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February 18, 2014

By Electronic Filing

David J Collins, Executive Secretary
Maryland Public Service Commission
William Donald Schaefer Tower
6 Saint Paul Street, 16th Floor
Baltimore, MD 21202-6806

Re: Case Nos. 9226 and 9232

Dear Mr. Collins:

On behalf of the Retail Energy Supply Association, enclosed please find an original and 17 copies of the Direct Testimony Richard J. Hudson, Jr.

Please feel free to contact me should you have any questions.

Sincerely,

A handwritten signature in blue ink, appearing to read 'B. R. Greene', written in a cursive style.

Brian R Greene

Cc. Richard J Hudson, Jr.
Service List

**BEFORE THE
PUBLIC SERVICE COMMISSION
OF MARYLAND**

In the Matter of the Review of the *
Delmarva Power and Light Company *
Standard Offer Service Administrative * Case No. 9226
Charge *

In the Matter of the Review of the *
Potomac Electric Power Company *
Standard Offer Service Administrative * Case No. 9232
Charge *

DIRECT TESTIMONY

OF

RICHARD J. HUDSON, JR.

On Behalf of

Retail Energy Supply Association

February 18, 2014

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1 **I. INTRODUCTION AND BACKGROUND**

2 **Q. PLEASE STATE YOUR NAME AND TITLE.**

3 A. My name is Richard J. Hudson Jr. I am employed directly by ConEdison Solutions as the
4 Director of Regulatory and Legislative Affairs. I am also the Pennsylvania State
5 Chairman for the Retail Energy Supply Association (“RESA”).¹ My responsibilities
6 with respect to RESA include representing the collective interests of the trade association
7 in regulatory proceedings, primarily in the Commonwealth of Pennsylvania but also
8 elsewhere such as Maryland.

9 **Q. PLEASE DESCRIBE YOUR EDUCATIONAL AND EMPLOYMENT HISTORY.**

10 A. I received a bachelor’s degree in business and economics from the University of North
11 Carolina at Greensboro. Prior to joining ConEdison Solutions I was employed by two
12 other retail suppliers – RRI Energy and Strategic Energy, LLC – in positions similar to
13 the one I now hold with ConEdison Solutions. I was also previously employed by the
14 Federal Energy Regulatory Commission (“FERC”) for approximately four years during
15 which I worked on a wide variety of FERC jurisdictional regulatory issues related to the
16 wholesale electricity industry that presented complex technical, legal and public policy
17 issues.

¹ RESA’s members include: AEP Energy, Inc.; Champion Energy Services, LLC; ConEdison Solutions; Constellation NewEnergy, Inc.; Direct Energy Services, LLC; GDF SUEZ Energy Resources NA, Inc.; Homefield Energy; IDT Energy, Inc.; Integrys Energy Services, Inc.; Just Energy; Liberty Power; MC Squared Energy Services, LLC; Mint Energy, LLC; NextEra Energy Services; Noble Americas Energy Solutions LLC; NRG Energy, Inc.; PPL EnergyPlus, LLC; Stream Energy; TransCanada Power Marketing Ltd. and TriEagle Energy, L.P. The comments expressed in this filing represent the position of RESA as an organization but may not represent the views of any particular member of RESA.

1 **Q. HAVE YOU EVER TESTIFIED BEFORE THIS COMMISSION?**

2 A. Yes, I submitted prepared testimony in Case No. 9221 involving Baltimore Gas and
3 Electric Company's ("BGE's) standard offer service ("SOS") administrative charges. I
4 have also testified in numerous other proceedings, a list of which is set forth in RESA
5 Exhibit RJH-1.

6 **Q. ON WHOSE BEHALF ARE YOU TESTIFYING IN THIS PROCEEDING?**

7 A. My testimony is submitted on behalf of RESA.

8 **Q. PLEASE DESCRIBE THE RETAIL ENERGY SUPPLY ASSOCIATION.**

9 A. RESA is a nonprofit organization and trade association that represents the interests of a
10 broad and diverse group of energy suppliers who share the common vision that
11 competitive retail and wholesale energy markets deliver a more efficient, customer-
12 oriented outcome than the regulated utility structure. We are devoted to working with all
13 stakeholders to promote vibrant and sustainable competitive retail energy markets for all
14 consumers. RESA members currently serve residential, commercial and industrial
15 ("C&I") and institutional customers in Maryland and other jurisdictions in North
16 America that have enacted retail choice.

17 **Q. WHAT IS THE PURPOSE OF YOUR TESTIMONY?**

18 A. On February 4, 2014, RESA, Potomac Electric Power Company ("Pepco"), Delmarva
19 Power and Light Company ("Delmarva Power"), and the Staff of the Maryland Public
20 Service Commission ("Staff")² filed a Joint Motion for Approval of Agreement of
21 Stipulation and Settlement. The purpose of my testimony is to generally describe certain

² Pepco and Delmarva Power are referred to collectively herein as "the Companies." Also, the term "Settling Parties" refers to RESA, Pepco, Delmarva Power, and Staff.

1 provisions in the Settlement Agreement and to explain why I believe the Settlement is in
2 the public interest and should be approved by this Commission.

3 **Q. PLEASE SUMMARIZE THE PROVISIONS OF THE SETTLEMENT AS THEY**
4 **PERTAIN TO RETAIL SUPPLIERS.**

5 **A.** The proposed Settlement Agreement resolves a number of key concerns associated with
6 the Companies' SOS Administrative Charges for each of the SOS customer classes. In
7 this regard, the Settlement Agreement, if adopted, would establish regulatory certainty
8 with regard to the SOS Administrative Charge. Such regulatory certainty is vitally
9 important to competitive retail suppliers operating in the state. Importantly, the
10 Settlement Agreement continues the current structure of the Administrative Charge,
11 while at the same time making it more transparent and reflective of the Companies'
12 actual costs incurred in providing SOS for certain cost components. Specifically, the
13 proposed Settlement Agreement provides as follows:

- 14 1. The Administrative Charges will continue to be composed of a utility return,
15 incremental costs, uncollectibles, and an Administrative Adjustment, and will
16 continue to apply exclusively to kWh of SOS load (§ 2);
- 17 2. The residential return component will be reduced from the current 1.5 mils to 1.3
18 mils, while the returns for Type I, Type II, and Hourly-Priced Service will remain
19 2.0, 2.0, and 2.25 mils, respectively (§ 3);
- 20 3. For residential SOS, the Companies would recover their actual incremental costs,
21 which is currently fixed at 0.5 mils, and would be trued up annually. For Types I
22 and II SOS, the Companies will continue the successful mechanism of fixing the

1 incremental costs and crediting back to all customers in that particular class any
2 over-recovered funds (§ 4);

3 4. The Companies will continue to use the most recent base distribution rate case to
4 calculate its residential uncollectibles expense, while the non-residential classes
5 will continue the existing methodology (§ 5);

6 5. The Administrative Adjustment for residential SOS, which provides for the
7 crediting of revenues back to all residential ratepayers, will continue (§ 6); and

8 6. The Companies' cash working capital needs would be recovered separately from
9 the Administrative Charge and trued up annually for all SOS classes (§ 7).

10 **Q. WHY IS THIS SETTLEMENT IN THE PUBLIC INTEREST?**

11 **A.** The Settlement is consistent with the purposes of the Electric Customer Choice and
12 Competition Act ("the Act"), including establishing customer choice of electricity supply
13 and supply services; creating competitive retail electricity supply and supply services
14 markets; and providing economic benefits for all customer classes.³ The Act also
15 mandates that the Commission, in overseeing the regulation of the restructured electric
16 industry, "be fair" to customers, utilities, and retail electricity suppliers.⁴

17 The Administrative Charge is an important feature of the SOS pricing structure and retail
18 market design in Maryland. It plays an essential role in ensuring that SOS prices are
19 market prices that properly reflect all of the utility's costs and risks involved in providing
20 SOS. The Administrative Charge ensures that the utilities, in providing SOS, recover

³ Md. Code Ann. § 7-504 (Public Utilities Article).

⁴ Md. Code Ann § 7-505(a) (Public Utilities Article).

1 their “verifiable, prudently incurred costs” plus a “reasonable return” for providing SOS.⁵
2 Beyond that, however, the Administrative Charge, with its Administrative Adjustment
3 mechanism for residential customers and administrative credit mechanisms for Types I
4 and II, acts as a proxy for the full and complete unbundling of all generation service-
5 related costs from distribution rates, and it serves to reflect the types of costs that retail
6 suppliers must include in their retail supply offers. In essence, the Administrative Charge
7 helps to create a level playing field on which retail suppliers can compete to offer various
8 electricity and electricity supply products and services to the Companies’ ratepayers.

9 By continuing and refining the Administrative Charge methodology to ensure that SOS is
10 priced at market rates that reflect the Companies’ costs and a return, the Settlement
11 Agreement properly captures the purposes, goals, and plain meaning of the Act, and will
12 play a key role in the continued development of retail competitive electricity markets in
13 Maryland.

14 **II. INCREMENTAL AND UNCOLLECTIBLE COSTS**

15 **Q. DOES RESA AGREE WITH THE SETTLEMENT AGREEMENT’S**
16 **TREATMENT OF THE INCREMENTAL AND UNCOLLECTIBLE COSTS IN**
17 **THE SOS ADMINISTRATIVE CHARGES?**

18 **A.** Yes. For residential customers, the Settlement Agreement would replace the fixed
19 incremental component with a component that is based on actual incremental costs and
20 trued up annually, and would continue to utilize the most recent base rate case for the
21 utility’s uncollectible allocation. This is a reasonable resolution of the recovery of

⁵ Md. Code Ann. § 7-510(c) (Public Utilities Article).

1 incremental and uncollectible costs and ensures that the Companies do not over- or
2 under-recover these costs.

3 **III. RETURN**

4 **Q. DOES RESA AGREE WITH THE SETTLEMENT AGREEMENT'S**
5 **TREATMENT OF THE RETURN COMPONENTS IN THE SOS**
6 **ADMINISTRATIVE CHARGES?**

7 A. Yes. As explained above, the Administrative Charge should reflect all of the costs and
8 risks incurred by the Companies in providing SOS. That includes a return component,
9 which is also mandated by statute. From a policy perspective, retail suppliers expect to
10 earn returns and must do so to satisfy investors and attract capital to maintain their
11 respective businesses. Without an adequate return component in the SOS Administrative
12 Charge, retail suppliers would be competing against an SOS price that does not include
13 pricing components that are similar to those included in retail supplier offerings. That
14 said, RESA is always concerned that SOS or default service providers should not be
15 incentivized to keep customers on SOS or default service. The returns for each SOS
16 customer class in the Settlement Agreement strike the right balance between these two
17 competing interests and appear "reasonable" as required by statute, as retail suppliers
18 generally would expect to earn returns in excess of those in the Settlement.

19 **IV. ADMINISTRATIVE ADJUSTMENT**

20 **Q. DOES RESA AGREE WITH THE SETTLEMENT AGREEMENT'S**
21 **CONTINUATION OF THE ADMINISTRATIVE ADJUSTMENT FOR**
22 **RESIDENTIAL CUSTOMERS AND THE ADMINISTRATIVE CREDIT FOR**
23 **TYPE I AND II CUSTOMERS?**

24 A. Yes. As noted above, the current Administrative Adjustment is the "residual" millage
25 amount that remains after subtracting the other three elements from the total
26 Administrative Charge for that SOS rate class. The Administrative Adjustment is,

1 therefore, a proxy for the full scope of costs that should be reflected in SOS rates but
2 which the Companies instead recover through their distribution service base rates. While
3 the revenue from the Administrative Adjustment is ultimately credited back to customers,
4 it plays a critical role in reflecting certain costs in avoidable SOS rates and is an essential
5 component of the retail market in Maryland.

6 **Q. PLEASE ELABORATE ON WHY THE ADMINISTRATIVE ADJUSTMENT IS**
7 **AN ESSENTIAL COMPONENT OF THE RETAIL MARKET IN MARYLAND.**

8 A. Retail supplies incur numerous costs associated with the provision of electric retail
9 service which are similar to the types of costs that the Companies incur in their provision
10 of SOS. These costs can include administrative and general expenses, sales and
11 advertising to acquire new customers, customer accounts information that must be
12 maintained, customer support such as maintaining a call center, and credit and collections
13 services. While the level of costs may differ as between retail suppliers, each retail
14 supplier incurs these types of costs. Each retail supplier must include the costs of these
15 services in their respective retail offerings. In other words, each retail supplier must price
16 its particular product such that the supplier can recover its operating costs and earn a
17 return.

18 Maryland IOUs, including the Companies, incur these types of costs in providing
19 SOS, but these costs are not reflected in the utilities' SOS rates. Rather, the IOUs
20 recover these types of costs in their distribution rates. The purpose of the Administrative
21 Adjustment for residential customers (and the administrative credit for Types I and II) is
22 to account for some portion of these joint and common costs that the Companies incur
23 while providing SOS but which are paid for by all customers, including shopping

1 customers. The Administrative Adjustments and credit mechanisms are designed to be
2 revenue-neutral to the Companies, ensure that the Companies do not double recover their
3 costs, and simulate the types of costs that retail suppliers incur and must recover from
4 their customers through the prices they offer. Without either an Administrative
5 Adjustment/credit mechanism or a full unbundling, the Companies would be offering
6 SOS at rates that do not include the full costs of the Companies' services, and retail
7 suppliers would be in the unreasonable and unenviable position of marketing against an
8 SOS rate that is, in effect, a discounted below-market price.

9 **V. CASH WORKING CAPITAL**

10 **Q. DOES RESA AGREE WITH THE SETTLEMENT AGREEMENT'S PROPOSAL**
11 **REGARDING THE COMPANIES' RECOVERY OF THEIR SOS-RELATED**
12 **CASH WORKING CAPITAL REQUIREMENTS?**

13 A. Yes. Cash working capital costs are real costs incurred in the provision of SOS, and
14 retail supplies incur cash working capital costs as well in the daily operations of their
15 businesses. The Settlement Agreement's proposal to allow the Companies to recover
16 their actual SOS-related cash working capital requirements, subject to annual true-ups, is
17 appropriate.

18 **VI. CONCLUSION**

19 **Q. DOES THIS COMPLETE YOUR DIRECT TESTIMONY?**

20 A. Yes.