Q. On page 14, line 24, of the Cost of Service Evidence, Stone and Webster stated “Hydro is regulated in an embedded cost jurisdiction”. Please explain in detail Stone and Webster’s view on how this affects the application of marginal cost principles?

A. In an embedded cost environment, fully-allocated cost of service is the industry standard to assess the degree to which the utility’s revenue requirement is equitably allocated among customer classes. Rate structures that are reflective of the demand, energy and customer components of embedded costs are also used to assess intraclass subsidies. Marginal costs can play a role in rate design by providing price signals as to the cost of marginal energy use during certain periods; setting demand rates that signal the cost shifting between on-peak and off-peak periods; and as a guide to moderating the level of the demand rate to emphasize or de-emphasize its significance. However, rate design in an embedded cost jurisdiction is rarely, if ever, based predominately on marginal costs.