

POINT OF VIEW »

COST OF SERVICE MODELS: TOP FIVE MUST-HAVES

In this era of increasing regulatory transparency and the need for innovation in rate design alternatives, utilities must have a state-of-the-art cost of service model to perform the necessary analyses. MCR recently conducted a survey of utility regulatory professionals on what they see as the five most important features in a cost of service model today. Respondents identified these “Top Five” as the ability to:

- 1 » Quickly and easily change allocators, functionalization methods, and/or rate classes
- 2 » Easily import and load cost data into the model from source data sets (general ledger, plant accounting, etc.)
- 3 » Automatically functionalize imported data
- 4 » Run scenarios with different inputs and compare the results against base case study results
- 5 » Provide transparency of model calculations to commission staff and intervenors

MCR’s Cost of Service (COST™) model was developed to address these five key features and more. COST™ was designed to replace the outdated “black box” cost of service models that are still being used. COST™ is rich in features for the user as well as the regulatory strategist. Within the COST™ model, you will find:

- **Visibility.** Built in Microsoft Excel, COST™ is a spreadsheet model with open logic for audit, review, and user editing. All model logic is clearly identified, allowing for quick turnaround on incorporating required updates. Users can decide how much or how little of the model is locked down through Excel’s native protection capabilities.
- **Regulatory Transparency.** Regulators and intervenors are seeking greater insights into utility cost of service and are pushing for access to utility cost of service models. COST™ allows utilities to provide a working copy of the model to external parties.
- **Flexibility.** COST™ allows for development of the cost of service without any buried code or time-consuming run-time macros. New cost elements, revenues, or rate base items can be quickly integrated into the analysis; adding new rate schedules is as simple as inserting a column into Excel.
- **Data Management.** With its data import logic, COST™ enables users to manage data sources seamlessly. Users can quickly select data sources while ensuring the integrity of the model. Source information is clearly marked to assist in file and data management.
- **Scenario Analysis.** During a rate case, the cost of service is the tool often used by intervenors to attempt to shift costs away from their clients (e.g., residential, commercial, or industrial customers).

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COST™ has a built-in scenario analyzer to permit third parties to test alternatives while ensuring the results are accurate. Scenario adjustments can be compared to the “as filed” case, which is controlled by the utility, so that there are no surprise outcomes to the rate case.

- **Defensibility.** Results from the COST™ model can stand up to the scrutiny of intervenors. The results are easily auditable and defensible, which helps to get all stakeholders to agree that your ratemaking methods are sound.

CASE STUDY

How Arizona Public Service Implemented a Transparent Cost of Service Model

Arizona Public Service (APS) began their search for a new cost of service model in 2017 at the end of a general rate case proceeding. The new rates sought significant structural changes in net metering and other related areas. The nature of the changes prompted the input of many intervenors and intense review of APS’s rate and cost of service filings.

The existing database tool APS was using generated the appropriate filing reports in spreadsheet form, but these reports were essentially pasted values with no underlying logic. Given the scrutiny of the filing, commission staff and intervenors sought to have more transparency on the logic, which was buried in proprietary code. As part of the final rate order, APS agreed to implement a more transparent cost of service model.

After a review of various alternatives, APS selected MCR’s Cost of Service Tool. COST™ met two important criteria for the utility per Jessica Hobbick, Manager of Rate Design & Revenue Requirements at APS: “We were looking for something Excel-based, so intervening parties could make changes to see how the revenue requirement changes,” she said. “We also wanted something that didn’t rely on as much vendor support—a living, breathing model that we could change between rate cases.”

The MCR team worked closely with APS staff to quickly implement COST™, with the new model up and running in a matter of weeks. COST™ met the requirement for transparency, allowing external party review of all model logic coupled with the ability to adjust key inputs. In addition, APS staff were able to quickly learn the model and incorporate modifications to meet ongoing changes in their rate structure.

“MCR was very responsive and thorough. We’re impressed with how quickly they were able to implement the model; it was a much shorter process than other vendors’ estimates.”

—Jessica Hobbick, Manager of Rate Design & Revenue Requirements, APS



MCR is a management consultancy that works collaboratively with clients to ensure successful project outcomes.

The experts who led the development of our COST™ model have an average of 20 years’ experience in the industry. We combine our knowledge of utility financials with each client’s unique needs, ensuring our clients’ satisfaction with the final product.

To learn more, visit mcr-group.com/regulatory or contact:

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