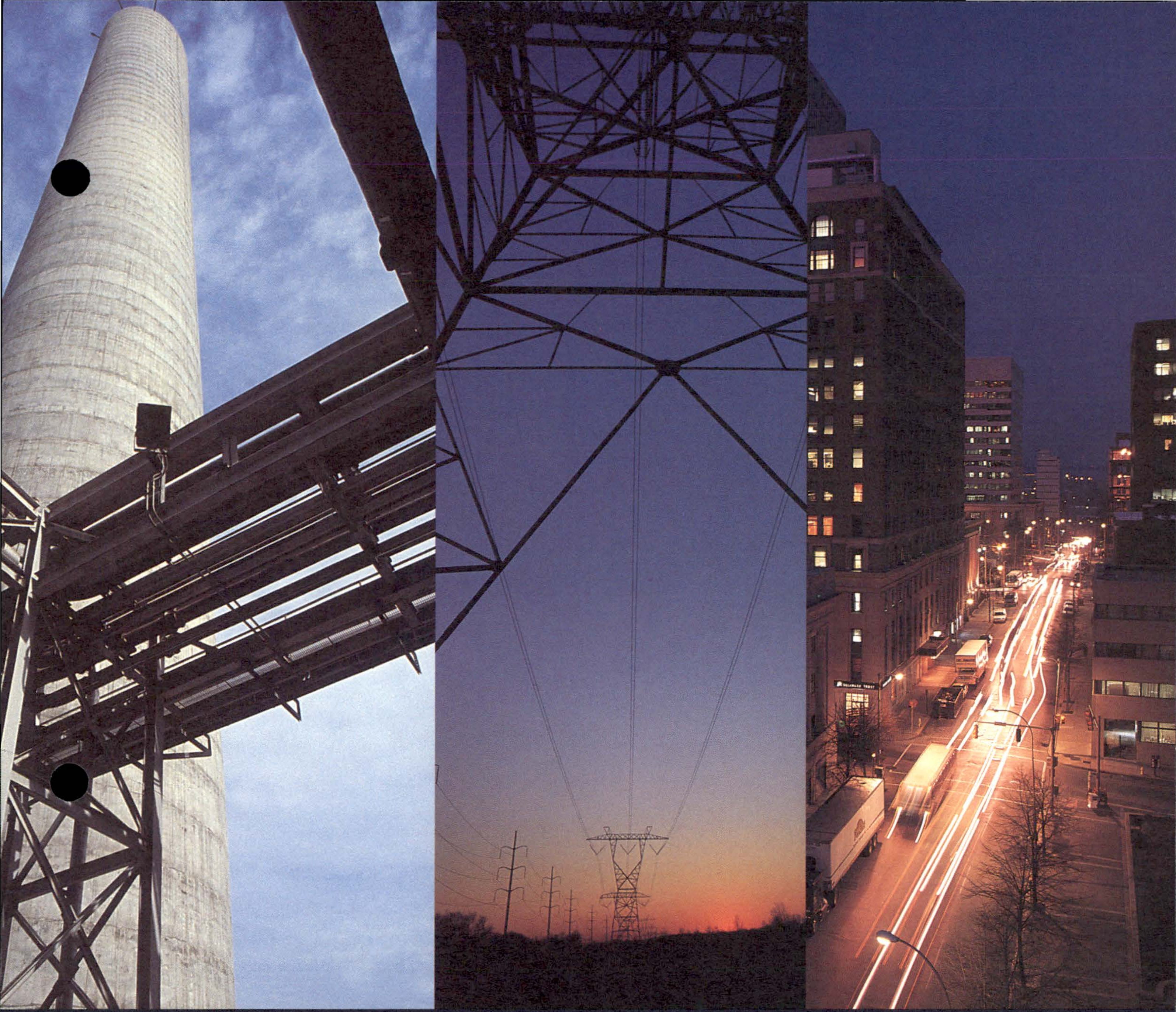
As always, I appreciate your support.

Sincerely,

Howard Cosgrove

Howard E. Cosgrove

Chairman, President, and Chief Executive Officer



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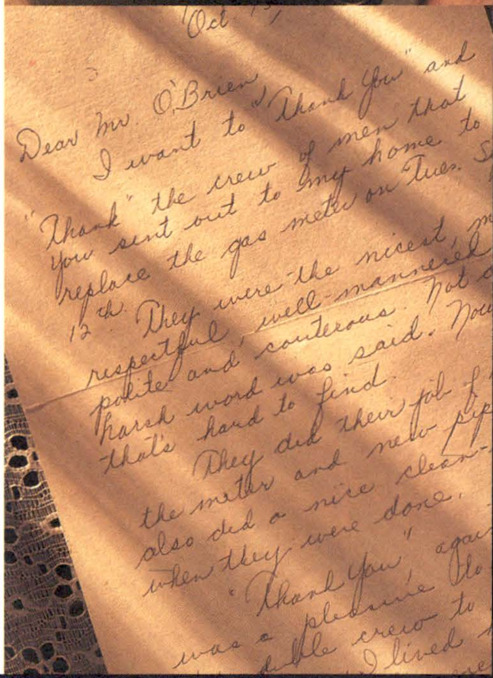
We've looked into the future of the utility business. Where some people see power plants, we see commodities. Where some people see power lines, we see energy delivery opportunities. Where some people see a brightly lighted landscape, we see customers, allies, people.

Building On Traditional Values

Over the years, we've developed rapport and trust with our customers. They know they can depend on us for reliable service and accurate information. This customer loyalty is vital to our success in a more competitive industry. We're offering customers more of what they want and need. When our customers have a choice about their energy supplier, we want them to choose us.

From power plants to helpful customer service representatives, Delmarva Power provides the service our customers rely on. That bedrock of our success is the foundation for our future growth.

Keeping Our Energy Reliable. Customers like Martha Morris expect their electronic equipment to be on line when they need it, their lights to go on when they flip a switch, and their air conditioners to run without pause. That reliable electricity depends on the professional, efficient operation of our power plants. Last fall, our largest coal-burning unit, Unit #4 at our Indian River Power Plant, was scheduled for Clean Air Act revisions. Our production department employees took that opportunity to overhaul the unit to ensure its availability and competitiveness over the long term. We replaced the unit's twenty-four burners and installed an electronic control system that will improve the unit's performance and assure compliance with stringent environmental regulations.



Service When Our Customers Need It. When Donald Ferris's gas furnace broke down, he called us. "Your serviceman was at my door within an hour," Don reported. Don's natural gas appliances are protected through the Gas Service Plan. He knows we'll fix them whenever they break down, day or night. All our customers trust us to restore their service as quickly as we can, no matter what the cause. When a fierce windstorm swept over Ocean City, Maryland, trouble-and-servicemen like Graison Wainwright, below, repaired the damage in record time. Delmarva Power's growth in the future is grounded in such consistent, dedicated service.

Responsive To Customer Calls. Our customer service representatives fielded more than one million customer telephone calls last year and they did it with a smile. Our customers responded, writing letters of appreciation and calling with their thanks. We anticipate an increase in the number of calls each year as we grow. How do we ensure they all get answered? We consolidated our telephone centers and instituted an 800 number. Customers can also make inquiries and download the latest information on Delmarva Power products and services through our Internet site, **http://www.delmarva.com**. Simple solutions for our busy customers are also cost effective for Delmarva Power.

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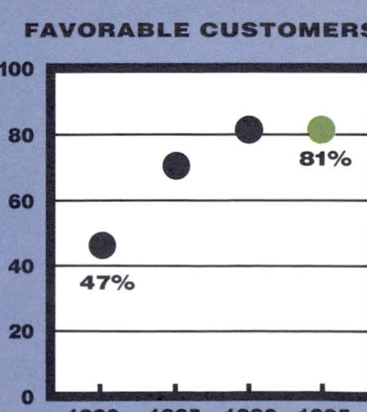

Over the past fifteen years, our favorability rating has almost doubled.

Partnering For Future Growth

Through proven winners like the Gas Service Plan, we've successfully taken our business beyond the meter for more than 20 years. We're also taking our commercial and industrial business from the outside in through energy management agreements, strategic business alliances, and power quality evaluations.

We Tailor Our Agreements. In the fall of 1995, Al Williams, national accounts manager, asked Alan Levin, president of Happy Harry's, a growing regional retailer, about his energy management policies. Who oversees his energy costs? Are his buildings energy efficient? How can we help? Levin is impressed that Delmarva Power has taken an interest in his business at this level. We're cementing a strategic relationship, sharing business resources with a longtime, growing customer. Our energy-related expertise can take Happy Harry's well into the next century.

Strategic Alliances With Customers. Our strategic alliances are built on our electrical service and equipment expertise. For example, MBNA America, the world's second largest lender through bank credit cards, recently moved into an additional location in Delaware. Through a fifteen-year agreement, Delmarva Power will operate, maintain, test, and repair outdoor electrical equipment there.

Power Quality Keeps Industry Thriving. Our commercial and industrial customers depend on our reliable service to power their electrical equipment. Most power-related operating problems, however, are caused by power disturbances within a building. Our power quality services group assesses vulnerability to such disturbances, provides electrical diagnostics, and engineers solutions to help businesses eliminate and prevent internally generated problems. Power quality evaluations help keep our customers' equipment operating efficiently, consistently, and profitably.

Energy Expertise. From comfortable living rooms to corporate corridors, we are thinking and acting on our customers' behalf. In fact, since 1994, we've developed eleven new business services, from power quality to substation maintenance. Our residential customers can also look forward to new beyond-the-meter products and services. We're taking our energy expertise beyond the peninsula, talking to regional companies about establishing energy and business alliances. As the utility industry changes, these alliances will provide another growing source of revenue for Delmarva Power.

We're developing new products for customers' security and ease at home. The first of these, Surge Solution℠, offers whole-house protection against lightning-related surges that could ruin delicate and expensive home electronics. Based on Surge Solution's successful introduction, more new products are on the way.

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"In an increasingly competitive business environment, we need to find ways to become more efficient. Our alliance with Delmarva Power enables us to concentrate our efforts on our core retail business."

—Alan Levin
President, Happy Harry's

Securing Our Economic Future

In 1995, we stabilized all our municipal relationships through long-term energy sales agreements. We're working to finalize facilities management and other energy-related alliances with other wholesale customers. In addition, through our collaborative efforts with state and local governments and active business recruitment, we help keep businesses here and attract new ones to the area.

Economic Development. When PRS Guitars' owner Paul Reed Smith needed more concrete information to make a move to Maryland's Eastern Shore, the Queen Anne's County Development Office called us. We developed a rate analysis that showed power costs on the Eastern Shore to be 8% below those PRS was paying. We evaluated different heating and air-conditioning systems for energy efficiency. No detail was too small, down to who was to own the transformer. By November 1995, PRS had purchased a building in Stevensville on Kent Island. We gained a new, growing industrial customer, one of a dozen we helped bring to the peninsula last year. And we're negotiating with more.

Energy Sales And Management. The lights on Lakeview Avenue go on one by one. Gradually the City of Milford, Delaware, is illuminated with power supplied by us. In 1995, Milford signed an eight-year energy sales agreement with Delmarva Power. We had restructured its rate, saving the city a significant sum over the length of the contract. But Milford needed more from us—our energy facilities management expertise. When Milford's utility manager left, we stepped in to manage the facility under a one-year agreement. We're working with other municipalities to formulate energy-related options that meet their needs.

We work hard to secure energy sales agreements and to bring businesses and jobs to the areas we live in and serve. Armed with detailed power cost analyses, we helped bring a dozen new, growing businesses here in 1995. Bringing industry and businesses into the peninsula helps the people here who need jobs and increases revenues for the area and for Delmarva Power.

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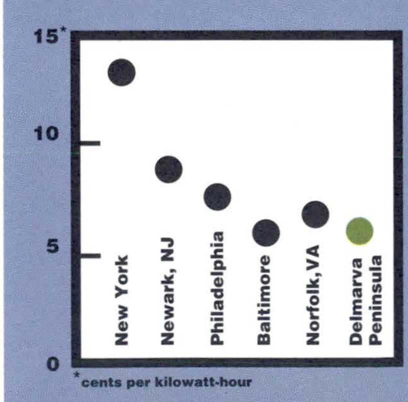
LOWER PRICES



Our energy prices rank among the lowest on the Eastern Seaboard.

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Future [Based On] Tradition

An opportunity to add 37,000 new customers presents itself—250 people from all over the company work together to make it happen. A hurricane knocks out power to 100,000 people in Ocean City. Our crews restore 90% of all service 24 hours ahead of schedule. How can we move so fast and so well? Our employees have learned to think on their feet and act. We learned to listen to our customers. These skills are paying off every day for Delmarva Power, our customers, shareholders, and employees.

Our dedicated employees will make our growth in the future a reality. Their ability to act quickly and safely as a team is vital to our success. They're ready for the challenge.

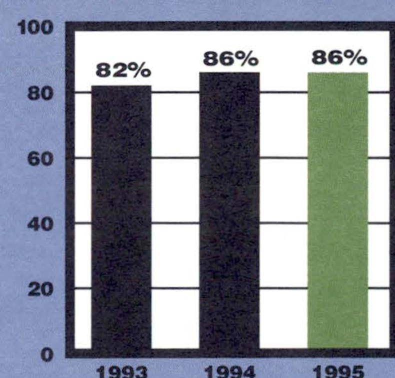
Taking Action For Change. Our employees have learned to make important decisions quickly. In the early 1980s, we began to streamline our decision-making process with the introduction of PSP, the participative skills process. PSP is based on the premise that the people closest to a problem know best how to deal with it. Knowing a problem first-hand and being confident in making a decision, however, takes practice. Delmarva Power employees have honed their skills, bringing a depth of experience to each new situation we face. Our employees can evaluate on the spot and decide on the right action. Then they take it.

Gaining Customers. We've already moved quickly when an opportunity came along. In 1994, we offered to buy the Conowingo Power Company from PECO Energy Company. This purchase would bring 37,000 new customers to Delmarva Power. In June 1995, we sealed the sale and created the Conowingo District. Our new customers have services and programs never available to them before. And their rates are approximately 20% lower than those projected by Conowingo Power Company for 1996. Purchasing Conowingo enhanced our value by increasing our retail revenue.

Increasing Sales Opportunities. In early 1995, our marketing department sent out a call to Delmarva Power employees to become actively involved in providing sales leads and ideas, supporting sales efforts, and seeking sales opportunities. Using point rankings for different categories, employees were encouraged to achieve 100,000 sales success points by the end of 1995. Once again, we exceeded our own expectations, accumulating almost 155,000 sales success points. But what do those points add up to? Over $12.5 million in revenues for Delmarva Power in 1995.

Working Together For The Future. With our Conowingo purchase, we gained more than customers; we also gained 60 new employees. Today they work side by side with long-time Delmarva Power employees. They quickly became part of our team for the future. Pictured from back to front are District Manager, Tim Smith; Michele McKeever; Mark Dell; Karen Shivers; Rich Stickley; Paige Copes; Deborah Mann; Julie Tall; Maralyn Webb; Stan Mohn; and Russell Robinson.

KEEPING OUR CUSTOMERS SAFE



Our customers consistently rank us highly in our concern for their safety.

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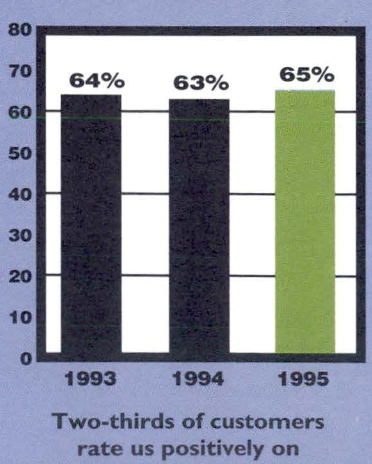
SERVING & CONSERVING DELMARVA



Two-thirds of customers rate us positively on environmental protection.

Traditional Commitment

To Our Communities

Stop some Delmarva Power customers on the street and ask them about us. They'll probably tell you they know someone who works for Delmarva. But our customers know us not only because our employees are highly visible contributors to their communities on the job—they're vital to their communities off the job, volunteering so that people will live better.

Our employees are highly visible in their communities, volunteering wherever they see a need. Those needs are diverse, from senior citizens waiting for a hot meal to traditional watermen concerned about their way of life.

Helping People Who Need It. More than a dozen people around Wilmington look forward to seeing Gary Fullman and Alice Parks at lunch. Throughout the week during their lunch hours, Gary, Alice, and up to 40 other Delmarva Power volunteers deliver Meals on Wheels to senior citizens, ensuring that they get a hot meal that day. For the people who receive the food, this may be their only contact with other people for the day. And that contact is almost as important as the meal.

Upholding Our Traditions. The waterman's open boat on the Chesapeake Bay is as familiar on the Eastern Shore as the yellow Delmarva Power truck out in a storm. Because of Delmarva Power volunteers, though, the association is more than poetic. At the beginning of the 20th century, 17.5 million pounds of shad were harvested each year in the Chesapeake Bay area. By the 1970s, the shad population was almost nonexistent and a moratorium was placed on shad fishing. The moratorium is still in place today. Last spring, Vienna Power Plant volunteers at our fish hatchery there fed 20,000 shad larvae three times a day, seven days a week for several weeks. They worked hard—off the job—to raise the shad for release into the waters of the Nanticoke River. For commercial watermen, moratoriums spell the end of their way of life. But fish hatchery volunteers helped lift a similar moratorium on striped bass fishing. They'll do the same with shad.

Volunteering For Our Communities. Meals on Wheels and the fish hatchery work only because employees volunteer their time. And Delmarva Power volunteers do more. They coach Little League. They fight fires. They teach reading. They coordinate fund-raising events. They mentor students. Why do they work so hard on their off time? Because they live here. Because they want to. Because through their efforts, their communities are better places to live. Restoring power or restoring the spirits of an old friend, our employees are on the job for their communities every day.

Strategy Committee members Tom Shaw, Barbara Graham, Ralph Klesius, Howard Cosgrove, and Joseph Ford discuss ways to seize new opportunities for growth in the region.

A Vision For The Future

Your investment in Delmarva Power is in good hands. Our Board of Directors and Strategy Committee are committed to directing industry change to your advantage by building on our traditional strengths and planning ahead for a challenging future.

Board of Directors

as of December 31, 1995

Michael G. Abercrombie, President of Cato Inc. (a petroleum distributorship), Salisbury, Maryland; member since 1993; serves on nominating and nuclear oversight committees; term expires in 1996.

R. Franklin Balotti, Member of the law firm of Richards Layton & Finger, Wilmington, Delaware; member since 1995; term expires in 1997.

Robert D. Burris, President of Burris Foods Inc. (a refrigerated food distribution company); Milford, Delaware; member since 1993; serves on audit and nuclear oversight committees; term expires in 1996.

Howard E. Cosgrove, Chairman of the Board, President, and Chief Executive Officer of the Company; member since 1986; serves on executive, investment, and nuclear oversight committees; term expires in 1998.

Audrey K. Doberstein, President of Wilmington College, New Castle, Delaware; member since 1992; serves on audit, investment, and nominating committees; term expires in 1998.

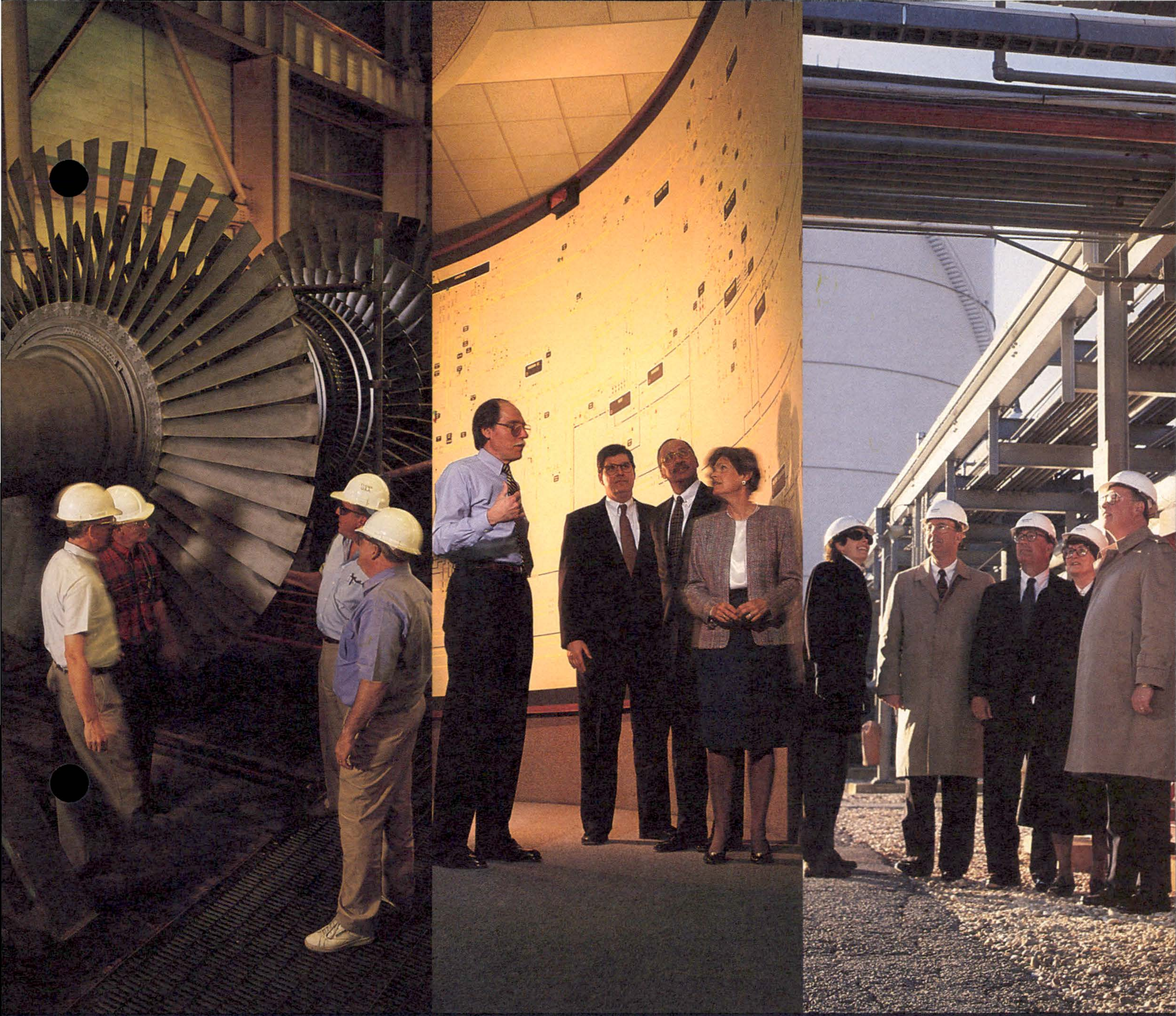
Michael B. Emery, Senior Vice President of E.I. duPont de Nemours & Company (a diversified chemical, energy, and specialty products company), Wilmington, Delaware; member since 1994; serves on compensation and executive committees; term expires in 1997.

James H. Gilliam Jr., Director, Executive Vice President, and General Counsel of the Beneficial Corporation (a financial services company), Wilmington, Delaware; member since 1993; serves on compensation and investment committees; term expires in 1996.

Sarah I. Gore, Human Resources Associate, W. L. Gore & Associates, Inc. (a high technology manufacturing company), Newark, Delaware; member since 1990; serves on compensation and executive committees; term expires in 1997.

James C. Johnson, President and Chief Executive Officer of Loyola Federal Savings Bank, Baltimore, Maryland; member since 1992; serves on audit, compensation, and executive committees; term expires in 1998.

Weston E. Nellius, President, Nellius Management Associates (a financial, management, and government relations consulting firm), Dover, Delaware; member since 1995; serves on investment and nominating committees; term expires in 1998.



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Our Board of Directors takes to the field to keep abreast of improvements in and changes to our operations. Left, Indian River Power Plant Manager Chuck Gates with Board members Michael Abercrombie, Robert Burris, and Pete Nellius examine the newly overhauled turbine. Center, Jim Wittine of Systems Operations discusses with Directors Howard Cosgrove, James Gilliam, and Sarah Gore how Systems Operations ensures service reliability and quick restoration. Right, Nancy Giove of our Gas Division with Board members James Johnson, Frank Balotti, Audrey Doberstein, and Michael Emery inspect our natural gas storage facility.

REGIONAL ENERGY PRICES	ELECTRIC	GAS
New York	13.64	76.61
Newark, N.J.	9.64	52.76
Philadelphia	7.91	76.62
Baltimore	6.06	59.73
Norfolk, Va.	6.38	74.13
Delmarva Peninsula	6.07	51.97

The chart states electric prices in cents per kilowatt-hour and natural gas prices in cents per 100 cubic feet for the 12 months ended September 30, 1995

TEN-YEAR ANNUAL AVERAGE GROWTH RATE	
Electric sales (mWh)	3.7%
Gas sales & transportation (mcf)	3.1%
Electric customers	3.2%
Gas customers	2.7%

Delmarva Power has a 100-year tradition of providing electric and natural gas services to customers on the Delmarva Peninsula. We're growing in our traditional area, having added more than 46,000 customers last year. But we're expanding our horizons for the future. Our proximity to major markets along the Eastern Seaboard and upcoming regulatory changes will enable us to move new energy products and services beyond the meter and beyond the peninsula into the greater region. Within 150 miles lie Baltimore, Washington, Philadelphia, and New York City. One third of the population of the United State lives within 350 miles of us. We're well positioned for the competitive future, using our traditional strengths to meet it successfully.

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Selected Financial Data

(Dollars in Thousands, Except Per Share Amounts)

	Year Ended December 31,				
	1995	1994	1993	1992	1991
Operating Results and Data					
Operating Revenues	**$995,103**	$991,021	$970,607	$864,044	$855,821
Operating Income	**$178,406**	$163,156(1)	$164,139	$143,711(2)	$136,410
Income Before Cumulative Effect of a Change in Accounting Principle	**$117,488**	$108,310(1)	$111,076	$98,526(2)	$80,506
Cumulative Effect of a Change in Accounting for Unbilled Revenues	**—**	—	—	—	$12,730
Net Income	**$117,488**	$108,310(1)	$111,076	$98,526(2)	$93,236
Earnings Applicable to Common Stock	**$107,546**	$98,940(1)	$101,074	$90,177(2)	$85,259
Electric Sales (kWh 000)(3)	**12,310,921**	12,505,082	12,280,230	11,520,811	11,460,280
Gas Sold and Transported (mcf 000)	**21,371**	20,342	19,605	20,168	18,184
Common Stock Information					
Earnings Per Share of Common Stock Before Cumulative Effect of a Change in Accounting Principle	**$1.79**	$1.67(1)	$1.76	$1.69(2)	$1.44
Cumulative Effect of a Change in Accounting for Unbilled Revenues	**—**	—	—	—	$0.25
Total Earnings Per Share	**$1.79**	$1.67(1)	$1.76	$1.69(2)	$1.69
Dividends Declared Per Share of Common Stock	**$1.54**	$1.54	$1.54	$1.54	$1.54
Average Shares Outstanding (000)	**60,217**	59,377	57,557	53,456	50,581
Year-End Common Stock Price	**$22 3/4**	$18 9/64	$23 5/8	$23 1/4	$21 1/4
Book Value Per Common Share	**$15.20**	$14.85	$14.66	$13.77	$13.42
Return on Average Common Equity	**11.7%**	11.1%	12.0%	12.2%	12.4%
Capitalization					
Variable Rate Demand Bonds (VRDB) (4)	**$86,500**	$71,500	$41,500	$41,500	$41,500
Long-Term Debt	**853,904**	774,558	736,368	787,387	770,146
Preferred Stock	**168,085**	168,085	168,085	176,365	136,365
Common Stockholders' Equity	**923,440**	884,169	862,195	745,789	706,583
Total Capitalization with VRDB	**$2,031,929**	$1,898,312	$1,808,148	$1,751,041	$1,654,594
Other Information					
Total Assets	**$2,866,685**	$2,669,785	$2,592,479	$2,374,793	$2,263,718
Long-Term Capital Lease Obligation	**$20,768**	$19,660	$23,335	$26,081	$29,337
Construction Expenditures (5)	**$135,614**	$154,119	$159,991	$207,439	$181,820
Internally Generated Funds (IGF) (6)	**$137,394**	$123,948	$108,693	$130,275	$96,081
IGF as a Percent of Construction Expenditures	**101%**	80%	68%	63%	53%

(1) An early retirement offer decreased earnings net of income taxes and earnings per share by $10.7 million and $0.18, respectively.

(2) The settlement of a lawsuit with PECO Energy Company increased earnings net of income taxes and earnings per share by $11.4 million and $0.21, respectively.

(3) Excludes interchange deliveries.

(4) Although Variable Rate Demand Bonds are classified as current liabilities, the Company intends to use the bonds as a source of long-term financing as discussed in Note 12 to the Consolidated Financial Statements.

(5) Excludes Allowance for Funds Used During Construction.

(6) Net cash provided by operating activities less common and preferred dividends.

Earnings Summary

The earnings per average share of common stock attributed to the core utility business and nonutility subsidiaries are shown below.

	1995	1994	1993
Core Utility			
Operations	**$1.72**	$1.81	$1.73
Early Retirement Offer	**—**	(0.18)	—
	1.72	1.63	1.73
Nonutility Subsidiaries	**0.07**	0.04	0.03
Total	**$1.79**	$1.67	$1.76

Earnings per share from core utility operations decreased by $0.09 in 1995 compared to 1994 due to a portion of estimated additional costs that were expensed for the Salem Nuclear Generating Station (Salem) arising from operational problems, including the current outage, which is discussed further under "Salem Outage." Excluding the portion of estimated additional costs that were expensed for Salem, earnings per share from core utility operations in 1995 were unchanged from 1994, reflecting the Company's success in offsetting decreased wholesale (resale) revenues with a combination of cost reduction efforts, retail sales growth, and modest price increases pursuant to the Company's "Three-Legged Stool" strategy, which is discussed further under "Strategic Plans for Competition—Resale Business." Operating results from the new Conowingo District, which began in June 1995 as a result of the Company's acquisition of Conowingo Power Company (COPCO), had a minimal impact on earnings, as expected. Refer to Note 4 to the Consolidated Financial Statements for information concerning the Company's acquisition of COPCO.

Earnings per share from core utility operations increased by $0.08 in 1994 compared to 1993 primarily due to additional electric base revenues from rate increases and additional electric sales. The earnings growth from additional electric base revenues was partially offset by higher depreciation expense and the dilutive effect of additional common shares outstanding.

Core utility earnings were reduced in 1994 by $10.7 million after taxes, or $0.18 per share, to reflect a voluntary early retirement offer (ERO), which resulted in a work force reduction of 10.5% or 296 people. Refer to Note 5 to the Consolidated Financial Statements for additional information concerning the ERO.

Dividends

On December 20, 1995, the Board of Directors declared a common stock dividend of $0.38 1/2 per share for the fourth quarter. As the utility industry moves from a regulated to a competitive environment, the Company believes it can best provide shareholder value through maintaining the current dividend level and providing annual earnings growth. Over time, this strategy is expected to reduce the Company's dividend payout ratio and allow the Company to invest in opportunities that are anticipated to have a sustainable positive impact on earnings growth.

Salem Outage

The Company owns 7.41% of Salem, which consists of two pressurized water nuclear reactors (PWR) and is operated by Public Service Electric & Gas Company (PSE&G). As of December 31, 1995, the Company's net investment in plant in-service for Salem was approximately $57 million for Unit 1 and $60 million for Unit 2. Each unit represents approximately 2% of the Company's total assets and approximately 3% of the Company's installed electric generating capacity.

Salem Units 1 and 2 were removed from operation by PSE&G on May 16, 1995, and June 7, 1995, respectively, due to operational problems and maintenance concerns. The units will remain shut down until PSE&G makes the equipment and management changes necessary to operate the units reliably over the long term. The restart of the units is subject to Nuclear Regulatory Commission (NRC) authorization. In December 1995, PSE&G completed a workscope assessment of both units and estimated that Unit 1 would return to service in the second quarter of 1996 and Unit 2 in the third quarter of 1996.

On February 21, 1996, PSE&G informed the Company that partial results from recent inspections of Unit 1 using a new testing technology revealed indications of degradation in a significant number of steam generator tubes. PSE&G is continuing its inspections and also will conduct further laboratory analysis of the tubes with results expected in April 1996. Based on the results of inspections to date, PSE&G has concluded that the Unit 1 outage will be extended for an indefinite period to evaluate the state of the steam generators and to subsequently determine an appropriate course of action. Degradation of steam generators in PWRs has become of increasing concern for the nuclear industry. Nationally and internationally, utilities have undertaken actions to repair or replace steam generators. In the extreme, degradation of steam generators has contributed to the retirement of several American nuclear power reactors.

PSE&G also has informed the Company that recent steam generator inspections of Unit 2 using the new testing technology have revealed that the condition of the Unit 2 steam generators is within current repair limits at the present time. However, to confirm the Unit 2 test results, PSE&G also will conduct laboratory analysis of the tubes for Unit 2. As a result of the delay in the restart of Unit 1, PSE&G is focusing its efforts on the return of Unit 2 to service in the third quarter of 1996, as scheduled. However, the Company cannot predict when the NRC will approve the restart of the unit or when the restart actually will occur.

In 1995, the Company incurred higher than expected operation and maintenance costs at Salem of approximately $5 million, which reflect the operational problems at the plant. These costs were expensed as incurred. Also, outage-related replacement power costs were estimated to be approximately $8 million. One-half of the estimated replacement power costs was expensed and the other one-half was deferred on the Company's Consolidated Balance Sheet in expectation of future recovery. Based on PSE&G's current estimates, the Company estimates that its share of additional costs related to the outage in 1996 will consist of operation and maintenance costs ranging from $4 million to $7 million, which will be expensed as incurred, and replacement power costs while the units are out of service of approximately $750,000 per month, per unit. In total, the Company estimates that its share of outage-related costs in 1996 will range from $17 million to $22 million. However, these 1996 estimates could change as a result of PSE&G's analysis of the degradation of the steam generator tubes. Beyond 1996, the Company cannot predict the amount of outage-related costs it could incur. During 1996, the Company plans to file a proposal with the Delaware Public Service Commission (DPSC), the Company's primary rate jurisdiction, for recovery of replacement power costs.

Since the periods during which these units will be out of service, the extent of the maintenance that will be required, and the costs of replacement power and the extent of its recovery may be different from those currently anticipated, the actual costs to be incurred by the Company may vary from the foregoing estimates.

Strategic Plans for Competition

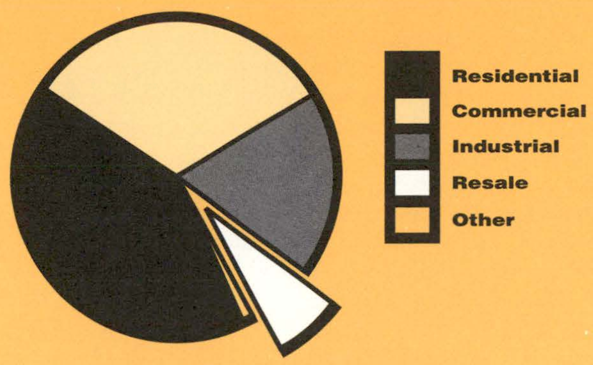
The electric resale segment of the utility industry has become highly competitive as a result of federal legislation. Resale customers now can choose their electric supplier. Competition in the retail markets also is being discussed at both the Federal and State levels. As the retail segment of the industry transitions to a more competitive market, the Company is making changes in the way it manages its business.

Resale Business

The Company's total electric resale revenues as a percent of total billed electric sales revenues decreased from 13% in 1994 to 7% in 1995, primarily due to Old Dominion Electric Cooperative's (ODEC) purchase of about one-half of its capacity and energy requirements from other suppliers beginning January 1, 1995. The resulting decrease in resale non-fuel revenues in 1995 of $24.2 million was offset through the Company's "Three-Legged Stool" strategy, which involved a combination of cost reduction efforts, retail sales growth, and modest price increases.

The Company has reduced substantially the financial risk related to its resale business. In 1994 and 1995, the Company successfully bid against other suppliers and retained all of its municipal customers under long-term contracts. In addition, the Company negotiated extended notice provisions on the remaining portion of ODEC's capacity and energy requirements served by the Company. These notice provisions require ODEC to provide the Company with two years' notice for up to a 30% load reduction and five years' notice for load reductions greater than 30%. ODEC has indicated that it may issue a request for proposals in early 1996 for the remaining portion of its capacity and energy requirements currently served by the Company. To the extent there is any further reduction in load, the notice provisions provide the Company with the ability to manage the financial impact.

REDUCED RESALE FINANCIAL RISK



1995 Billed Electric Sales Revenues

The Company has substantially reduced the financial risk of its resale business by signing long-term contracts and extended notice provisions with all of its resale customers.

Retail Business

Retail customers also are expected to be able to choose their energy suppliers in the future. The Company is well positioned for competition, due to its relatively low prices within the region, and is taking steps to manage its separate businesses in a competitive market, as discussed below.

During 1995, the Company introduced various new products and services and extended its markets into the region. Through an expanded marketing team, the Company is offering consulting, design, construction, and operating and maintenance services to commercial, industrial, and resale customers; developing and marketing residential products and services; and exploring the use of its energy delivery infrastructure to provide services to the telecommunications industry. In addition, the Company is working closely with neighboring communities, governments, and businesses to attract new customers and new jobs to the Company's service territory.

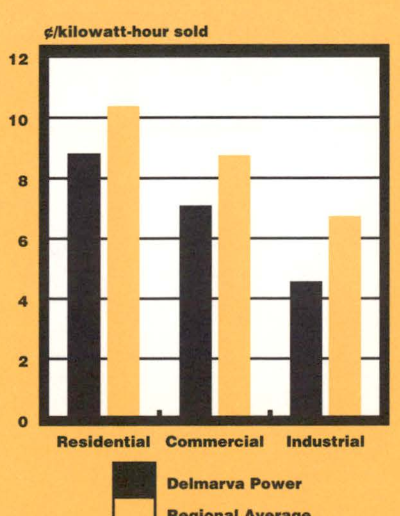
During 1996, the Company will reorganize into three separate business units—energy supply, regulated delivery, and energy services—to better focus on the evolving energy markets. The Company also is investing in information technology systems that will provide immediate access to the information needed to manage the business units in a competitive environment.

In February 1996, the Company presented to the DPSC and the Maryland Public Service Commission a proposal to enter into a collaborative process to develop the transition from a regulated to a competitive energy market. The Company believes that the benefits of a competitive market can best be realized when addressed together by the Company, the Commissions, and customers. The Company also believes that this process should develop solutions for the following key issues: retail wheeling, stranded investment, the unbundling of electric price elements, and performance-based pricing mechanisms. The first goal will be to seek agreement on the objectives and principles for the transition to a market that allows choices for all customers. Afterwards, specific details and filings with the Commissions will be addressed.

Impact of Competition on Stranded Costs

As the electric utility industry transitions from a regulated to a competitive environment, utilities may not be able to recover certain costs, resulting in these costs being "stranded." Stranded costs could result from the shift from current cost-of-service based pricing to market-based pricing and from customers changing energy suppliers. Potential stranded costs include above-market costs associated with generation facilities; long-term purchased power contracts; and regulatory assets, which are expenses that have been deferred pending recovery from customers pursuant to Statement of Financial Accounting Standards (SFAS) No. 71, "Accounting for the Effects of Certain Types of Regulation." If changes in the regulatory environment ultimately require a recognition of any stranded costs, the Company could be required to write down asset values, and such write-downs could be material. However, since the time frame of further deregulation, the market conditions relative to capacity and energy demand and prices at the time of deregulation, and the extent to which regulatory commissions allow recovery of stranded costs are not known at this time, the Company cannot predict the level of stranded costs it could incur. Based on recent independent studies, the Company has less exposure to stranded costs than many other utilities in the industry.

Refer to "Impact of New Accounting Standards" for discussion of a related topic and Note 8 to the Consolidated Financial Statements for additional information on regulatory assets.



ELECTRIC PRICE COMPARISON*

The Company's prices for electricity are below the regional average. A balanced and flexible energy supply plan helped the Company gain this advantage.

*Based on 1994 data

Components of Utility Revenues

Fuel and energy costs billed to customers (fuel revenues) generally are based on rates in effect in fuel adjustment clauses which are adjusted periodically to reflect cost changes and are subject to regulatory approval. Rates for non-fuel costs billed to customers are dependent on rates determined in base rate proceedings before regulatory commissions. Changes in non-fuel (base rate) revenues can affect directly the earnings of the Company. Fuel revenues, or fuel costs billed to customers, generally do not affect net income, since the expense recognized as fuel costs is adjusted to match the fuel revenues. The amount of under- or over-recovered fuel costs generally is deferred until it is subsequently recovered from or returned to utility customers.

Electric revenues also include interchange delivery revenues which result primarily from the sale of electric power to utilities in the Pennsylvania-New Jersey-Maryland Interconnection Association (PJM Interconnection). The PJM Interconnection is an electric power pool comprised of eight utilities in the region, including the Company. The power pool provides both capital and operating economies to member utilities. Interchange delivery revenues are reflected in the calculation of rates charged to customers under fuel adjustment clauses. Due to this ratemaking treatment, interchange delivery revenues generally do not affect net income.

Electric Revenues and Sales

In 1995, the percentages of total billed sales revenues contributed by the various customer classes were as follows: residential—41.4%; commercial—32.1%; industrial—18.6%; resale—7.0%; and other—0.9%.

Details of the changes in the various components of electric revenues are shown below.

Comparative Increase (Decrease) from Prior Year in Electric Revenues

(Dollars in Millions)	1995	1994
Non-fuel (Base Rate) Revenues		
Retail Sales Volume	**$54.9**	$4.1
Resale Sales Volume	**(24.2)**	(0.2)
Increased Rates	**3.3**	15.9
Fuel Revenues	**(6.9)**	(15.4)
Interchange Delivery Revenues	**(15.1)**	1.0
Other Operating Revenues	**4.5**	2.1
Total	**$16.5**	$7.5

For 1995 compared to 1994, Non-fuel Revenues increased $54.9 million from Retail Sales Volume due to a 7.3% increase in total retail kilowatt-hour (kWh) sales, which resulted primarily from Conowingo District sales beginning June 19, 1995. Excluding the Conowingo District, retail sales increased 2.9%, mainly due to higher commercial sales resulting from a strong economy in the Company's service territory, a 1.4% increase in the number of retail customers, and the favorable impact of hotter summer weather. Excluding the Conowingo District, billed sales to residential and commercial customers increased by 1.1% and 4.5%, respectively; industrial sales were flat.

For 1994 compared to 1993, Non-fuel Revenues increased $4.1 million from Retail Sales Volume due to a 1.9% increase in total retail sales, which resulted primarily from a 1.6% increase in the total number of retail customers, an improving economy in the Company's service territory, and colder winter weather, offset in part by cooler summer weather. Billed sales to residential and commercial customers increased by 2.3% and 3.7%, respectively; industrial sales were flat.

Non-fuel Revenues decreased $24.2 million in 1995 from Resale Sales Volume due to a 44.0% decrease in resale sales, mainly due to ODEC's purchase of about one-half of its capacity and energy requirements from other suppliers beginning January 1, 1995. Changes in resale sales have less of an impact on non-fuel revenues than changes in retail sales, since average resale non-fuel rates are significantly lower than average retail non-fuel rates.

The increases in Non-fuel Revenues from Increased Rates resulted from increases in electric customer base rates which became effective during 1993 and 1995. Refer to Note 2 to the Consolidated Financial Statements for information concerning these rate increases.

In 1995, Fuel Revenues decreased $6.9 million mainly due to lower total sales. In 1994, Fuel Revenues decreased $15.4 million due to lower rates charged to customers under the fuel adjustment clauses, partially offset by higher total sales.

In 1995, Interchange Delivery Revenues decreased $15.1 million, mainly due to lower sales and billing rates to the PJM Interconnection.

Gas Revenues, Sales, and Transportation

The Company earns gas revenues from the sale of gas to customers and also from transporting gas through the Company's system for some customers who purchase gas directly from other suppliers.

In 1995, total gas revenues decreased $12.5 million from 1994 because of a $4.0 million increase in non-fuel revenues and a $16.5 million decrease in fuel revenues. The increase in non-fuel revenues was due to $2.7 million of additional revenue from a base rate increase that became effective November 1, 1994, and a $1.3 million increase in sales volume. Total volumes of gas sold and transported in 1995 increased 5.1% due to a 1.9% increase in firm gas sales, resulting primarily from a 2.9% increase in the number of customers, and a 17.2% increase in non-firm sales and gas transported. Gas fuel revenues decreased $16.5 million in 1995 due to lower average fuel rates charged to customers and a $6.8 million refund in 1995 of over-recovered fuel costs.

In 1994, total gas revenues increased $13.0 million from 1993 due to a $3.0 million increase in non-fuel revenues and a $10.0 million increase in fuel revenues. The increase in non-fuel revenues was due to $0.6 million of additional revenue from a November 1, 1994 base rate increase and a $2.4 million increase in sales volume. Total volumes of gas sold and transported in 1994 increased 3.8% due to a 2.9% increase in the number of customers and colder winter weather during the first quarter. Gas fuel revenues increased $10.0 million in 1994 due to higher average fuel rates and higher sales.

Electric Fuel and Purchased Power Expenses

In 1995, electric fuel and purchased power expenses decreased $14.7 million from 1994 primarily due to lower kWh output and lower purchased power prices. The $14.7 million decrease is net of $4.1 million of expense, which represents one-half of the total Salem outage-related replacement power costs that were estimated for 1995.

In 1994, electric fuel and purchased power expenses decreased $15.7 million from 1993 primarily due to variances in fuel costs deferred and subsequently amortized under the Company's fuel adjustment clauses.

The kWh output required to serve load within the Company's service territory is substantially equivalent to total output less interchange deliveries. In 1995, the Company's output for load within its service territory was provided by 39.4% coal generation, 32.1% oil and gas generation,16.4% net purchased power, and 12.1% nuclear generation.

Gas Purchased

For 1995, compared to 1994, the cost of gas purchased decreased $15.2 million, primarily due to a $6.8 million refund in 1995 of over-recovered fuel costs and variances in fuel costs deferred and subsequently amortized under the Company's fuel adjustment clause. The refund of over-recovered fuel costs reduced the amount of expense recorded for gas purchased because fuel expense is adjusted to match fuel revenues as explained under "Components of Utility Revenues."

For 1994, compared to 1993, the cost of gas purchased increased $10.2 million, primarily due to variances in fuel costs deferred and subsequently amortized under the Company's fuel adjustment clause.

Operation, Maintenance, Depreciation, and Income Tax Expenses

Operation and maintenance expenses increased in 1995 by $8.0 million compared to 1994. The most significant factor contributing to the increase was $29.5 million of costs related to the Conowingo District, including $26.1 million for capacity purchase charges under the Company's contracts to purchase the Conowingo District's electric power requirements from PECO Energy Company (PECO). Also contributing to the increase in expense were higher than expected costs at Salem of approximately $5 million, which reflect the operational problems at the plant, including the current outage. Largely offsetting these increases were a $17.5 million ERO expense recorded in 1994, salary and wage savings in 1995 from reduced staff levels, and lower storm damage costs.

Operation and maintenance expenses increased in 1994 by $19.2 million compared to 1993 due mainly to the following factors: the $17.5 million ERO expense, a $3.5 million increase in winter storm damage costs, a $3.5 million increase in the cost for postretirement benefits other than pensions (OPEB), and a $7.8 million reduction in pension expense, of which $4.5 million was due to a lower assumed rate of salary increase. The Company's OPEB costs were deferred during part of 1993 due to probable rate recovery. In 1994, the deferral for the Delaware jurisdiction (electric and gas) was expensed in accordance with a settlement agreement, approved October 18, 1994, concerning the Company's gas base rate case.

Depreciation expense increased in 1995, primarily due to the addition of the Conowingo District. In 1994, depreciation expense increased mainly due to additions to the electric system, including Hay Road Unit 4 in mid-1993.

Inflation affects the Company through increased operating expenses and higher replacement costs for utility plant assets. Although timely rate increases can lessen the effects of inflation, due to competition and the changing nature of the utility industry, the Company does not plan to file for an increase in base rates in the near term. The Company plans to use its existing cost control programs and sales initiatives as its primary means to mitigate the effects of inflation.

Income tax expense on operations increased $7.4 million in 1995 in comparison to 1994 and decreased $2.0 million in 1994 in comparison to 1993, mainly due to a corresponding increase and decrease in pre-tax income.

Utility Financing Costs

Interest expense increased $6.3 million in 1995 in comparison to 1994, primarily due to the issuance of debt to acquire COPCO. Also contributing to the increase were higher average short-term debt balances and rates. Interest expense decreased $2.0 million in 1994, mainly due to the redemption on June 1, 1993, of $50 million of 10% First Mortgage Bonds with proceeds from a public offering of common stock.

Allowance for equity and borrowed funds used during construction (AFUDC) decreased $2.4 million in 1995, mainly due to a lower AFUDC rate. The decrease in AFUDC of $3.6 million in 1994 was primarily due to lower average construction balances.

Due to common equity financing, the average number of shares of common stock outstanding increased in 1995 and 1994. The additional shares outstanding decreased earnings per share by $0.03 in 1995 and $0.05 in 1994.

Energy Supply

The Company's energy supply plan reflects its strategy to provide an adequate, reliable supply of electricity to customers, while minimizing adverse impacts on the environment and keeping prices competitive. This plan, which is updated annually, is based on forecasts of demand for electricity in the service territory and reserve requirements of the PJM Interconnection. The plan emphasizes balance and flexibility, and may be accelerated, slowed, or altered in response to changing energy demands, fluctuating fuel prices, and emerging technologies. The plan considers customer-oriented load management and strategic conservation programs ("demand-side" alternatives), with short-term power purchases, long-term power contracts, and new or renovated power plants ("supply-side" alternatives).

The plan currently matches customers' energy requirements and does not require large investments for new resources. The Company must balance the risks of providing too much or too little capacity. The main risks of too much capacity are that the Company's prices may become uncompetitive and that regulators may not allow the associated costs to be recovered through customer rates. The principal risks of inadequate capacity are unreliable service and the payment of capacity deficiency charges to the PJM Interconnection. The PJM Interconnection requires the Company to plan for and to provide an adequate capacity level.

During the past three years, the Company's plan has reduced customers' demand for electricity by an additional 47 megawatts (MW), provided 205 MW of capacity from a long-term power contract with PECO beginning in 1996, and provided 175 MW of capacity from a new power plant, Hay Road Unit 4. Looking forward through 2000, the Company's plan includes the following provisions:

(1) "Demand-side" — No additional peak load reduction through customer-oriented load management and strategic conservation programs. The Company filed to close its existing demand-side programs to new participants in Delaware and Maryland on October 3, 1995, because these programs are not considered the most appropriate and cost effective resources for meeting future demand requirements.

(2) "Supply-side" — Starting in 1997 and continuing through 2000, up to 125 MW of short-term power purchases, in addition to the long-term power contract discussed above.

Liquidity and Capital Resources

The Company's primary capital resources are internally generated funds (net cash provided by operating activities less common and preferred dividends) and external financings. These resources provide capital for utility plant construction expenditures and other capital requirements, such as repayment of maturing debt and capital lease obligations. Utility construction expenditures are the Company's largest on-going capital requirement and are affected by many factors, including growth in demand for electricity, compliance with environmental regulations, and the need for improvement and replacement of existing facilities.

Operating activities provided cash inflows of $239.4 million in 1995, $224.6 million in 1994, and $206.7 million in 1993. After deducting common and preferred dividend payments of $102.0 million in 1995, $100.6 million in 1994, and $98.0 million in 1993, internally generated funds were $137.4 million in 1995, $124.0 million in 1994, $108.7 million in 1993. Internally generated funds provided 101%, 80%, and 68% of the cash required for utility construction in 1995, 1994, and 1993, respectively.

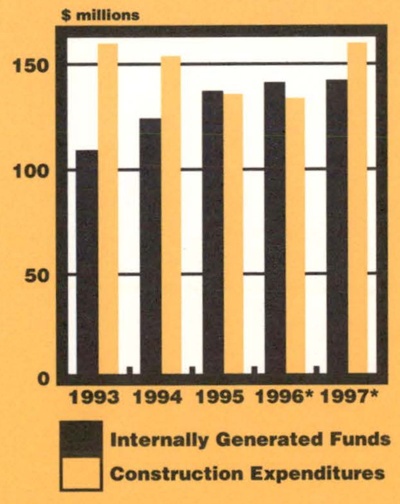
Utility construction expenditures were $135.6 million in 1995, $154.1 million in 1994, and $160.0 million in 1993. Construction expenditures in 1995, 1994, and 1993 included $16.4 million, $20.7 million, and $9.2 million, respectively, for projects attributed to environmental compliance.

In 1995, the Company acquired COPCO for $158.2 million ($157.0 million net of cash acquired) with $125.8 million of long-term debt and the balance with short-term debt. During 1993–1995, investments by the Company's nonutility subsidiaries were primarily construction expenditures at a landfill business as well as the purchase of a $5.7 million office building in 1994. In 1995 and 1994, the subsidiaries raised $3.7 million and $4.6 million, respectively, through the sale of real estate. In 1993, the subsidiaries sold interests in leveraged leases, which resulted in a $21.5 million cash inflow.

Capital raised externally during 1993–1995, net of $303.3 million of redemptions and refinancings, consisted of $146.3 million of common stock, $67.0 million of long-term debt, and $45.0 million of variable rate demand bonds. Preferred stock outstanding decreased $8.3 million. After considering $15.2 million of costs associated with issuing and refinancing debt and equity securities during 1993–1995, the net amount of capital raised from external financings during this period was $234.8 million.

Issuances of common stock during 1993–1995 included a public offering in 1993 of 3,300,000 shares for $77.1 million. The Company's 1993 financing requirements associated with utility plant were principally satisfied by issuing common stock in order to strengthen the Company's capital structure. Additional common stock was issued during 1993–1995, primarily through the Dividend Reinvestment and Common Share Purchase Plan (DRIP). Depending on the financing needs of the Company, shares issued through the DRIP may be either newly issued shares or shares purchased in the open market. During 1993–1995, shares issued through the DRIP were newly issued shares, except during the last seven months of 1994 when the shares were purchased in the open market. Effective January 1, 1996, shares issued through the DRIP are being purchased in the open market. Book value per share of common stock increased to $15.20 as of December 31, 1995, from $14.85 as of December 31, 1994.

In addition to the Company's issuance in 1995 of $125.8 million of long-term debt to acquire COPCO, one of the Company's nonutility subsidiaries issued $15.0 million of variable rate demand bonds to finance the past and future expansion of its landfill business. During the year, the Company's term loan balance of $45.0 million was repaid using cash from operations. No other significant debt redemption occurred in 1995.



INTERNALLY GENERATED FUNDS & CONSTRUCTION EXPENDITURES

The percentage of construction expenditures funded internally is expected to remain high through 1997.

* Forecast

The Company's capital structure as of December 31, 1995 and 1994, expressed as a percentage of total capitalization, is shown below.

	1995	1994
Long-term debt and variable rate demand bonds	**46.3%**	44.6%
Preferred stock	**8.3%**	8.8%
Common stockholders' equity	**45.4%**	46.6%

Capital requirements for the period 1996–1997 are estimated to be $324 million, including $25 million for maturity of First Mortgage Bonds in 1997 and $294 million for utility construction expenditures, excluding AFUDC. The estimate of 1996–1997 utility construction expenditures includes $11 million related to environmental compliance plans, including provision of the Clean Air Act Amendments of 1990. During 1998–2000, an additional $42 million of construction expenditures (excluding AFUDC) related to compliance with environmental regulations are planned.

The Company anticipates that $283 million will be generated internally during 1996–1997, net of power purchase commitments. This represents 87% of estimated capital requirements and 96% of estimated utility construction expenditures for 1996–1997. During this period, no long-term external financings are presently planned.

Since the Company's future construction program, internal generation of funds, and need for outside capital will be affected by such matters as customer demand, inflation, competition, and rate regulation, future results may vary from the foregoing estimates.

Nonutility Subsidiaries

Information on the Company's nonutility subsidiaries, in addition to the following discussion, can be found in Notes 1 and 18 to the Consolidated Financial Statements.

Earnings per share of nonutility subsidiaries were $0.07 in 1995 in comparison to $0.04 in 1994. The $0.03 increase in earnings was primarily due to higher recoveries of previously written-off joint venture assets, the receipt of an additional payment related to a prior year sale of a leveraged lease interest, and a 1994 adjustment to reduce the realizable value of oil and gas wells. The increase in 1995 earnings was partially offset by lower earnings from solid waste group operations. Both 1995 and 1994 included gains from the sale of real estate.

Earnings per share of nonutility subsidiaries were $0.04 in 1994 in comparison to $0.03 in 1993. The $0.01 increase in earnings was mainly attributed to gains on the sale of real estate, improved operating results of the solid waste group, and higher earnings from various other nonutility business activities. These earnings increases were largely offset by a 1994 adjustment to the realizable value of oil and gas wells and by 1993 after-tax gains on sales of leveraged leases.

Impact of New Accounting Standards

In March 1995, the Financial Accounting Standards Board (FASB) issued SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," which requires the Company to review long-lived assets and certain identifiable intangibles held and used by the Company for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If an asset is considered impaired, then its value would be written down with a corresponding charge to earnings. SFAS No. 121 also requires rate-regulated companies to write off regulatory assets against earnings whenever those assets no longer meet the criteria for recognition of a regulatory asset as defined by SFAS No. 71. The new standard is effective in 1996. Based on current circumstances, the Company does not expect the adoption of SFAS No. 121 to have a material effect upon the Company's financial condition or results of operations. However, the effects of the electric utility industry's transition to a competitive environment could result in the future write-down of asset values as discussed under "Strategic Plans for Competition—Impact of Competition on Stranded Costs."

In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation," which encourages, but does not require, entities to recognize compensation costs for stock-based employee compensation plans using a fair value based method of accounting rather than the intrinsic value based method of accounting currently prescribed by Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." Entities electing to continue using the accounting prescribed by APB Opinion No. 25 are required to disclose pro forma net income and earnings per share as if the fair value based method of accounting under SFAS No. 123 had been applied. The new standard is effective in 1996. The Company does not expect to adopt the accounting provisions of SFAS No. 123 for income statement recognition purposes.

Report of Management

Management is responsible for the information and representations contained in the Company's financial statements. Our financial statements have been prepared in conformity with generally accepted accounting principles, based upon currently available facts and circumstances and management's best estimates and judgments of the expected effects of events and transactions.

Delmarva Power & Light Company maintains a system of internal controls designed to provide reasonable, but not absolute, assurance of the reliability of the financial records and the protection of assets. The internal control system is supported by written administrative policies, a program of internal audits, and procedures to assure the selection and training of qualified personnel.

Coopers & Lybrand L.L.P., independent accountants, are engaged to audit the financial statements and express their opinion thereon. Their audits are conducted in accordance with generally accepted auditing standards which include a review of selected internal controls to determine the nature, timing, and extent of audit tests to be applied.

The Audit Committee of the Board of Directors, composed of outside directors only, meets with management, internal auditors, and independent accountants to review accounting, auditing, and financial reporting matters. The independent accountants are appointed by the Board on recommendation of the Audit Committee, subject to stockholder approval.

Howard E. Cosgrove

Howard E. Cosgrove
Chairman of the Board, President,
and Chief Executive Officer

Barbara S. Graham

Barbara S. Graham
Senior Vice President, Treasurer,
and Chief Financial Officer

Report of Independent Accountants

To the Board of Directors and Stockholders
Delmarva Power & Light Company
Wilmington, Delaware

We have audited the accompanying consolidated balance sheets and statements of capitalization of Delmarva Power & Light Company and Subsidiary Companies as of December 31, 1995 and 1994, and the related consolidated statements of income, changes in common stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1995. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Delmarva Power & Light Company and Subsidiary Companies as of December 31, 1995 and 1994, and the consolidated results of their operations and their cash flows for each of the three years in the period ended December 31, 1995, in conformity with generally accepted accounting principles.

Coopers & Lybrand L.L.P.

2400 Eleven Penn Center
Philadelphia, Pennsylvania
February 2, 1996, except as to the information presented under the caption Salem Outage in Note 16, for which the date is February 26, 1996

Consolidated Statements of Income

(Dollars in Thousands)	Year Ended December 31, 1995	1994	1993
Operating Revenues			
Electric	**$899,662**	$883,115	$875,663
Gas	**95,441**	107,906	94,944
	995,103	991,021	970,607
Operating Expenses			
Electric fuel and purchased power	**267,885**	282,570	298,307
Gas purchased	**48,615**	63,814	53,631
Operation and maintenance	**275,165**	267,207	248,052
Depreciation	**113,022**	109,523	100,929
Taxes other than income taxes	**38,449**	38,585	37,419
Income taxes	**73,561**	66,166	68,130
	816,697	827,865	806,468
Operating Income	**178,406**	163,156	164,139
Other Income			
Nonutility Subsidiaries			
Revenues and gains	**52,042**	43,142	37,636
Expenses including interest and income taxes	**(47,896)**	(40,790)	(35,828)
Net earnings of nonutility subsidiaries	**4,146**	2,352	1,808
Allowance for equity funds used during construction	**708**	3,389	5,309
Other income, net of income taxes	**557**	(285)	511
	5,411	5,456	7,628
Income Before Utility Interest Charges	**183,817**	168,612	171,767
Utility Interest Charges			
Interest expense	**68,395**	62,076	64,095
Allowance for borrowed funds used during construction	**(2,066)**	(1,774)	(3,404)
	66,329	60,302	60,691
Earnings			
Net income	**117,488**	108,310	111,076
Dividends on preferred stock	**9,942**	9,370	10,002
Earnings applicable to common stock	**$107,546**	$ 98,940	$101,074
Common Stock			
Average shares of common stock outstanding (000)	**60,217**	59,377	57,557
Earnings per average share of common stock	**$1.79**	$1.67	$1.76
Dividends declared per share of common stock	**$1.54**	$1.54	$1.54

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Cash Flows

(Dollars in Thousands)	Year Ended December 31, 1995	1994	1993
Cash Flows from Operating Activities			
Net income	**$117,488**	$108,310	$111,076
Adjustments to reconcile net income to net cash provided by operating activities			
Depreciation and amortization	**120,897**	120,803	112,926
Allowance for equity funds used during construction	**(708)**	(3,389)	(5,309)
Investment tax credit adjustments, net	**(2,516)**	(1,898)	(2,515)
Deferred income taxes, net	**15,992**	4,829	(1,171)
Provision for early retirement offer	**—**	17,500	—
Net change in:			
Accounts receivable	**(14,022)**	7,980	(15,851)
Inventories	**18,590**	(21,409)	5,314
Accounts payable	**3,269**	5,811	(3,749)
Other current assets & liabilities(1)	**(14,349)**	(10,668)	11,441
Other, net	**(5,213)**	(3,282)	(5,438)
Net cash provided by operating activities	**239,428**	224,587	206,724
Cash Flows from Investing Activities			
Construction expenditures, excluding AFUDC	**(135,614)**	(154,119)	(159,991)
Allowance for borrowed funds used during construction	**(2,066)**	(1,774)	(3,404)
Change in working capital for construction	**1,102**	(439)	3,123
Acquisition of COPCO, net of cash acquired	**(157,014)**	—	—
Cash flows from leveraged leases			
Sales of interests in leveraged leases	**1,314**	—	21,542
Other	**1,685**	1,592	1,511
Proceeds from sales of subsidiary property	**3,656**	4,596	—
Investment in subsidiary projects and operations	**(3,645)**	(11,045)	(2,827)
Net (increase)/decrease in bond proceeds held in trust funds	**2,658**	(11,816)	1,152
Deposits to nuclear decommissioning trust funds	**(3,612)**	(2,438)	(2,657)
Other, net	**(3,544)**	(2,336)	(389)
Net cash used by investing activities	**(295,080)**	(177,779)	(141,940)
Cash Flows from Financing Activities			
Dividends: Common	**(92,221)**	(91,175)	(87,989)
Preferred	**(9,813)**	(9,464)	(10,042)
Issuances: Long-term debt(2)	**125,800**	4,640	148,200
Variable rate demand bonds	**15,000**	30,000	15,500
Common stock	**24,693**	14,974	109,463
Preferred stock	**—**	—	20,000
Redemptions: Long-term debt(2)	**(1,388)**	(26,096)	(184,206)
Variable rate demand bonds	**—**	—	(15,500)
Common stock	**(1,253)**	(794)	(748)
Preferred stock	**—**	—	(28,280)
Principal portion of capital lease payments	**(7,875)**	(11,280)	(9,956)
Net change in term loan	**(45,000)**	35,000	10,000
Net change in short-term debt	**53,154**	10,000	(17,000)
Cost of issuances and refinancings	**(1,523)**	(601)	(13,097)
Net cash provided/(used) by financing activities	**59,574**	(44,796)	(63,655)
Net change in cash and cash equivalents	**3,922**	2,012	1,129
Beginning of year cash and cash equivalents	**25,029**	23,017	21,888
End of year cash and cash equivalents	**$28,951**	$25,029	$23,017

(1) Other than debt and deferred income taxes classified as current.
(2) Excluding net change in term loan.

See accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

(Dollars in Thousands)	As of December 31, 1995	1994
Assets		
Utility Plant—At Original Cost		
Electric	**$2,942,969**	$2,676,871
Gas	**208,245**	196,188
Common	**130,949**	120,933
	3,282,163	2,993,992
Less: Accumulated depreciation	**1,189,269**	1,062,565
Net utility plant in service	**2,092,894**	1,931,427
Construction work-in-progress	**105,588**	85,220
Leased nuclear fuel, at amortized cost	**31,661**	30,349
	2,230,143	2,046,996
Investments and Nonutility Property		
Investment in leveraged leases	**48,367**	49,595
Funds held by trustee	**36,275**	32,824
Other investments and nonutility property, net	**54,781**	57,289
	139,423	139,708
Current Assets		
Cash and cash equivalents	**28,951**	25,029
Accounts receivable		
Customers	**116,606**	93,739
Other	**14,630**	15,144
Inventories, at average cost		
Fuel (coal, oil, and gas)	**30,076**	48,262
Materials and supplies	**36,823**	37,055
Prepayments	**12,969**	9,014
Deferred income taxes, net	**5,400**	9,276
	245,455	237,519
Deferred Charges and Other Assets		
Prepaid pension cost	**16,899**	5,905
Unamortized debt expense	**12,256**	11,387
Deferred debt refinancing costs	**23,972**	26,530
Deferred recoverable income taxes	**151,250**	149,206
Other	**47,287**	52,534
	251,664	245,562
Total	**$2,866,685**	$2,669,785

See accompanying Notes to Consolidated Financial Statements.

Consolidated Balance Sheets

(Dollars in Thousands)	As of December 31, 1995	1994
Capitalization and Liabilities		
Capitalization (See Statements of Capitalization)		
Common stock, $2.25 par value; 90,000,000 shares authorized; shares outstanding: 1995—60,759,365, 1994—59,542,006	**$136,713**	$133,970
Additional paid-in capital	**506,298**	484,377
Retained earnings	**281,862**	267,002
Unearned compensation	**(1,433)**	(1,180)
Total common stockholders' equity	**923,440**	884,169
Preferred stock	**168,085**	168,085
Long-term debt	**853,904**	774,558
	1,945,429	1,826,812
Current Liabilities		
Short-term debt	**63,154**	10,000
Long-term debt due within one year	**1,485**	1,399
Variable rate demand bonds	**86,500**	71,500
Accounts payable	**64,056**	59,596
Taxes accrued	**4,802**	7,264
Interest accrued	**16,355**	15,459
Dividends declared	**23,426**	22,831
Current capital lease obligation	**12,604**	12,571
Deferred energy costs	**222**	12,241
Other	**33,595**	27,538
	306,199	240,399
Deferred Credits and Other Liabilities		
Deferred income taxes, net	**519,597**	505,435
Deferred investment tax credits	**45,061**	47,577
Long-term capital lease obligation	**20,768**	19,660
Other	**29,631**	29,902
	615,057	602,574
Commitments and Contingencies (Notes 13 and 16)	—	—
Total	**$2,866,685**	$2,669,785

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Capitalization

(Dollars in Thousands)			As of December 31, 1995	1994
Common Stockholders' Equity				
Total common stockholders' equity (1)			**$923,440**	$884,169
Cumulative Preferred Stock				
Par value $1 per share, 10,000,000 shares authorized, none outstanding			**—**	—
Par value $25 per share, 3,000,000 shares authorized, 7 3/4% Series, 1,600,000 shares issued (2)			**40,000**	40,000
Par value $100 per share, 1,800,000 shares authorized:				
Series	Shares outstanding	Current call price per share		
3.70%–5%	320,000	$103.00–$105.00	**32,000**	32,000
6 3/4%	200,000	(3)	**20,000**	20,000
7.52%	150,000	$103.50	**15,000**	15,000
Adjustable—5.56%, 5.54% (4)	160,850	$103.00 (5)	**16,085**	16,085
Auction rate—4.54%, 3.32% (4)	450,000	$100.00	**45,000**	45,000
			168,085	168,085
Long-Term Debt				
First Mortgage Bonds:				
Maturity	Interest Rates			
1997	6 3/8%		**25,000**	25,000
2002–2003	6.40%–6.95%		**120,000**	120,000
2014–2015	7.30%–8.15%		**81,000**	81,000
2018–2022	5.90%–8.50%		**208,200**	208,200
2025	7.71%		**100,000**	—
2032	6.05%		**15,000**	15,000
			549,200	449,200
Amortizing First Mortgage Bonds, due 1997–2008, 6.95%			**25,800**	—
Other Bonds, due 2011–2017, 7.15%–7.50%			**54,500**	54,500
Pollution Control Notes:				
Series 1973, due 1996–1998, 5 3/4%			**6,250**	6,375
Series 1976, due 1996–2006, 7 1/8%–7 1/4%			**3,100**	3,200
Medium Term Notes, due 1998, 5.69%			**25,000**	25,000
Medium Term Notes, due 1999, 7 1/2%			**30,000**	30,000
Medium Term Notes, due 2002–2004, 8.30%–9.29%			**39,000**	39,000
Medium Term Notes, due 2007, 8 1/8%			**50,000**	50,000
Medium Term Notes, due 2020–2021, 8.96%–9.95%			**61,000**	61,000
Mortgage Notes, 9.65% (6)			**6,938**	7,606
Mortgage Note, 8% (7)			**4,279**	4,588
Term Loan (8)			**—**	45,000
Other Obligations, due 1996–2000, 9.63%			**940**	1,126
Unamortized premium and discount, net			**(618)**	(638)
Current maturities of long-term debt			**(1,485)**	(1,399)
Total long-term debt			**853,904**	774,558
Total capitalization			**1,945,429**	1,826,812
Variable Rate Demand Bonds (9)			**86,500**	71,500
Total capitalization with Variable Rate Demand Bonds			**$2,031,929**	$1,898,312

(1) Refer to Consolidated Statements of Changes in Common Stockholders' Equity for additional information.
(2) Redeemable beginning September 30, 2002, at $25 per share.
(3) Redeemable beginning November 1, 2003, at $100 per share.
(4) Average rates during 1995 and 1994, respectively.
(5) Call price changes to $100 per share for redemptions on or after July 1, 1996.
(6) Repaid through monthly payments of principal and interest over 15 years ending November 2002.
(7) Repaid through monthly payments of principal and interest using a 15-year principal amortization, with the unpaid balance due in September 1999.
(8) Refer to Note 12 to the Consolidated Financial Statements for additional information.
(9) Classified under current liabilities as discussed in Note 12 to the Consolidated Financial Statements.

See accompanying Notes to Consolidated Financial Statements.

Consolidated Statements of Changes in Common Stockholders' Equity

(Dollars in Thousands)

	Common Shares Outstanding	Par Value (1)	Additional Paid-in Capital	Retained Earnings	Treasury Stock (2)	Unearned Compen-sation	Total
Balance as of January 1, 1993	54,143,853	$121,824	$374,976	$249,176	—	$(187)	$745,789
Net income				111,076			111,076
Cash dividends declared							
Common stock ($1.54)				(89,792)			(89,792)
Preferred stock				(10,002)			(10,002)
Issuance of common stock							
Public offering	3,300,000	7,425	69,713				77,138
DRIP (3)	1,246,380	2,804	26,519				29,323
Stock options	139,050	313	2,689				3,002
Expenses			(2,627)				(2,627)
Reacquired shares	(31,490)				$(748)		(748)
Shares granted (4)	31,490				748	(748)	—
Amortization of unearned compensation						260	260
Refinancing of preferred stock			(273)	(951)			(1,224)
Balance as of December 31, 1993	58,829,283	132,366	470,997	259,507	—	(675)	862,195
Net income				108,310			108,310
Cash dividends declared							
Common stock ($1.54)				(91,436)			(91,436)
Preferred stock				(9,370)			(9,370)
Issuance of common stock							
DRIP (3)	703,726	1,584	13,199				14,783
Other Issuance	8,997	20	171				191
Reacquired shares	(36,840)				(794)		(794)
Shares granted (4)	36,840				794	(794)	—
Amortization of unearned compensation						289	289
Other			10	(9)			1
Balance as of December 31, 1994	59,542,006	133,970	484,377	267,002	—	(1,180)	884,169
Net income				117,488			117,488
Cash dividends declared							
Common stock ($1.54)				(92,686)			(92,686)
Preferred stock				(9,942)			(9,942)
Issuance of common stock							
DRIP (3)	1,210,048	2,723	21,806				24,529
Stock options	3,900	9	63				72
Other issuance	4,731	11	82				93
Reacquired shares	(63,370)				(1,253)	19	(1,234)
Shares granted (4)	62,050				1,223	(1,223)	—
Amortization of unearned compensation						951	951
Balance as of December 31, 1995	60,759,365	$136,713	$506,328	$281,862	$(30)	$(1,433)	$923,440

(1) The Company's common stock has a par value of $2.25 per share and 90,000,000 shares are authorized.

(2) Treasury Stock, which is recorded at cost, is included in Additional Paid-in Capital on the Consolidated Balance Sheet.

(3) Dividend Reinvestment and Common Share Purchase Plan (DRIP)—As of December 31, 1995, 149,648 shares remained on the registration for issuance through the DRIP. On January 29, 1996, the Company filed with the Securities and Exchange Commission to register an additional 6,000,000 shares for issuance through the DRIP.

(4) Shares of restricted common stock granted under the Company's Long Term Incentive Plan.

See accompanying Notes to Consolidated Financial Statements.

1. Significant Accounting Policies

Nature of Business

The Company is predominately a public utility that provides electric and gas service. The Company provides electric service to retail (residential, commercial, and industrial) and wholesale (resale) customers in Delaware, ten primarily Eastern Shore counties in Maryland, and the Eastern Shore area of Virginia in an area consisting of about 6,000 square miles with a population of approximately 1.1 million. In 1995, 90% of the Company's operating revenues were derived from the sale of electricity. The Company provides gas service to retail and transportation customers in an area consisting of about 275 square miles with a population of approximately 470,000 in northern Delaware, including the City of Wilmington.

In addition, the Company and its wholly-owned subsidiaries are engaged in nonutility activities. The Company is developing and marketing energy-related products and services primarily targeted to customers in retail markets. The subsidiaries' nonutility activities include landfill and wastehauling operations, the operation and maintenance of energy-related projects, real estate sales and development, and investments in leveraged equipment leases.

Regulation of Utility Operations

The Company is subject to regulation with respect to its retail utility sales by the Delaware and Maryland Public Service Commissions (DPSC and MPSC, respectively) and the Virginia State Corporation Commission (VSCC), which have powers over rate matters, accounting, and terms of service. Gas sales are subject to regulation by the DPSC. The Federal Energy Regulatory Commission (FERC) exercises jurisdiction with respect to the Company's accounting systems and policies, the transmission of electricity, the wholesale sale of electricity, and interchange and other purchases and sales of electricity involving other utilities. The FERC also regulates the price and other terms of transportation of natural gas purchased by the Company. The percentage of electric and gas utility operating revenues regulated by each Commission for the year ended December 31, 1995, was as follows: DPSC, 64%; MPSC, 27%; VSCC, 3%; and FERC, 6%.

Refer to Note 8 to the Consolidated Financial Statements for a discussion of regulatory assets arising from the financial effects of rate regulation.

Reporting of Subsidiaries

The consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries—Delmarva Capital Investments, Inc.; Delmarva Energy Company; Delmarva Industries, Inc.; and Delmarva Services Company. The results of operations of the Company's nonutility subsidiaries are reported in the Consolidated Statements of Income as "Other Income." Refer to Note 18 to the Consolidated Financial Statements for financial information about the Company's nonutility subsidiaries.

Use of Estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make certain estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Utility Revenues

At the end of each month, there is an amount of electric and gas service rendered from the last meter reading to the month-end which has not yet been billed to customers. The non-fuel (base rate) revenues associated with such unbilled services are accrued by the Company.

When interim rates are placed in effect subject to refund, the Company recognizes revenues based on expected final rates.

Fuel Expense

Fuel costs charged to the Company's results of operations generally are adjusted to match fuel costs included in customer billings (fuel revenues). The difference between fuel revenues and actual fuel costs incurred is reported on the Consolidated Balance Sheets as "Deferred energy costs." The deferred balance is subsequently recovered from or returned to utility customers.

The Company's share of nuclear fuel at the Peach Bottom Atomic Power Station (Peach Bottom) and the Salem Nuclear Generating Station (Salem) is financed through a contract which is accounted for as a capital lease. Nuclear fuel costs, including a provision for the future disposal of spent nuclear fuel, are charged to fuel expense on a unit-of-production basis.

Depreciation Expense

The annual provision for depreciation on utility property is computed on the straight-line basis using composite rates by classes of depreciable property. The relationship of the annual provision for depreciation for financial accounting purposes to average depreciable property was 3.6% for 1995 and 1994, and 3.7% for 1993. Depreciation expense includes a provision for the Company's share of the estimated cost of decommissioning nuclear power plant reactors based on amounts billed to customers for such costs. Refer to Note 7 to the Consolidated Financial Statements for additional information on nuclear decommissioning.

Interest Expense

The amortization of debt discount, premium, and expense, including refinancing expenses, is included in interest expense.

Allowance for Funds Used During Construction

Allowance for Funds Used During Construction (AFUDC) is included in the cost of utility plant and represents the cost of borrowed and equity funds used to finance construction of new utility facilities. In the Consolidated Statements of Income, the borrowed funds component of AFUDC is reported under "Utility Interest Charges" as a reduction of interest expense and the equity funds component of AFUDC is reported as "Other Income." AFUDC was capitalized on utility plant construction at the rates of 7.1% in 1995, 9.3% in 1994, and 9.6% in 1993.

Cash Equivalents

In the consolidated financial statements, the Company considers highly liquid marketable securities and debt instruments purchased with a maturity of three months or less to be cash equivalents.

Leveraged Leases

As of December 31, 1995, the Company's portfolio of leveraged leases, held by a nonutility subsidiary, consists of five aircraft which are leased to three separate airlines. The Company's investment in leveraged leases includes the aggregate of rentals receivable (net of principal and interest on nonrecourse indebtedness) and estimated residual values of the leased equipment less unearned and deferred income (including investment tax credits). Unearned and deferred income is recognized at a level rate of return during the periods in which the net investment is positive.

Funds Held By Trustee

Funds held by trustee generally include deposits in the Company's external nuclear decommissioning trusts and unexpended, restricted, tax-exempt bond proceeds. Earnings on such trust funds are also reflected in the balance.

2. Base Rate Matters

Electric and gas base rate increases which became effective in 1993, 1994, and 1995 are summarized in the following table.

Jurisdiction	Annualized Base Revenue Increase	Effective Date	Return On Common Equity Allowed
Retail Electric			
Delaware(1)	$ 4.5 million or 0.9%	05/01/95	11.5%
Delaware(2)	$24.9 million or 5.8%	06/01/93	11.5%
Maryland(3)	$ 7.8 million or 4.3%	04/01/93	—
Virginia	$ 1.3 million or 5.4%	10/05/93	11.05%
Resale (FERC)(4)	$ 1.5 million or 1.5%	06/03/93	—
Gas(5)	$ 3.1 million or 3.1%	11/01/94	11.5%

(1) Net of reduced fuel rates, customer rates decreased 1.45%.

(2) Net of fuel savings from Hay Road Unit 4, customer rates increased 3.7%.

(3) Although a return on equity was not specified, the Company believes that the implied return on equity approaches 12%. Net of fuel savings from Hay Road Unit 4, customer rates increased 2.3%.

(4) The settlement agreement did not specify a return on equity.

(5) Net of reduced fuel rates, customer rates decreased 1.75%.

On April 18, 1995, the DPSC approved a joint resolution submitted by the Company and two customer groups for a $4.5 million or 0.9% increase in electric base rates effective May 1, 1995. The rate increase was designed to recover the costs of "limited issues," which primarily are costs imposed by government and are outside the reasonable control of the Company. The joint resolution also provided for the following:

- A rate moratorium whereby the Company will not increase its electric base rates before January 1, 1997. However, the Company is permitted to file for a redesign of electric base rates that would not result in a change in total electric base revenues.

- A provision whereby the Company would be required to submit a proposal supporting current rate levels if its return on common equity exceeds its currently approved rate of 11.5%. A return on common equity test will be performed quarterly beginning with the twelve-month period ended December 31, 1995, and continuing through the twelve-month period ended December 31, 1996.

- Funding of nuclear decommissioning costs at the current Nuclear Regulatory Commission (NRC) minimum financial assurance amount. See Note 7 to the Consolidated Financial Statements for a further discussion of the Company's accounting and funding policies for nuclear decommissioning.

In 1994, the Company also had filed an application with the MPSC for a $3.9 million "limited issues" increase in electric base rates. In April 1995, the MPSC denied the Company's application to increase rates because it was unable to determine the reasonableness of the Company's current base rates due to the "limited issues" format of the case.

The electric base rate increases that became effective in 1993 were designed to recover higher costs associated with completion of Hay Road Unit 4, costs for postretirement benefits other than pensions, and other items, including general inflation.

The gas base rate increase effective in 1994 was designed to recover higher operating costs and plant investment levels than were reflected in the previous rates.

3. Income Taxes

The Company and its wholly-owned subsidiaries file a consolidated federal income tax return. Income taxes are allocated to the Company's utility business and subsidiaries based upon their respective taxable incomes, tax credits, and effects of the alternative minimum tax, if any.

Deferred income tax assets and liabilities represent the tax effects of temporary differences between the financial statement and tax bases of existing assets and liabilities and are measured using presently enacted tax rates. The portion of the Company's deferred tax liability applicable to utility operations that has not been reflected in current customer rates represents income taxes recoverable through future rates and is reflected on the Consolidated Balance Sheets as "Deferred recoverable income taxes." Deferred recoverable income taxes were $151.3 million and $149.2 million as of December 31, 1995 and 1994, respectively.

Deferred income tax expense represents the net change during the reporting period in the net deferred tax liability and deferred recoverable income taxes.

Investment tax credits (ITC) from regulated operations are being amortized over the useful lives of the related utility plant. ITC associated with leveraged leases are being amortized over the lives of the related leases during the periods in which the net investment is positive.

Components of Consolidated Income Tax Expense

(Dollars in Thousands)		**1995**	1994	1993
Operation				
Federal:	Current	**$46,517**	$50,276	$50,264
	Deferred	**16,452**	5,592	7,710
State:	Current	**9,851**	11,268	10,839
	Deferred	**3,257**	928	1,832
Investment tax credit adjustments, net		**(2,516)**	(1,898)	(2,515)
Total Operation		**73,561**	66,166	68,130
Other income				
Federal:	Current	**5,263**	2,789	9,398
	Deferred	**(3,686)**	(2,008)	(9,398)
State:	Current	**433**	349	287
	Deferred	**(31)**	317	(1,315)
Total Other Income		**1,979**	1,447	(1,028)
Total income tax expense		**$75,540**	$67,613	$67,102

Reconciliation of Effective Income Tax Rate

The amount computed by multiplying income before tax by the federal statutory rate is reconciled below to the total income tax expense.

	1995		1994		1993	
(Dollars in Thousands)	**Amount**	**Rate**	Amount	Rate	Amount	Rate
Statutory federal income tax expense	**$67,560**	**35%**	$61,574	35%	$62,362	35%
Increase (decrease) due to						
State income taxes, net of federal tax benefit	**8,792**	**5**	8,361	4	7,567	4
Other, net	**(812)**	**(1)**	(2,322)	(1)	(2,827)	(1)
Total income tax expense	**$75,540**	**39%**	$67,613	38%	$67,102	38%

Components of Deferred Income Taxes

The tax effect of temporary differences that give rise to the Company's net deferred tax liability are shown below.

	As of December 31	
(Dollars in Thousands)	**1995**	1994
Deferred Tax Liabilities		
Utility plant basis differences		
Accelerated depreciation	**$307,346**	$296,651
Other	**99,941**	98,437
Leveraged leases	**44,662**	47,080
Deferred recoverable income taxes	**64,376**	64,130
Other	**54,507**	44,418
Total deferred tax liabilities	**570,832**	550,716
Deferred Tax Assets		
Deferred ITC	**15,719**	17,763
Other	**40,916**	36,794
Total deferred tax assets	**56,635**	54,557
Total deferred taxes, net	**$514,197**	$496,159

Valuation allowances for deferred tax assets were not material as of December 31, 1995 and 1994.

4. Purchase of Conowingo Power Company

On June 19, 1995, the Company acquired Conowingo Power Company (COPCO), the Maryland retail electric subsidiary of PECO Energy Company (PECO), for $158.2 million ($157.0 million net of cash acquired). As disclosed in Note 12 to the Consolidated Financial Statements, the Company financed the acquisition with $125.8 million of long-term debt and the balance with short-term debt. The acquisition resulted in approximately 37,500 new electric retail customers, which represents 9% of the Company's current customer base.

The acquisition has been accounted for as a purchase. Immediately after the acquisition, COPCO was merged into the Company and is now being operated as the Conowingo District. Operating results of the Conowingo District have been included in the Consolidated Statements of Income since June 19, 1995. Pro forma results of the Company, assuming the acquisition had taken place at the beginning of each period presented, would not be materially different from the results reported.

Under FERC accounting requirements, the COPCO assets have been recorded at their net book value, reflecting electric plant of $107.8 million and related accumulated depreciation of $31.7 million and other net assets and liabilities of $7.9 million. The difference between the amount paid to PECO plus acquisition costs and the net book value of the COPCO assets, or $75.8 million, has been recorded as goodwill and is included in electric utility plant. The MPSC has approved recovery of this goodwill using a sinking fund method through Maryland retail rates in two components. Approximately $50 million of the goodwill will be recovered as an acquisition adjustment with a carrying charge over 20 years beginning at the time of the Company's next Maryland base rate case. The remaining $26 million will be recovered with a carrying charge over approximately 10 years via a pre-approved surcharge to the Company's existing Maryland retail rates. This surcharge was placed in effect for Conowingo District customers on February 1, 1996. For financial statement purposes, the goodwill is being amortized on a straight-line basis over 40 years beginning July 1995.

In conjunction with the acquisition, the Company signed a contract with PECO to purchase electric capacity and energy from the PECO system beginning February 1, 1996, and ending May 31, 2006. The base amount of the capacity purchase, which is subject to certain possible adjustments, will start at 205 megawatts (MW) and will increase annually to 279 MW in 2006. Under another contract, the Company agreed to purchase the Conowingo District's interim electric power requirements from PECO from the acquisition date until February 1, 1996.

5. Early Retirement Offer

In the third quarter of 1994, the Company completed a voluntary early retirement offer (ERO) for all management and union employees at least 55 years old with at least 10 years of continuous service by December 31, 1994. The ERO was accepted by 10.5% of the Company's workforce (296 people), which represented an 82% participation rate among eligible employees. In accordance with Statement of Financial Accounting Standards (SFAS) No. 88, "Employers' Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits," the Company expensed $17.5 million of costs associated with the ERO ($10.7 million after taxes or $0.18 per share).

6. Jointly Owned Plant

The Company's Consolidated Balance Sheets include its proportionate share of assets and liabilities related to jointly owned plant. The Company's share of operating and maintenance expenses of the jointly owned plant is included in the corresponding expenses in the Consolidated Statements of Income. The Company is responsible for providing its share of financing for the jointly owned facilities. Information with respect to the Company's share of jointly owned plant as of December 31, 1995 was as follows:

(Dollars in Thousands)	Ownership Share	Megawatt Capability Owned	Plant in Service	Accumulated Depreciation	Construction Work in Progress
Nuclear					
Peach Bottom	7.51%	164 MW	$129,028	$69,134	$9,595
Salem	7.41%	164 MW	210,458	93,728	10,103
Coal-Fired					
Keystone	3.70%	63 MW	19,244	7,506	339
Conemaugh	3.72%	63 MW	32,406	8,543	520
Transmission Facilities	Various		4,564	2,103	—
Other Facilities	Various		1,721	128	797
Total			$397,421	$181,142	$21,354

7. Nuclear Decommissioning

The Company records a liability for its share of the estimated cost of decommissioning the Peach Bottom and Salem nuclear reactors over the remaining lives of the plants based on amounts collected in rates charged to electric customers. For utility rate-setting purposes, the Company estimates its share of future nuclear decommissioning costs based on NRC regulations concerning the minimum financial assurance amount for nuclear decommissioning. The Company is presently recovering, through electric rates in the Delaware and Virginia jurisdictions, nuclear decommissioning costs based on the current NRC minimum financial assurance amount of approximately $122 million. In the Maryland and FERC jurisdictions, the Company is presently recovering nuclear decommissioning costs based on the 1990 NRC minimum financial assurance amount of approximately $50 million.

The Company's accrued nuclear decommissioning liability, which is reflected in the accumulated reserve for depreciation, was $37.2 million as of December 31, 1995. The provision reflected in depreciation expense for nuclear decommissioning was $3.6 million in 1995, $2.4 million in 1994, and $2.3 million in 1993. External trust funds established by the Company for the purpose of funding nuclear decommissioning costs had an aggregate balance of $25.5 million as of December 31, 1995. Earnings on the trust funds are recorded as an increase to the accrued nuclear decommissioning liability, which, in effect, reduces the expense recorded for nuclear decommissioning.

The ultimate cost of nuclear decommissioning for the Peach Bottom and Salem reactors may exceed the NRC minimum financial assurance amount, which is updated annually under a NRC prescribed formula.

8. Regulatory Assets

In conformity with generally accepted accounting principles, the Company's accounting policies reflect the financial effects of rate regulation and decisions issued by regulatory commissions having jurisdiction over the Company's utility business. In accordance with the provisions of SFAS No. 71, "Accounting for the Effects of Certain Types of Regulation," the Company defers expense recognition of certain costs and records an asset, a result of the effects of rate regulation. These "regulatory assets" are included on the Company's Consolidated Balance Sheets under "Deferred Charges and Other Assets." As of December 31, 1995, the Company had $207.0 million of regulatory assets, which included the following: Deferred debt refinancing costs—$24.0 million; Deferred recoverable income taxes—$151.3 million (refer to Note 3 to the Consolidated Financial Statements); Deferred recoverable plant costs—$9.8 million; Deferred costs for decontamination and decommissioning of United States Department of Energy gaseous diffusion enrichment facilities—$7.2 million; Deferred demand-side management costs—$5.4 million; and other regulatory assets —$9.3 million. The costs of these assets are either being recovered or are probable of being recovered through customer rates. Generally, the costs of these assets are recognized in operating expenses over the period the cost is recovered from customers.

In March 1995, the FASB issued SFAS No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to Be Disposed Of," which requires the Company to review long-lived assets and certain identifiable intangibles held and used by the Company for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If an asset is considered impaired, then its value would be written down with a corresponding charge to earnings. SFAS No. 121 also requires rate-regulated companies to write off regulatory assets against earnings whenever those assets no longer meet the criteria for recognition of a regulatory asset as defined by SFAS No. 71. The new standard is effective in 1996. Based on current circumstances, the Company does not expect the adoption of SFAS No. 121 to have a material effect upon the Company's financial condition or results of operations.

9. Investments

As of December 31, 1995, the Company had $39.6 million of investments in securities which were included in the following balance sheet classifications: Funds held by trustee—$36.3 million; Other investments and nonutility property, net—$1.6 million; Cash and cash equivalents—$1.7 million. These securities, based on the Company's intent and criteria established by SFAS No. 115, "Accounting for Certain Investments in Debt and Equity Securities," are categorized as available-for-sale securities. The fair value of such securities was not materially different from book value as of December 31, 1995. Gains and losses from the sale of investment securities were not material to the Company's operating results in 1995, 1994, and 1993. As of December 31, 1995, the Company's investments in debt securities, other than those considered to be cash equivalents, had the following maturities: $2.4 million due in 1996; $9.3 million due in 1997–2000; and $8.7 million due in 2001–2005.

10. Common Stock

Refer to the Consolidated Statements of Changes in Common Stockholders' Equity for information concerning issuances and redemptions of common stock during 1993–1995.

The Company's Restated Certificate and Articles of Incorporation and the Mortgage and Deed of Trust collateralizing the Company's outstanding First Mortgage Bonds contain restrictions on the payment of dividends on common stock. Such restrictions would become applicable if the Company's capital and retained earnings fall below certain specific levels or if preferred dividends are in arrears. Under the most restrictive of these provisions, as of December 31, 1995, approximately $246.2 million was available for payment of common dividends.

Prior to January 1, 1993, the Company had a nonqualified stock option plan for certain employees. Options were priced at the actual market value on the grant date. Effective January 1, 1993, the Company's Board of Directors declared that no new stock options will be granted and that the performance-based restricted stock program will be the program in effect under the Long Term Incentive Plan. Changes in stock options are summarized below.

	1995		1994		1993	
	Number of Shares	**Option Price**	Number of Shares	Option Price	Number of Shares	Option Price
Beginning-of-year balance	**53,050**	**$17½–$21¼**	53,050	$17½–$21¼	192,100	$17½–$21¼
Options exercised	**3,900**	**$17½–$18⅛**	—	—	139,050	$17½–$21¼
Options forfeited	**2,800**	**$20½–$21¼**	—	—	—	—
End-of-year balance	**46,350**	**$17½–$21¼**	53,050	$17½–$21¼	53,050	$17½–$21¼
Exercisable	**46,350**	**$17½–$21¼**	53,050	$17½–$21¼	53,050	$17½–$21¼

In October 1995, the FASB issued SFAS No. 123, "Accounting for Stock-Based Compensation," which encourages, but does not require, entities to recognize compensation costs for stock-based employee compensation plans using a fair value based method of accounting rather than the intrinsic value based method of accounting currently prescribed by Accounting Principles Board (APB) Opinion No. 25, "Accounting for Stock Issued to Employees." Entities electing to continue using the accounting prescribed by APB Opinion No. 25 are required to disclose pro forma net income and earnings per share as if the fair value based method of accounting under SFAS No. 123 had been applied. The new standard is effective in 1996. The Company does not expect to adopt the accounting provisions of SFAS No. 123 for income statement recognition purposes.

11. Preferred Stock

On November 4, 1993, the Company issued 200,000 shares of 6 3/4%, cumulative preferred stock, $100 per share par value, for $20 million. On December 1, 1993, the Company used the proceeds and cash on-hand to redeem $18.28 million of its 7.88% series and $10.0 million of its 7.84% series preferred stock.

12. Debt

Substantially all utility plant of the Company is subject to the lien of the Mortgage and Deed of Trust collateralizing the Company's First Mortgage Bonds.

On June 19, 1995, the Company issued the following debt to finance the $158.2 million acquisition of COPCO: $100 million of First Mortgage Bonds, Series I, 7.71% Bonds Due June 1, 2025; $25.8 million of First Mortgage Bonds, Series I, 6.95% Amortizing Bonds Due June 1, 2008, with principal repayable in annual installments beginning June 1, 1997; and the balance with short-term debt.

On August 30, 1995, the Schuylkill County Industrial Development Authority, Commonwealth of Pennsylvania, issued on behalf of a nonutility subsidiary of the Company, $15 million of Variable Rate Demand Revenue Bonds due on demand or at maturity on October 1, 2019. Proceeds from the bonds are being used to finance the past and future expansion of a landfill which is owned and operated by the subsidiary.

The Company's debt obligations included Variable Rate Demand Bonds (VRDB) in the amounts of $86.5 million as of December 31, 1995, and $71.5 million as of December 31, 1994. Although VRDB are classified as current liabilities because VRDB are due on demand by the bondholder, such bonds are immediately remarketed because the interest rate is set at market. The Company may also utilize one of the fixed rate/fixed term conversion options of the bonds. Thus, the Company considers the VRDB to be a source of long-term financing. The $86.5 million balance of VRDB outstanding as of December 31, 1995, matures in 2017 ($26 million), 2019 ($15 million), 2028 ($15.5 million), and 2029 ($30 million). Average annual interest rates on the VRDB were 4.0% in 1995.

As of December 31, 1995, the Company had $150 million of bank lines of credit, including $130 million of such credit lines under which the Company may convert short-term borrowings to a term loan with a maturity date of 12 to 24 months following the date of the requested conversion. As of December 31, 1994, the Company had reclassified $45 million of short-term debt as long-term debt ("Term Loan") in recognition of the expected refinancing on a long-term basis and long-term financing capability provided by the credit lines. During 1995, this short-term debt was repaid resulting in no term loan balance as of December 31, 1995. The Company generally is required to pay commitment fees for its credit lines. The lines of credit are periodically reviewed by the Company, at which time they may be renewed or canceled.

Maturities of long-term debt and sinking fund requirements during the next five years are as follows: 1996—$3.2 million; 1997—$29.0 million; 1998—$35.0 million; 1999—$37.4 million; 2000—$4.2 million.

As of December 31, 1995, the fair market value of the Company's long-term debt was $936.5 million in comparison to the book value of $853.9 million. As of December 31, 1994, the fair market value of the Company's long-term debt was $752.5 million in comparison to the book value of $774.6 million. The fair market value of the Company's long-term debt was based on quoted market prices of the Company's securities or securities with similar characteristics.

13. Commitments

The Company currently estimates its expenditures for construction of utility plant, excluding AFUDC, and commitments for purchases under fuel supply contracts, excluding nuclear fuel, to be approximately $223 million in 1996 and $236 million in 1997.

The Company has a 26-year agreement with Star Enterprise, effective through May 2018, to purchase 48 MW of capacity supplied by the Delaware City Power Plant. As discussed in Note 4 to the Consolidated Financial Statements, the Company also has agreements to purchase capacity and energy from PECO effective June 19, 1995, through May 31, 2006. Under the terms of these agreements, the Company's expected commitments for capacity and energy charges are as follows: 1996—$57.6 million; 1997—$58.6 million; 1998—$63.6 million; 1999—$70.9 million; 2000—$77.3 million; after 2000—$505.5 million; total—$833.5 million.

The Company's share of nuclear fuel at Peach Bottom and Salem is financed through a nuclear fuel energy contract which is accounted for as a capital lease. Payments under the contract are based on the quantity of nuclear fuel burned by the plants. The Company's obligation under the contract generally is the net book value of the nuclear fuel financed, which was $31.7 million as of December 31, 1995.

The Company leases an 11.9% interest in the Merrill Creek Reservoir. The lease is considered an operating lease and payments over the remaining lease term, which ends in 2032, are $158.1 million in aggregate. The Company also has long-term leases for certain other facilities and equipment. Minimum commitments as of December 31, 1995, under the Merrill Creek Reservoir lease and all other noncancelable lease agreements (excluding payments under the nuclear fuel energy contract which cannot be reasonably estimated) are as follows: 1996—$6.1 million; 1997—$6.1 million; 1998—$6.1 million; 1999—$6.0 million; 2000—$4.1 million, after 2000—$140.9 million; total—$169.3 million. Approximately 93% of the minimum lease commitments shown above are payments due under the Merrill Creek Reservoir lease.

Rentals Charged to Operating Expenses

The following amounts were charged to operating expenses for rental payments under both capital and operating leases:

(Dollars in Thousands)	**1995**	1994	1993
Interest on capital leases	**$1,773**	$1,560	$1,296
Amortization of capital leases	**8,044**	11,456	10,243
Operating leases	**13,619**	14,552	15,176
	$23,436	$27,568	$26,715

14. Pension Plan

The Company has a defined benefit pension plan covering all regular employees. The benefits are based on years of service and the employee's compensation. The Company's funding policy is to contribute each year the net periodic pension cost for that year. However, the contribution for any year will not be less than the minimum required contribution nor greater than the maximum tax deductible contribution. Pension plan assets consist primarily of equity securities, fixed income securities, and cash equivalents.

The following schedules show the funded status of the plan, the components of pension cost, and assumptions.

Reconciliation of Funded Status of the Plan

(Dollars in Thousands)	As of December 31, 1995	1994
Accumulated benefit obligation		
Vested	**$338,485**	$265,597
Nonvested	**26,024**	19,311
	364,509	284,908
Effect of estimated future compensation increases	**109,706**	67,947
Projected benefit obligation	**474,215**	352,855
Plan assets at fair value	**616,600**	502,588
Excess of plan assets over projected benefit obligation	**142,385**	149,733
Unrecognized prior service cost	**29,191**	19,155
Unrecognized net gain	**(124,850)**	(129,842)
Unrecognized net transition asset	**(29,827)**	(33,141)
Prepaid pension cost	**$16,899**	$5,905

Components of Net Pension Cost

(Dollars in Thousands)	Year ended December 31, 1995	1994	1993
Service cost—benefits earned during period	**$9,719**	$10,939	$13,152
Interest cost on projected benefit obligation	**30,654**	26,574	26,411
Actual return on plan assets	**(135,850)**	3,349	(58,247)
Net amortization and deferral	**83,981**	(52,601)	14,748
Net pension cost	**$(11,496)**	$(11,739)	$(3,936)

Assumptions	1995	1994	1993
Discount rates used to determine projected benefit obligation as of December 31	**7.00%**	8.25%	7.25%
Rates of increase in compensation levels	**5.00%**	5.50%	6.50%
Expected long-term rates of return on assets	**9.00%**	8.25%	8.25%

The net pension cost excludes the expense recorded in 1994 under SFAS No. 88 for the Company's ERO. Prepaid pension cost as of December 31, 1994, was reduced by the ERO. Refer to Note 5 to the Consolidated Financial Statements for additional information on the ERO.

The net 1994 pension cost reflects a decrease of $4.5 million attributed to a reduction in the assumed rate of increase in compensation levels from 6.5% to 5.5%, effective January 1, 1994. Also, the discount rate was increased from 7.25% to 8.25%, effective October 1, 1994.

15. Postretirement Benefits Other Than Pensions

The Company provides health-care and life insurance benefits to its retired employees and substantially all of the Company's employees may become eligible for these benefits upon retirement. The Company's policy is to fund its obligation to the extent that costs are reflected in customer rates, including amounts which are capitalized. Plan assets held in external trust funds consist primarily of investments in domestic equity securities and fixed income securities.

The following schedules show the funded status of the plan, the components of the cost of postretirement benefits other than pensions, and assumptions.

Reconciliation of Funded Status of the Plan

(Dollars in thousands)	As of December 31, 1995	1994
Accumulated postretirement benefit obligation (APBO)		
Active employees fully eligible for benefits	**$6,019**	$9,319
Other active employees	**23,990**	12,638
Current retirees	**63,629**	58,445
	93,638	80,402
Plan assets at fair value	**24,900**	15,140
APBO in excess of plan assets	**68,738**	65,262
Unrecognized prior service cost	**(423)**	—
Unrecognized net loss	**(5,212)**	(256)
Unrecognized transition obligation	**(61,493)**	(65,110)
Accrued/(prepaid) postretirement benefit cost	**$1,610**	$(104)

Annual Cost of Postretirement Benefits Other Than Pensions

(Dollars in thousands)	Year ended December 31, 1995	1994	1993
Service cost—benefits earned during period	**$2,152**	$2,127	$2,206
Interest cost on projected benefit obligation	**6,601**	5,520	5,613
Actual return on plan assets	**(1,008)**	100	—
Amortization of the unrecognized transition obligation	**3,617**	3,617	3,617
Other, net	**149**	(481)	—
Net postretirement benefit cost	**$11,511**	$10,883	$11,436

Assumptions	**1995**	1994	1993
Discount rates used to determine APBO as of December 31	**7.00%**	8.25%	7.25%
Rates of increase in compensation levels	**5.00%**	5.50%	6.50%
Expected long-term rates of return on assets	**9.00%**	8.25%	8.25%
Health-care cost trend rate	**10.50%**	11.00%	12.00%

The health-care cost trend rate, or the expected rate of increase in health-care costs, is assumed to decrease to 10.0% in 1996 and gradually decrease to 5.5% by 2005. Increasing the health-care cost trend rates of future years by one percentage point would increase the accumulated postretirement benefit obligation by $4.4 million and would increase annual aggregate service and interest costs by $0.3 million.

16. Contingencies

Salem Outage

The Company owns 7.41% of Salem, which consists of two pressurized water nuclear reactors (PWR) and is operated by Public Service Electric & Gas Company (PSE&G). As of December 31, 1995, the Company's net investment in plant in-service for Salem was approximately $57 million for Unit 1 and $60 million for Unit 2. Each unit represents approximately 2% of the Company's total assets and approximately 3% of the Company's installed electric generating capacity.

Salem Units 1 and 2 were removed from operation by PSE&G on May 16, 1995, and June 7, 1995, respectively, due to operational problems and maintenance concerns. The units will remain shut down until PSE&G makes the equipment and management changes necessary to operate the units reliably over the long term. The restart of the units is subject to NRC authorization. In December 1995, PSE&G completed a workscope assessment of both units and estimated that Unit 1 would return to service in the second quarter of 1996 and Unit 2 in the third quarter of 1996.

On February 21, 1996, PSE&G informed the Company that partial results from recent inspections of Unit 1 using a new testing technology revealed indications of degradation in a significant number of steam generator tubes. PSE&G is continuing its inspections and also will conduct further laboratory analysis of the tubes with results expected in April 1996. Based on the results of inspections to date, PSE&G has concluded that the Unit 1 outage will be extended for an indefinite period to evaluate the state of the steam generators and to subsequently determine an appropriate course of action. Degradation of steam generators in PWRs has become of increasing concern for the nuclear industry. Nationally and internationally, utilities have undertaken actions to repair or replace steam generators. In the extreme, degradation of steam generators has contributed to the retirement of several American nuclear power reactors.

PSE&G also has informed the Company that recent steam generator inspections of Unit 2 using the new testing technology have revealed that the condition of the Unit 2 steam generators is within current repair limits at the present time. However, to confirm the Unit 2 test results, PSE&G also will conduct laboratory analysis of the tubes for Unit 2. As a result of the delay in the restart of Unit 1, PSE&G is focusing its efforts on the return of Unit 2 to service in the third quarter of 1996, as scheduled. However, the Company cannot predict when the NRC will approve the restart of the unit or when the restart actually will occur.

In 1995, the Company incurred higher than expected operation and maintenance costs at Salem of approximately $5 million, which reflect the operational problems at the plant. These costs were expensed as incurred. Also, outage-related replacement power costs were estimated to be approximately $8 million. One-half of the estimated replacement power costs was expensed and the other one-half was deferred on the Company's Consolidated Balance Sheet in expectation of future recovery. Based on PSE&G's current estimates, the Company estimates that its share of additional costs related to the outage in 1996 will consist of operation and maintenance costs ranging from $4 million to $7 million, which will be expensed as incurred, and replacement power costs while the units are out of service of approximately $750,000 per month, per unit. In total, the Company estimates that its share of outage-related costs in 1996 will range from $17 million to $22 million. However, these 1996 estimates could change as a result of PSE&G's analysis of the degradation of the steam generator tubes. Beyond 1996, the Company cannot predict the amount of outage-related costs it could incur. During 1996, the Company plans to file a proposal with the DPSC, the Company's primary rate jurisdiction, for recovery of replacement power costs.

Since the periods during which these units will be out of service, the extent of the maintenance that will be required, and the costs of replacement power and the extent of its recovery may be different from those currently anticipated, the actual costs to be incurred by the Company may vary from the foregoing estimates.

Environmental Matters

The Company is subject to regulation with respect to the environmental effects of its operations, including air and water quality control, solid and hazardous waste disposal, and limitation on land use by various federal, regional, state, and local authorities. The Company has incurred, and expects to continue to incur, capital expenditures and operating costs because of environmental considerations and requirements. The disposal of Company-generated hazardous substances can result in costs to clean up facilities found to be contaminated due to past disposal practices. Federal and state statutes authorize governmental agencies to compel responsible parties to clean up certain abandoned or uncontrolled hazardous waste sites. The Company is currently a potentially responsible party (PRP) at three federal superfund sites and is alleged to be a third-party contributor at two other federal superfund sites. The Company also has two former coal gasification sites in Delaware and one former coal gasification site in Maryland, each of which is a state superfund site. The Company is currently participating with the States of Delaware and Maryland in evaluating the coal gasification sites to assess the extent of contamination and risk to the environment. The Company has accrued a liability of $2 million for clean-up and other potential costs related to the federal and state superfund sites. The Company does not expect such future costs to have a material effect on the Company's financial position or results of operations.

Nuclear Insurance

In the event of an incident at any commercial nuclear power plant in the United States, the Company could be assessed for a portion of any third-party claims associated with the incident. Under the provisions of the Price Anderson Act, if third party claims relating to such an incident exceed $200 million (the amount of primary insurance), the Company could be assessed up to $23.7 million for such third-party claims. In addition, Congress could impose a revenue-raising measure on the nuclear industry to pay such claims.

The co-owners of Peach Bottom and Salem maintain property insurance coverage in the aggregate amount of $2.8 billion for each unit for loss or damage to the units, including coverage for decontamination expense and premature decommissioning. The Company is self-insured, to the extent of its ownership interest, for its share of property losses in excess of insurance coverages. Under the terms of the various insurance agreements, the Company could be assessed up to $5.4 million in any policy year for losses incurred at nuclear plants insured by the insurance companies.

The Company is a member of an industry mutual insurance company, which provides replacement power cost coverage in the event of a major accidental outage at a nuclear power plant. The premium for this coverage is subject to retrospective assessment for adverse loss experience. The Company's present maximum share of any assessment is $1.4 million per year.

Other

The Company is involved in certain legal and administrative proceedings before various courts and governmental agencies concerning rates, fuel contracts, tax filings, and other matters. The Company expects that the ultimate disposition of these proceedings will not have a material effect on the Company's financial position or results of operations.

17. Supplemental Cash Flow Information

Cash Paid during the Year for	Year Ended December 31,		
(Dollars In Thousands)	**1995**	1994	1993
Interest, net of capitalized amount	**$62,660**	$57,837	$58,154
Income taxes, net of refunds	**$66,764**	$67,922	$72,384

18. Nonutility Subsidiaries

The following presents condensed financial information of the Company's nonregulated wholly-owned subsidiaries: Delmarva Capital Investments, Inc.; Delmarva Energy Company; and Delmarva Industries, Inc. A subsidiary that leases real estate to the Company's utility business, Delmarva Services Company, is excluded from these statements since its income is derived from intercompany transactions which are eliminated in consolidation.

Condensed Subsidiary Statements of Income

(Dollars In Thousands)

	1995	1994	1993
Revenues and Gains			
Landfill and waste hauling	**$13,505**	$14,186	$11,745
Operating services	**26,564**	22,468	22,118
Real estate	**5,820**	4,450	1,677
Leveraged leases	**1,772**	272	835
Other revenue	**4,381**	1,766	1,261
	52,042	43,142	37,636
Costs and Expenses			
Operating expenses	**45,594**	38,499	36,424
Interest expense, net	**492**	370	—
Income tax expense (benefit)	**1,810**	1,921	(596)
	47,896	40,790	35,828
Net income	**$4,146**	$2,352	$1,808
Earnings per share of common stock attributed to subsidiaries	**$0.07**	$0.04	$0.03

Condensed Subsidiary Balance Sheets

(Dollars In Thousands)

Assets	As of December 31, **1995**	1994
Current assets		
Cash and cash equivalents	**$19,483**	$8,631
Other	**6,633**	5,702
	26,116	14,333
Noncurrent assets		
Investment in		
Leveraged leases	**48,367**	49,595
Other	**9,925**	4,354
Landfill & waste hauling property, plant & equipment	**24,177**	25,424
Other	**9,778**	9,558
	92,247	88,931
Total	**$118,363**	$103,264

Liabilities and Stockholder's Equity	As of December 31, **1995**	1994
Current liabilities		
Debt due within one year	**$506**	$489
Variable rate demand bonds	**15,000**	—
Other	**7,801**	6,873
	23,307	7,362
Noncurrent liabilities		
Long-term debt	**4,713**	5,225
Deferred income taxes	**50,064**	53,592
Other	**2,389**	2,342
	57,166	61,159
Stockholder's Equity	**37,890**	34,743
Total	**$118,363**	$103,264

19. Segment Information

Segment information with respect to electric and gas operations was as follows:

(Dollars In Thousands)	**1995**	1994	1993
Electric Operations			
Operating revenues	**$899,662**	$883,115	$875,663
Operating income	**165,914**	153,409	154,412
Depreciation	**105,780**	102,746	94,549
Construction expenditures	**118,655**	133,884	142,238
Gas Operations			
Operating revenues	**95,441**	107,906	94,944
Operating income	**12,492**	9,747	9,727
Depreciation	**7,242**	6,777	6,380
Construction expenditures	**16,959**	20,235	17,753
Identifiable Assets, Net			
Electric	**2,493,797**	2,314,448	2,267,050
Gas	**189,339**	188,813	160,618
Assets not allocated	**183,549**	166,524	164,811

20. Quarterly Financial Information (Unaudited)

The quarterly data presented below reflect all adjustments, consisting of normal recurring accruals and unusual items as noted below, necessary in the opinion of the Company for a fair presentation of the interim results. Quarterly data normally vary seasonally because of temperature variations, differences between summer and winter rates, the timing of rate orders, and the scheduled downtime and maintenance of electric generating units.

Quarter Ended	Operating Revenue	Operating Income (Dollars in Thousands)	Net Income	Earnings Applicable to Common Stock	Average Shares Outstanding (In Thousands)	Earnings per Average Share
1995						
March 31	$257,600	$48,252	$35,408	$32,889	59,738	$0.55
June 30	213,228	34,178	19,444	16,962	60,109	0.28
September 30	283,065	60,960	42,714	40,238	60,372	0.67
December 31	241,210	35,016	19,922	17,457	60,651	0.29
	$995,103	$178,406	$117,488	$107,546	60,217	$1.79
1994						
March 31	$292,394	$53,770	$39,641	$37,377	59,022	$0.63
June 30	218,465	33,994	20,776	18,453	59,402	0.31
September 30	260,601	42,921	29,366	27,008	59,542	0.46
December 31	219,561	32,471	18,527	16,102	59,542	0.27
	$991,021	$163,156	$108,310	$98,940	59,377	$1.67

In the third quarter of 1994, the Company expensed the costs associated with the ERO (Note 5 to the Consolidated Financial Statements), which decreased net income by $10.7 million ($0.18 per share).

In the fourth quarter of 1994, the Company reduced the rate of salary increase assumed for computation of pension cost, effective January 1, 1994, which increased net income by $2.1 million ($0.03 per share).

Consolidated Statistics

		1995	1994	1993	1992	1991
Electric Revenues						
(Thousands)	Residential	**$344,351**	$312,224	$305,446	$273,463	$275,888
	Commercial	**267,239**	242,506	237,785	220,659	218,558
	Industrial	**155,108**	145,594	150,178	144,094	144,272
	Resale	**58,680**	105,350	104,983	96,491	98,785
	Other sales revenues(1)	**14,211**	6,816	9,716	7,142	5,961
	Sales revenues	**839,589**	812,490	808,108	741,849	743,464
	Interchange deliveries	**47,271**	62,388	61,437	30,606	33,523
	Miscellaneous revenues	**12,802**	8,237	6,118	7,720	7,612
	Total electric revenues	**$899,662**	$883,115	$875,663	$780,175	$784,599
Electric Sales						
(1,000 Kilowatt-Hours)	Residential	**3,829,807**	3,578,743	3,499,387	3,228,237	3,236,616
	Commercial	**3,744,879**	3,461,058	3,336,847	3,140,149	3,098,599
	Industrial	**3,351,834**	3,248,131	3,232,233	3,115,677	3,105,338
	Resale	**1,213,459**	2,166,154	2,131,920	1,987,393	1,952,312
	Other sales(2)	**170,942**	50,996	79,843	49,355	67,415
	Total electric sales	**12,310,921**	12,505,082	12,280,230	11,520,811	11,460,280
Electric Customers						
(End of Period)	Residential	**386,948**	347,997	342,710	336,076	330,632
	Commercial	**48,345**	44,060	43,324	42,427	41,539
	Industrial	**704**	699	715	726	753
	Resale	**12**	12	12	12	12
	Other	**641**	604	593	578	566
	Total electric customers	**436,650**	393,372	387,354	379,819	373,502
Gas Revenues						
(Thousands)	Residential	**$47,135**	$55,091	$47,022	$43,147	$35,636
	Commercial	**24,458**	28,088	23,065	20,175	16,370
	Industrial	**14,588**	17,589	17,586	15,365	14,395
	Interruptible and other(1)	**6,969**	5,498	6,274	3,775	3,746
	Gas transported	**1,870**	1,191	561	1,032	710
	Miscellaneous revenues	**421**	449	436	375	365
	Total gas revenues	**$95,441**	$107,906	$94,944	$83,869	$71,222
Gas Sales and						
Gas Transported	Residential	**7,328**	7,717	7,311	7,264	6,410
(Million Cubic Feet)	Commercial	**4,809**	4,746	4,423	4,286	3,653
	Industrial	**3,935**	3,858	4,348	4,358	4,398
	Interruptible and other(2)	**2,406**	1,766	1,984	1,105	1,113
	Total gas sales	**18,478**	18,087	18,066	17,013	15,574
	Gas transported	**2,893**	2,255	1,539	3,155	2,610
	Total gas sales and gas transported	**21,371**	20,342	19,605	20,168	18,184
Gas Customers						
(End of Period)	Residential	**90,890**	88,518	86,027	82,996	80,874
	Commercial	**7,369**	6,982	6,751	6,500	6,313
	Industrial	**146**	150	150	152	154
	Interruptible and other	**12**	12	12	11	10
	Total gas customers	**98,417**	95,662	92,940	89,659	87,351

(1) Includes unbilled revenues.
(2) Includes unbilled sales.

Quarterly Common Stock Dividend and Price Ranges

The Company's common stock is listed on the New York and Philadelphia Stock Exchanges and has unlisted trading privileges on the Cincinnati, Midwest and Pacific Stock Exchanges.

The Company had 56,646 holders of common stock as of December 31, 1995.

	Dividend	Price	
1995	Declared	High	Low
First Quarter	**$.38 1/2**	**$20**	**$17 7/8**
Second Quarter	**$.38 1/2**	**$21 1/4**	**$19 1/8**
Third Quarter	**$.38 1/2**	**$23**	**$19 1/2**
Fourth Quarter	**$.38 1/2**	**$23 5/8**	**$21 7/8**

	Dividend	Price	
1994	Declared	High	Low
First Quarter	$.38 1/2	$23 5/8	$20 1/2
Second Quarter	$.38 1/2	$21	$16 7/8
Third Quarter	$.38 1/2	$20	$17 3/4
Fourth Quarter	$.38 1/2	$19 1/4	$17 5/8

Shareholder Services

Carol C. Conrad, Assistant Secretary
Delmarva Power & Light Company
800 King Street, P.O. Box 231
Wilmington, Delaware 19899

or

Wilmington Trust Company
Corporate Trust Operations
P.O. Box 2111
Wilmington, Delaware 19899
Telephone (302) 429-3355 or toll-free (800) 365-6495

Stock Symbol

Common Stock, DEW—listed on the New York and Philadelphia Stock Exchanges

Annual Meeting

The Annual Meeting will be held on May 30, 1996, at 11:00 a.m. in the Clayton Hall, University of Delaware, Newark, Delaware.

Regulatory Commissions

Federal Energy Regulatory Commission

Elizabeth A. Moler—Chairperson
825 North Capitol Street, N.E.
Washington, D.C. 20426

Delaware Public Service Commission

Dr. Robert J. McMahon—Chairperson
1560 S. duPont Highway
P.O. Box 457
Dover, Delaware 19903-0457

Maryland Public Service Commission

H. Russell Frisby Jr.—Chairperson
6 St. Paul Street
Baltimore, Maryland 21202-6806

Virginia State Corporation Commission

Hullihen W. Moore—Chairperson
Tyler Building
P.O. Box 1197
Richmond, Virginia 23209

Transfer Agents and Registrars

First Mortgage Bond Trustee

Chemical Bank
450 West 33rd Street
New York, New York 10001

Common and Preferred Stock

Wilmington Trust Company
Corporate Trust Operations
P.O. Box 2111
Wilmington, Delaware 19899

Walk-in office:
1105 N. Market Street
Wilmington, Delaware

Additional Reports

To supplement information in this Annual Report, a Financial and Statistical Review (1985–1995) and the Annual Report on Form 10-K are available upon request. Please write to:

Delmarva Power & Light Company
c/o Wilmington Trust Company
Corporate Trust Operations
P.O. Box 2111
Wilmington, Delaware 19899

Duplicate Mailings

You may be receiving more than one copy of the Annual Report because of multiple accounts within your household. The Company is required to mail an Annual Report to each name on the shareholder list unless the shareholder requests that duplicate mailings be eliminated. To eliminate duplicate mailings, please send a written request to Wilmington Trust Company at the above address and enclose the mailing labels from the extra copies.

More Information

For more information about Delmarva Power, visit our Internet site:

http://www.delmarva.com

Officers as of December 31, 1995

Howard E. Cosgrove, Chairman of the Board, President, and Chief Executive Officer

Joseph W. Ford, Senior Vice President

Barbara S. Graham, Senior Vice President, Treasurer, and Chief Financial Officer

Ralph E. Klesius, Senior Vice President

Thomas S. Shaw, Senior Vice President/President, Delmarva Capital Investments, Inc.

Donald E. Cain, Vice President, Administration

Paul S. Gerritsen, Vice President

Wayne A. Lyons, Vice President

Frank J. Perry Jr., Vice President, Production

Dale G. Stoodley, Vice President and General Counsel

W. Douglas Boyce, Vice President, Central Division

Donald P. Connelly, Secretary

Hudson P. Hoen III, Vice President, Southern Division

James P. Lavin, Comptroller and Chief Accounting Officer

Dennis R. McDowell, Comptroller-Operating

Duane C. Taylor, Vice President, Electric Systems Engineering

Jack Urban, Vice President, Gas Division

D. Wayne Yerkes, Vice President, Northern Division

Board of Directors Committees

Audit Committee

James C. Johnson, Chairperson; Robert D. Burris; Audrey K. Doberstein

Compensation Committee

Sarah I. Gore, Chairperson; Michael B. Emery; James H. Gilliam Jr.; James C. Johnson

Executive Committee

Howard E. Cosgrove, Chairperson; Sarah I. Gore, Vice Chairperson; Michael B. Emery; James C. Johnson

Investment Committee

Howard E. Cosgrove, Chairperson; Audrey K. Doberstein; James H. Gilliam Jr.; Weston E. Nellius

Nominating Committee

Audrey K. Doberstein, Chairperson; Michael G. Abercrombie; Weston E. Nellius

Nuclear Oversight Committee

Michael G. Abercrombie, Chairperson; Robert D. Burris; Howard E. Cosgrove

Dividend Reinvestment and Common Share Purchase Plan

More than 40% of the Company's common shareholders of record are now participating in the Dividend Reinvestment and Common Share Purchase Plan. If you are not participating, you may want to consider the benefits of joining this plan. Under the plan, you can invest your cash dividends and also invest additional cash, up to $100,000 per calendar year, to purchase additional shares of common stock without a service fee. You may obtain a prospectus with the plan description and an enrollment authorization card by writing to:

Delmarva Power & Light Company
c/o Wilmington Trust Company
Corporate Trust Operations
P.O. Box 2111
Wilmington, DE 19899

OUR MISSION AT DELMARVA POWER

We will grow our business by exceeding our customers' expectations in providing high-quality products and services, energy, and regulated delivery services.

We will be the premier provider on the Delmarva Peninsula, as well as a significant regional competitor, while rewarding investors and valuing employees.

Designed, written [illegible]roduced by Delmarva Power, Communications Department Photography by Carlos Alejandro