



OEB COST ALLOCATION REVIEW

Phase 1: OEB Cost Allocation Principles and Methodologies

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November 2, 2005

Purpose of Cost Allocation

- To allocate the costs to provide service to the various customer rate classes based on cost causality principles
- To assess the reasonableness of the rates charged to customers in relation to their allocated costs
- To support rate design

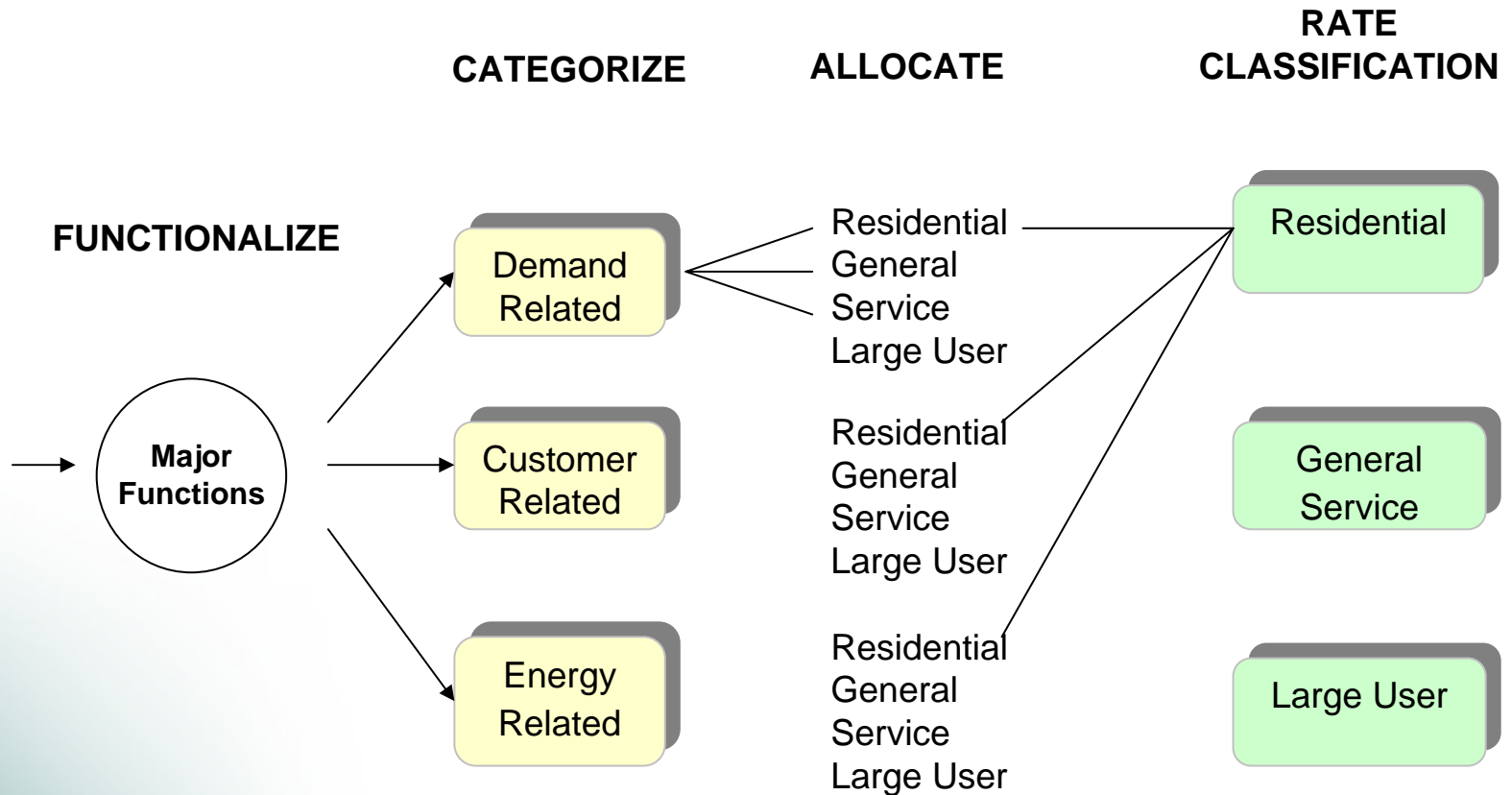
Traditional Cost Allocation Process

- Direct assignment
- Three-step process used to allocate common costs:
 - Functionalization
 - Categorization
 - Allocation

Traditional Cost Allocation Process (Cont'd)

MAJOR STEPS IN ALLOCATING COMMON COSTS

TOTAL REVENUE REQUIREMENT



Challenges

- Dealing with informational filings for 90+ distributors
 - Striking an appropriate balance between consistency across LDCs and accuracy of the studies
- Some LDCs have never performed a cost allocation study
- Inconsistencies across distributors in terms of record-keeping
- Some USoA accounts do not have the level of granularity desirable to conduct a cost allocation study

Over-Arching Principles

- To promote consistency and efficient review, cost allocation methodologies should be standardized to the extent possible
- Methodology and principles should be prescribed but limited flexibility over and above prescribed standard should be allowed if justified

Directly Assignable Costs

Costs that can be directly attributable to a specific rate class

- Defined as applicable where a one-to-one mapping exists between an account and a rate class
- Current proposal:
 - Very few accounts have been identified (e.g. maintenance of street lighting)
 - Direct allocation could be used if applicable

Functionalization

Grouping of costs into major functions performed by distributors

- Current proposal:
 - Categorization and allocation will be carried out at the account level
 - USoA generally provides an adequate level of granularity
 - Identified need for more information at the account level (e.g. separation of conductors into sub-transmission, primary and secondary lines)

Functionalization (Cont'd)

- Distributors will be required to re-classify accumulated depreciation and depreciation expense to the corresponding rate base account
 - Based on supporting documentation (if available)
 - Otherwise, prorated based on gross plant balances

Categorization

Separation of costs into sub-groups based on cost drivers

- Two principal categorization:
 - Demand-related
 - Customer-related
- Certain distribution assets and related O&M are categorized jointly as demand and customer related
- Current proposal: Minimum System Approach
 - Standard factors by strata (# customers/km of lines) and asset group to be used by all distributors

Allocation

- Allocation of categorized cost to the various customer rate classes:
 - Demand-related costs
 - Customer-related costs
 - Other costs

Allocation of Demand-Related Costs

- Current proposal:
 - Direct allocation where facilities are fully dedicated to one customer or one customer rate class
 - Non-coincident peak (1 class NCP): standard method for joint facilities
 - Use of coincident peak (CP) in defined instances
 - Demand allocators to be adjusted for line losses, and peak-load carrying capacity

Allocation of Customer-Related Costs

- Current proposal:
 - Standard methodology for all customer-related costs
 - Distributors could file their own weighted allocation factors for information purposes in addition to the standard factors

Allocation of Other Costs

Residual costs (A&G, General Plant, Taxes, Misc. Revenue)

- Current proposal:
 - Standard methodology for all distributors
 - Materiality does not warrant flexibility