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March 16, 2005

Mr. Richard Stout
Chief Regulatory Officer
British Columbia Hydro and Power Authority
17th Floor, 333 Dunsmuir Street
Vancouver, B.C. V6B 5R3

Dear Mr. Stout:

Re: British Columbia Hydro and Power Authority
2004/05 to 2005/06 Revenue Requirements Decision
Directives 72 and 73 (pages 212-213) – Engineering Services

This letter replies to the BC Hydro letter dated March 1, 2005 enclosing the filing ("First Stage Submission") regarding the provision of engineering services within BC Hydro.

By letter dated February 10, 2005, in reply to the BC Hydro letter dated January 10, 2005, the Commission stated that it accepted BC Hydro's proposed two stage response to Directives 72 and 73 provided that the options and action contemplate either open competitive processes for securing engineering services or, in the alternative, outsourcing the engineering function. Although Directives 72 and 73 did not state that all engineering would be subject to open competitive processes, the Commission believes that it is reasonably inferred from the Directives that it was the intention of the Commission that all engineering would ultimately be considered for open competitive processes, or in the alternative, outsourcing the engineering function to an outside engineering firm. The expected benefits to be derived from following Directives 72 and 73 relate to the hourly charge for engineering services, a commercial approach to defining the scope of engineering service requirements, and the efficiency by which engineering services are delivered. As stated in the October 29, 2004 Decision:

The Commission Panel is generally satisfied with the direction senior management are taking their lines of business and the general timetable they are working toward to make the necessary changes (BC Hydro Argument, p. 30), with the exception of the Engineering Services Group as discussed in Chapter 10.

In the March 1, 2005 First Stage Submission at page 9, BC Hydro identified fundamental principles for any evaluation of its required engineering services. Principle 3 states that:

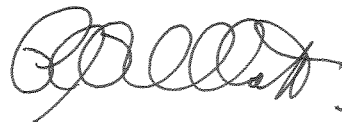
The majority of core engineering work will be performed by BC Hydro employees to ensure the quality and availability of resources, continuity of knowledge and approach, and to build and maintain a corporate technical memory.

Principle 4 states:

Non-core engineering work will be performed by either internal (BC Hydro) resources or external (non-BC Hydro) resources such as....

The Commission considers that these fundamental principles are inconsistent with Directives 72 and 73. In these circumstances where BC Hydro appears to be unwilling to pursue either open competitive processes for all engineering services or outsourcing the engineering function, the Commission considers that the benefits expected to be derived from Directives 72 and 73 may still be realized. Therefore, BC Hydro may either elect to follow Directives 72 and 73 and revise its fundamental principles or, alternatively, pursue the proposal set forth in the First Stage Submission. If BC Hydro elects to follow the proposal set forth in the First Stage Submission, then it will be relieved of the filing requirements of the Directives, including the September 1, 2005 filing. In either event, BC Hydro should anticipate that the comments and concerns raised in the Decision will be relevant considerations to a determination with respect to the costs of engineering services at the next revenue requirements proceeding. If BC Hydro elects to revise its fundamental principles, then the Commission requests that it revise its First Stage Submission before April 15, 2005.

Yours truly,

A handwritten signature in black ink, appearing to read 'R. Pellatt', with a stylized flourish at the end.

Robert J. Pellatt

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