

Cost Allocation Methodology

1. Introduction

1.1 The Cost Allocation Model is an annually updated working file that takes the principles of the “Xoserve Cost Allocation Methodology” (v4.0) and the CDSP Service Document “Budget and Charging Methodology” and practically applies them to the Xoserve cost base, as defined via the annual Business Planning cycle, so as to:

- a) allocate costs across the CDSP Service Areas, and;
- b) allocate the Service Area costs across the CDSP customer constituencies.

1.2 The output of the model directly feeds into the preparation of the Charging Statements that are published to customers via the Joint Office of Gas Transporters.

1.3 Costs are a mixture of Service & Operate (S&O) and Investment operating costs.

2. What is the format?

2.1 The Model consists of an Excel workbook with multiple input and output tabs.

2.2 The model owner or user enters data, typically consisting of £ and/or FTE values, and in some instances the type of cost and the associated Supplier are used.

2.3 The in-built formulae and logic subsequently aggregate Direct Costs to applicable Service Areas and disaggregates Indirect/Support costs across applicable Service Areas.

2.4 For an explanation of what constitutes Direct and Indirect Costs and the basis of their apportionment across Service Areas please refer to the Xoserve Cost Allocation Methodology (v4.0).

3. What process does the model undertake to allocate costs to a Service Area and subsequently to a customer?

3.1 There are currently nine stages from cost identification to final customer charge.

The Stages are as follows

Stages

1. Define Cost Centres of Business

People Costs

2. Allocate People Cost and FTE in each cost Centre
3. Allocate People Costs to Cost Bases

4. Allocate People Costs Per Cost Centre & Cost Base into Service Areas

Other Costs

5. Define and Calculate Other costs into Cost Bases
6. Define IS Costs By IS Category
7. Assign IS Costs to IS Application
8. Assign IS Applications and Other Costs to Service Area

Summary

9. Define Service Area to Customer Constituency
10. Summarise People, Other and IS costs by Service Area
11. Summarise Service Area by Customer Contingency

Stage 1 – Cost Centres Identification

- 3.2 This stage ensures all cost centres of Xoserve are documented. Some of these will be Direct in nature, whilst others will be Indirect, or a mixture of both.

Stage 2 & 3 – Allocate People Costs to Cost Centres & Cost Bases (Direct, Investment, Specific Service, Third Party & Support Costs.

- 3.3 The purpose of this stage is to allocate all FTEs within the business to either a Direct or Indirect cost base and calculate the associated Direct and Indirect £ values of those FTEs.
- 3.4 All cost centres (CC) are listed in rows, as per Stage 1.
- 3.5 Data is entered/calculated in subsequent columns as per the below.
- 3.6 Total people costs for each CC are entered along with the number of FTEs present in the CC.
- 3.7 The FTEs are then allocated across the following four Direct cost bases (whole FTEs are allocated, there are no fractions of an FTE):

- Direct Operations (S&O);
- Direct Investments (S&O);
- Specific Services (S&O); or
- 3rd Party (S&O).

3.8 If not all FTEs within a CC are allocated across the above four Direct cost bases, a balancing FTE figure is calculated, and these FTEs are deemed to be Indirect/Support FTEs.

3.9 The £ value equivalent of the five separate cost bases (including Indirect) per CC is calculated based on:

$$\frac{FTEs\ in\ cost\ base\ in\ given\ CC}{\sum FTEs\ in\ CC} \times Total\ people\ costs\ for\ CC$$

3.10 Whilst the above steps allocate Indirect costs to CCs, a further calculation is included on this tab to also allocate the Indirect costs back across the four Direct cost bases:

$$\frac{Direct\ cost\ base\ FTEs}{\sum Direct\ cost\ base\ FTEs} \times \sum Indirect\ people\ costs$$

3.11 The percentage equivalent of the ratio calculated in the first part of the above formula for each Direct cost base is also documented at this tab for use in future stages.

Stage 4 Allocating People Costs to Service Areas

3.12 The purpose of this stage is to allocate Direct and Indirect people costs, as per the calculations undertaken in *Stage 2* tab, across CDSP Service Areas, excluding the Direct Investments cost base.

3.13 All CDSP Service Areas are listed.

3.14 Further service areas are listed in relation to Specific Services and 3rd Party Services.

3.15 Those CCs that, per *Stage 2* that have FTEs allocated to Direct cost bases (Direct Operations etc. but excluding Direct Investments) are listed across subsequent columns.

3.16 FTEs are allocated in each CC column against Service Area rows. Check totals are included to ensure that the total of each CC column ties back to the total of the FTEs in each cost base per CC in as in *Stage 2*.

3.17 Based on 3.16 and the costs calculated as per 3.9, further columnar formulas calculate the £ cost of Direct FTEs by Service Area as follows:

$$\frac{\sum Direct\ FTEs\ in\ Service\ Area}{\sum Direct\ FTEs} \times \sum Direct\ people\ costs$$

3.18 The cost of Indirect people is also shared across Service Areas as follows:

$$\frac{\sum \text{Direct FTEs in Service Area}}{\sum \text{Direct FTEs}} \times \sum \text{Indirect people costs}$$

3.19 This stage has two components, one for the Operational Costs base and a second which deals only with those FTEs allocated to the Direct Investments cost base. However, these people are not Investment funded, rather they are S&O funded people that assist with the delivery of Investment activities.

Stage 5 – Other Costs - Capture

3.20 This stage captures the total of all non-people S&O related operating expenditure, whether Direct or Indirect, and allocates them to either a Direct cost base or an Indirect cost base.

3.21 Irrespective of the applicable Direct/Indirect cost base, the other costs are also aggregated as follows:

- a) IS – being Information Systems (IS) costs (broken down in greater detail in stages 6 & 70.
- b) Non-Staff – a range of various costs covering professional fees and consultancy through to training and development.
- c) Bought-In – Predominantly (but not exclusively) services that Xoserve procures on behalf of the industry such as AUGÉ, PAFA and DM/NDM reads, but also includes property costs.

3.22 The allocation of the non-people costs to Direct or Indirect cost bases is at the discretion of the Model Owner/Manager, who is expected to make suitable enquiries of cost owners to ascertain the nature of costs.

3.23 Similarly, to stages 3 & 4, the Indirect costs are allocated back against the Direct cost bases in accordance with the % ratio calculated at 3.11 i.e.:

$$\frac{\text{Direct cost base FTEs}}{\sum \text{Direct cost base FTEs}} \times \sum \text{Indirect non – people costs}$$

Stage 6 – IS Input

3.24 Provides a greater level of granularity of the costs making up Information System costs to help inform Stage 7.

Stage 7 - IS Cost to IS Application

- 3.25 IS costs are allocated against the systems that Xoserve operates on behalf of the industry, such as UK Link, Gemini etc. which are deemed to be Direct (system) costs, or allocated against Indirect (system) costs.
- 3.26 This stage takes the granular breakdown of costs per *Stage 6* and allocates a proportion of the costs across different IS Systems based on %s recorded in columns.
- 3.27 The system allocations have been provided by subject matter experts.
- 3.28 Typically, IS costs are broken down at sufficiently a granular level that they are deemed to be Direct costs or Indirect costs, there are no costs that are allocated to both cost types.

Stage 8 - Assign IS and Other Costs to Service Areas

- 3.29 This Stage allocates Direct and Indirect non-people S&O costs across to the CDSP Service Areas.
- 3.30 For Direct IS, Non-Staff and Bought-In costs, allocation percentages are utilised to calculate the costs of Direct and Indirect systems by Service Areas. In the case of IS costs, the calculations from *stage 7* are utilised, whereas for Non-Staff and Bought-In costs, these are attributed to a Service Area where they are incurred.
- 3.31 Systems allocation by Service Area were provided by subject matter experts.
- 3.32 For Indirect IS, Non-Staff and Bought-In costs, the calculations are allocated across Service Areas based on the number of Direct FTEs allocated to those Service Areas:

$$\frac{\sum S\&O\ FTEs\ in\ Service\ Area}{\sum Direct\ S\&O\ FTEs} \times \sum Indirect\ non - people\ costs$$

- 3.33 There are no Direct IS costs attributed to Investment Service Areas, only Indirect but these are allocated at this stage. As is the case with people costs, these Indirect non-people costs relate to the delivery of Investments via S&O resourcing rather than being funded directly by Investment income.

Stage 9 – Service Area to Customer Contingency

3.34 This records the allocation percentages for costs by Service Area across the different customer constituencies, as described in the CDSP Service Document “Budget and Charging Methodology”. This is the basis for the allocation of Service Area costs to customer constituencies in later tabs.

3.35 This is updated as and when new Service Areas are added or removed.

Stage 10 – Results @ Level One

- 3.36 This is the lowest level aggregation tab/working.
- 3.37 It takes every service area, including Specific Services and 3rd Party, as rows, and details every cost type in a columnar format: People, IS, Non-Staff, Bought-In, for both Direct and Indirect cost types.
- 3.38 It subsequently takes the totals of the Service Areas and allocates them against customer constituencies with reference to the percentages detailed in *stage 9*.
- 3.39 This then enables population of the Charging Statements at the end of the Business Planning cycle.

Stage 11 – Results @ Level Two

- 3.40 This aggregates results but to a higher level than Level One.
- 3.41 The aggregate of People costs are allocated across the customer constituencies with reference to the percentages detailed in *stage 9*.
- 3.42 The aggregate of other costs are allocated across the customer constituencies with reference to the percentages detailed in *stage 9*.
- 3.43 A comparison to the customer constituency calculations detailed in Level One is included for completeness.

4. What is the process for updating the model?

- 4.1 The model is updated iteratively as the Business Planning cycle evolves.
- 4.2 The model deals with S&O costs, be they people versus non-people, Direct or Indirect, updated in line with the S&O bridges that are prepared and published in the Business Plan.
- 4.3 The model does not start in a “blank” and input free state each year, rather the prior year model’s inputs are updated.

5. What checks and balances are in place to ensure the model’s accuracy?

- 5.1 Standard spreadsheet error checks are included from tab to tab to ensure that inputs and calculations flow through the model completely.

5.2 When the inputter believes they have finalised the model in line with the published Business Plan and that the associated Charging Statements have been prepared, prior to publishing, a separate member of the team undertakes a number of checks (not an exhaustive list):

- Ensuring that the totals for General Services, Specific Services and 3rd Party per the model agree back to the Business Plan.
- That the total of the Service Areas split by customer constituency agrees back to the *L1* total for the Service Area and therefore that 100% of costs have been allocated to the customer constituencies.
- That the formula references for allocating costs to customer constituencies are correct based on *stage 9* allocations.
- That the totals by Service Area and the customer constituency splits have been transposed into the Charging Statements accurately, prior to the application of inflation.
- That the previously communicated inflation rate is accurately applied to the Service Area totals and customer constituency splits.