

BC Hydro

**FINAL REPORT ON ASSESSMENT OF ARRANGEMENTS
TO OUTSOURCE INFORMATION TECHNOLOGY,
CUSTOMER CARE AND OTHER SERVICES TO
ACCENTURE BUSINESS SERVICES**

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Final Report on Assessment of Arrangements to Outsource Information Technology, Customer Care and Other Services to Accenture Business Services

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1. INTRODUCTION

The outsourcing arrangements between BC Hydro and Accenture became effective on April 1, 2003. The outsourcing contract (the MSA) effectively transferred responsibility for provision of a number of “support services” to Accenture Business Services (ABS). The bulk of the support services involve customer care and the provision and maintenance of technology based facilities for a number of the utility’s lines of business. The full extent of the functions affected by the outsourcing arrangement is shown later in this report as Figure 1.

On January 23, 2003, BC Hydro engaged Douglas Louth Associates Inc. (DLAI) to carry out an objective review of the outsourcing arrangements the utility was then proposing to implement with Accenture. We commenced our work on that date and prepared an interim report on our findings on May 10, 2003. The interim report covered the status of outsourcing arrangements at the point in time when they were first implemented. The contents of this report, the issues we then identified and the recommendations we made for on-going work by BC Hydro were accepted by the utility.

A major finding of the interim report was that, quite reasonably, a number of activities relating to full implementation of the arrangements had either not been completed by the first month of operation, or had not had time to mature to a point where our firm could objectively review the resulting impact. For these reasons, BC Hydro asked DLAI to return when the arrangements had been in place for six months, at which point we would complete our work by addressing the outstanding issues. We agreed to do so and commenced the second phase of our work on October 14, 2003.

Our final findings were presented to, and agreed with, BC Hydro on January 22, 2004. We have thus reached the final milestone in our assignments at which we are required to produce this final report.

We recommend that the reader familiarizes him/herself with our interim report before studying the final report. As a general rule, the issues identified in May 2003, and the recommended actions to address them, will not be discussed further in this document. We will only do so where we consider it necessary to support additional findings arising from follow-up review by our consultants.

It is however appropriate to record the fact that the majority of the issues identified in DLAI’s interim have been addressed and resolved by BC Hydro to our firm’s satisfaction. In later sections we will provide commentary to support our opinion that:

- The status of the relationship between the utility and ABS has matured positively and appears to be working,
- The levels of service being provided to external customers are at least as good as those achieved by BH Hydro prior to signing of the outsourcing agreement,

- Costs of service from ABS have proven to be very close to those budgeted by the utility, and savings over 2003/4 costs forecast by BC Hydro are very likely to be realized when final numbers are developed for the full fiscal year, and
- No new regulatory issues have been identified and those referred to in the interim report have presumably been addressed in the utility's 2004 rate application.

Only two issues identified in our interim report remain to be resolved. These are:

- Finalization of a favourable pricing model to be applied in the second year of the outsourcing contract, starting in April 2004, and
- Rationalization of service level standards to a point at which they become a more effective tool for monitoring of ABS' performance.

The rationale for our opinion on these and other issues will be described in later sections of this final report. Initially however it is necessary to reiterate DLAI's role in the final phase of our assignment, the terms under which the overall assignment was carried out, our qualifications to perform it and the timing of the work.

2. DLAI'S ROLE

DLAI's role in carrying out the review of the outsourcing arrangements was defined by BC Hydro upon our engagement in January 2003, during discussions with Mr. Bob Elton and Mr. Bob Steele. It is described in following paragraphs.

Terms of Reference

1. Review the outsourcing arrangements BC Hydro was finalizing with Accenture in respect of customer care and support services. We were instructed that this review was to be carried out at a level sufficient to allow DLAI to provide an opinion regarding the overall desirability of the outsourcing arrangements from BC Hydro's business perspective.
2. Also from BC Hydro's perspective, review the advantages and disadvantages of the proposed outsourcing arrangements, to a level of detail sufficient to verify costs and benefits estimated to accrue to BC Hydro.
3. Provide a formal report specifically directed to the preceding points. We were instructed that this report should cover the background to the assignment, all facets of the work and a formalization of DLAI's findings and opinions.
4. Prepare the formal report on the basis that it may potentially be used as supporting information in any public discussion of the outsourcing arrangements, or as evidence to be put before regulatory authorities.

In fulfilling these terms of reference, DLAI was instructed by BC Hydro to examine the impact and implications of the outsourcing contract on all lines of business affected by the ABS arrangements.

In all respects, DLAI was instructed to work as an independent and objective consultant to BC Hydro and to examine and comment on its findings on this basis.

Our work was to be carried out using a business perspective. We were not required to assess any wider strategic or political ramifications of the utility's outsourcing arrangements with Accenture.

Subsequent to the establishment of the initial terms of reference, it was agreed with BC Hydro that DLAI's consulting work should be split into two phases. Further, the reporting aspects of our work should be split into two parts. Such a split would allow greater balance to our reporting because we could then:

In Phase One:

- Provide an interim opinion on the Accenture arrangements following contract signing, but before the arrangements were implemented,
- Produce an interim report for BC Hydro identifying our immediate concerns,
- Provide input to the utility to help it address these concerns.

In Phase Two

- Carry out a further review six months after implementation, when any issues arising from our interim report would have been addressed by BC Hydro, and
- Produce a final report expressing our firm's opinion.

In addition to provision of professional opinion to BC Hydro, it was agreed with Mr. Elton that our work in both phases should also provide information to the utility in such a way that it could potentially be used in the regulatory environment. Specifically, our reports should provide reasoned opinion germane to BC Hydro's 2004 rate submission to the BC Utilities Commission. They would also form the basis for formal presentation of evidence to the Commission.

Reporting Relationships

Throughout the first stage of our assignment, leading to production of the interim report, we reported to Mr. Bob Steele of BC Hydro and worked closely with him to ensure identification and provision of key documents to our team. Mr. Steele also arranged access to persons it was necessary for us to interview. During the final phase of the work we reported to Ms. Jay Grewal of BC Hydro

Mr. Gary Sherlock was also heavily involved in making arrangements for many of our activities, particularly where identification of financial information was needed. Mr. Bob Elton was our primary contact with BC Hydro's executive group.

We were instructed that the majority of the work was to be carried out by DLAI's president, Douglas Louth, because he has extensive experience in the outsourcing and customer care area of the utilities industry. It was considered by BC Hydro that his qualifications in this regard would be useful in formulating a professional opinion on the Accenture arrangements.

Since this document will likely pass into the public domain, it is necessary to formalize Mr. Louth's credentials to complete the work for BC Hydro and present a qualified opinion on the outcome. To this end, his professional profile is attached to this report as Appendix A, and our firm's broader qualifications are presented in the next section of this report.

Mr. Louth was assisted throughout the assignment by Mr. Toby Symes, who carried out work in the areas of costs, budgets and financial analysis, using information provided to him by BC Hydro. Mr. Symes is a Chartered Accountant and, like Mr. Louth, was previously a Partner in the Vancouver office of Deloitte and Touche.

DLAI's Qualifications

DLAI is an international consulting firm specializing in the commercial aspects of the energy utility industry. Much of its work is in the customer care and technology areas. In addition to assignments for a number of North American utilities, DLAI has worked on overseas assignments with utilities in India, the United Arab Emirates, and Egypt. The firm is an accredited supplier of consulting services to foreign aid organizations such as the Asian Development Bank and USAID.

DLAI's president, Douglas Louth has personally carried out previous reviews in the province of BC relating to outsourcing arrangements similar in nature to the BC Hydro/Accenture contract. This work has been carried out both for the BC Utilities Commission and the client companies concerned. The outsourcing arrangements in question were made between Westcoast Energy and Enlogix and separately between BC Gas and CustomerWorks. In BC Gas' case, the outsourcing contract passed to Accenture when that company later acquired CustomerWorks. Mr. Louth's expert qualifications were accepted by BCUC in both of these cases.

Mr. Louth's expert qualifications have also been accepted by the Ontario Energy Board, to whom he has provided expert testimony in connection with Enbridge Gas Utility's outsourcing of customer care and information technology functions to a subsidiary of Accenture.

Timing of the Work

Investigative work on the final phase of DLAI's assignment took place in the months of October 2003 through January 2004. All BC Hydro documents reviewed by our consultants during these months were provided with the assurance that they were

current. All information provided by interviewees in BC Hydro, ABS and other organizations engaged by BC Hydro in connection with the outsourcing arrangements, was submitted on the same understanding.

The opinions expressed in this final report are based on DLAI's perception of the outsourcing project status that existed on January 22, 2004.

Additional Information

Our interim report described the history of the organizational context in which customer care, information technology services and other functions were outsourced by BC Hydro. It also described the information we reviewed in the course of our work. We do not feel it is necessary to repeat this information in the final document, with the exception of:

- Figure 1 which shows the services outsourced to ABS and the LOBs affected and,
- Appendix B which provides a synopsis of the outsourcing arrangements.

Both the figure and the appendix have been extracted from the interim report and are attached only to provide a framework for our final findings.

Figure 1 – Services transferred and LOBs affected

Services Transferred	Lines of Business Affected
• Customer Care	• Generation
• Technology Services	• Distribution
• Human Resources	• Transmission
• Financial Services	• Engineering Services
• Purchasing	• Field Services
• Disbursements	• Powerex
• Other Support Services	• Corporate Resources

It is important to understand the impact of the transfer of these services as it relates to the day-to-day fulfillment of responsibilities by each of the stakeholders. In particular, the reader should realize that notwithstanding outsourcing of procedures, ultimate control of the underlying processes remains with BC Hydro.

Only transactional responsibility for each of these services was transferred to ABS when the outsourcing arrangement was implemented. The lines of business within the utility retain responsibility for the functions generating these transactions and the results of transaction processing. For instance, though customer care transactions are now handled by ABS, responsibility for overall customer care policy, performance and service levels is retained by the Distribution LOB within BC Hydro.

Use of Acronyms

For reasons of brevity, we used a series of acronyms throughout the interim report. These will be used again in this final document and are shown in Figure 2 on the next page.

Figure 2 – Acronyms

“BCH” or “the utility” = BC Hydro	“DLAI” = Douglas Louth Associates Inc.
“ABS” = Accenture Business Services	“LOB” = Line of Business within BC Hydro
“BCHSAC” = BC Hydro Services Asset Corporation	“MAS” = Minimum Aggregate Spend (by BC Hydro)
“BCTC” = BC Transmission Company	“MSA” = The Master Services Agreement between BCH and Accenture
“BCUC” = BC Utilities Commission	“CIS” = Customer Information System

Disclaimer

It is important to note that DLAI’s consultants have made every effort to verify the accuracy and completeness of documents provided to us, and the comments expressed by those we have interviewed in the course of our work. However, to a great extent we have to rely on information provided by BC Hydro and ABS. Our work does not in any way constitute an audit or a detailed financial analysis of the outsourcing arrangements. We were not required to carry out such work and do not intend that it be reviewed as such.

3. SUMMARY OF DLAI’S OPINION

In order to provide the reader with an overview of what is to follow, this section contains an “executive summary” of our findings. Our intention is to provide only an overview of the many issues addressed in detail in subsequent paragraphs, together with high level substantiation of our opinion.

We strongly urge the reader to examine later sections of the document in order to understand the full rationale for, and extent of, our conclusions.

Our overall opinion is that the outsourcing arrangement with ABS was a desirable strategy for the utility to pursue. At a minimum-value level, we believe it provides the mechanism for the utility to avoid inflation and indeed to reduce its current costs for the services that make up the nucleus of the support provided by ABS. At a maximum-value level, it allows BC Hydro to manage its overall costs on these services while at the same time increasing its organizational efficiency and freeing resources to concentrate on its core business.

BC Hydro itself set out clear objectives for itself in deciding to outsource a range of services. We discussed these objectives with a number of persons with whom we conducted interviews in the second phase of our work. As can be seen from Figure 3, we believe Hydro's goals have been substantially met.

Figure 3 – Analysis of BC Hydro's Objectives

Original Objective	Percentage of Interviewees Considering Objectives to Have Been Met	DLAI's Opinion
Reduce Operating Costs	90%	Yes for 2003 costs. Longer term depends on management of services and relationship with ABS
Achieve Positive Organizational Change	81%	Yes
Focus on Core Business	72%	Yes
Create a More Viable Service Cost Structure	28%	Yes, but will need continued management
Conserve Capital	6%	Yes

In addition, there are many positive aspects of the outsourcing arrangement. BC Hydro and ABS have now been acting successfully as service partners for ten months. During this period, the relationship between the two parties has begun to mature positively and a number of milestones have been successfully passed:

- Service levels to the customer community have been preserved;
- Costs for those services covered by the outsourcing agreement are close to plan and budgets for the first year of operation. If the plan is realized for the full fiscal year, savings over those cost forecast by BC Hydro for 2003/2004 without the benefit of outsourcing will amount to approximately \$ 8.3m or 5.35%;
- The new CIS software system was installed on time (January 1, 2004) within BC Hydro's budget;
- Contract governance processes are in place and are, to a large extent, effective;
- We have been told that customer satisfaction levels remain high, and
- ABS has survived BC Hydro startup and is beginning to expand its business.

It is fair to say that in January 2003 DLAI was originally skeptical that so much could be achieved in such a relatively short time. The utility has in fact achieved a smoother transition to an outsourcing environment than most of DLAI's previous clients, due in no small part to its own organization and quality of effort.

In short, BC Hydro has achieved much in the first ten months of the ABS contract.

Notwithstanding its current level of achievement, DLAI believes BC Hydro still needs to address a number of issues, resolution of which will determine the ultimate level of success and benefit to the utility's ratepayers. These issues include:

- Rationalization of service level metrics and demerits to a point where measurement of ABS' performance is maintained, but metrics are directly related to benefit to the utility and its ratepayers;
- Finalization of a pricing model favourable to BC Hydro to replace the present transitional price structure that expires in March 2004;
- Simulation of the impact of predictable marketplace changes over the next ten years on prices and metrics. This task should be targeted at the desire to ensure that BC Hydro's position remains flexible and the overall desirability of the pricing model remains positive;
- Testing of this new model against comparable charges being incurred by other utilities who have outsourced comparable services;
- Strict control of costs, additional to those covered in the MSA. These costs can stem from a number of sources; they can be significant, and they have begun to surface in the first year of operations;
- Management of overall costs in order to achieve projected savings over the ten-year term of the ABS contract. Savings should be evaluated against the business case originally presented to, and approved by, the BC Hydro Board;
- Early preparation of a data base of costs and service levels that can be used in price and service benchmarks to be completed in 2006;
- Preservation of the greatest possible level of freedom of action available to BC Hydro in the service areas covered by the outsourcing arrangements;
- Completion of the necessary cultural change within the utility related to the transfer of responsibilities to ABS, and
- Progress from the present schedule of transitional activities to a more final process;

The body of our report expands upon the reasons for our identification of these issues. Where appropriate, it also suggests action steps that DLAI feels the utility should consider in order to address them.

To reiterate, the commentary above is a summary of our opinion. Full details of the rationale for our statements and the fact base underlying them are contained in later sections of this final report.

4. SUMMARY OF WORK COMPLETED IN PHASE TWO

At the beginning of the second phase of the project, Mr. Louth and Ms. Jay Grewal of BC Hydro jointly prepared a work plan to address the completion of DLAI's assignment. This work plan is attached for reference as Appendix C.

In summary, there were four major stages of work, namely:

1. **Review of new documentation.** A list of the new documents reviewed in the course of the second phase of our work is shown as Appendix D.
2. **Interviews with managers at BC Hydro and ABS.** An interview list is attached as Appendix E. All interviews were conducted during the period October through December 2003. In many cases, follow-up interviews were required to verify findings following initial interviews. These took place during November and December 2003, and January 2004.
3. **Analysis of data and development of draft final findings.** A draft of our findings was discussed with BC Hydro at review sessions held on January 19 and 22, 2004. During these discussions, we took the opportunity to verify the accuracy of the facts underlying our findings.
4. **Preparation of the final report.** The content and conclusions of the report were discussed, and the related facts verified, during further meetings with BC Hydro in mid-February 2004.

Our work on these tasks was not necessarily consecutive in nature. We discussed our findings as they emerged and continually back-tracked to verify our fact base and seek BC Hydro's response to our conclusions. This allowed us to develop a high level of confidence that our ultimate opinions are based on a correct reading of each situation.

We gratefully acknowledge the full cooperation we received from managers and staff at BC Hydro, ABS, Accenture and other parties involved in the outsourcing project. As a result of their participation and assistance, we are confident that we developed a fact base that is sufficiently comprehensive to support the opinions contained in both of our reports.

5. ORGANIZATION OF FINAL FINDINGS

Again, we will not repeat the conclusions regarding the initial status of the outsourcing arrangement that were covered in our interim report. To achieve complete understanding of our opinion, we urge the reader to review the interim document before reading this

final report. Only in this way can a complete understanding of DLAI's response to its terms of reference be achieved.

In subsequent sections of this report we will describe our understanding of the status of the outsourcing arrangements as at January 22, 2004. In presenting our overall findings, we will identify issues that we feel either influence the efficacy of the current contractual arrangements or have not currently been addressed.

In the course of examination of these issues, for each area identified we will address the status, the potential impact for BC Hydro and our findings. Where appropriate, we will provide BC Hydro's response in situations where it does not agree with our findings. Lastly, again where appropriate, we will summarize activities that we feel BC Hydro should undertake to continue to monitor and manage the outsourcing agreement.

6. ISSUES OUTSTANDING FROM DLAI'S INTERIM REPORT

In our interim report presented in May 2003, DLAI identified a number of issues that it contended could not be thoroughly reviewed until more time had elapsed and the service being provided by ABS had matured to a more final status. These issues are restated in Figure 4.

Figure 4 – Residual issues from interim report

Issue	Report Section Reference
Overall status of BC Hydro's relationship with ABS	8, 9, 13
Levels of service being provided by ABS	8, 9
Impact of transitional pricing model	8, 10, 12
Effectiveness of the (then) new relationship governance model	8, 13
Progress towards more comprehensive service level standards	8, 13
Potential impact of any special regulatory issues	10

Ten months have now passed since the implementation of the outsourcing agreement. Both BC Hydro and DLAI now have a considerably better appreciation of the deliverables from the relationship and it is appropriate for us to revisit the concerns expressed in our interim report and to identify any new issues that have emerged.

Residual Issues That Have Been Resolved

Based on our most recent review of the outsourcing status we believe that, in four of the areas noted in Figure 4, residual questions have been resolved and the topic no longer represents an issue.

Based on interviews with both parties, **the status of the relationship between BC Hydro and ABS remains generally positive and the governance model appears to be working** as well as could be expected. In our interim report we stated our opinion that “BC Hydro is vulnerable unless it can quickly establish contract management procedures.” We are pleased to report that the utility did indeed establish such procedures and they appear to have been initially effective in measuring ABS’ services and protecting BC Hydro’s interests. As an example, in December 2003 the utility discovered an error in ABS’ reporting of a particular key customer service level. This error was immediately brought to ABS’ attention and remedial action was taken.

The governance model at BC Hydro will mature over time, as has been the case in most of DLAI’s other clients. In our opinion, the utility has established a good basis on which maturation can be achieved. BC Hydro is aware of the constant need to pay attention to governance and we are confident it will do so.

Again based on our review of performance, and with the exception of the instance noted above, **levels of service being provided by ABS are at least as good** as those achieved by BC Hydro before the implementation of the outsourcing agreement. When measured against the performance metrics established by the utility, ABS is now fulfilling its obligations. We have been told by the utility that, in the first nine months of operation, no penalties to ABS were merited on the basis of sub-standard performance.

At the same time, customer satisfaction surveys show general satisfaction with service in areas related to the customer care function. Though a somewhat suspect measure (those customers with bad experience to report tend to dominate the respondents) such surveys do highlight the level of dissatisfaction if this is high. We are told that measurable customer dissatisfaction is not evident.

BC Hydro is still working on refinement and extension of the scope of its service level metrics. DLAI continues to see this as a worthwhile undertaking. However, we consider that, unless the process is carefully managed, the end result will be only a more comprehensive set of measurement tools. In our opinion, service levels are currently being adequately addressed and more measures will not likely lead to significant improvement of service level performance. There may indeed be a case for rationalization and reduction of service level metrics. We will discuss this issue further in subsequent sections.

Pages 34 and 35 of our interim report describe our overall opinion regarding BC Hydro’s potential vulnerability to regulatory review. Based on our latest evaluation of the outsourcing arrangements, we have no reason to change the commentary provided at that time.

We have not seen the utility's rate application documents and are therefore unable to comment on whether or not the issues we identified have been addressed. However, given the fact that submissions to BCUC have been made and the fact that we have not identified any new regulatory issues, **regulatory vulnerability has been removed from our current list as an issue to be resolved.**

Residual Issues Still Considered to be Outstanding

Of the six issues carried forward from our interim report, two issues still remain to be resolved. These are:

- The continued absence of a final pricing model and the related potential impact on BC Hydro's savings projections, and
- BC Hydro's progress towards effective service level standards.

The impact of these issues will be addressed in detail in later sections of this report and will be examined in the context of new issues that have emerged.

7. NEW ISSUES THAT HAVE EMERGED AS A RESULT OF DLAI'S CURRENT WORK

DLAI's most recent work has concentrated on evaluation of the emerging value of the outsourcing arrangements to BC Hydro and its ratepayers. As we have previously stated, there are many positive accomplishments to report, on the achievement of which the utility should be congratulated. The outsourcing arrangement has made a successful start and all signs are that it will continue to contribute to the business efficiency and effectiveness of the organization.

However, in our firm's opinion, there remain a number of issues needing resolution before the ultimate value of the arrangements can be determined. These are:

- Finalization of a favourable pricing model to replace the present transitional price structure that expires in March 2004. This was a residual issue first identified in our interim report;
- Rationalization of service level metrics to a point where measurement of ABS' performance is directly related to benefit to the utility and its ratepayers. This too was identified in our interim report, but emerging circumstances have changed the emphasis of the issue from number of metrics to the value of those metrics;
- Strict control of future costs, additional to those covered in the MSA. These costs are beginning to surface;
- Management of overall costs in order to achieve projected savings over the ten-year term of the ABS contract;
- Preservation of the greatest possible level of freedom of action available to BC Hydro in the service areas covered by the outsourcing arrangements;

- Progress from the present schedule of transitional activities to a more final process;
- Completion of the cultural change within the utility related to the transfer of responsibilities to ABS.

In our opinion, none of these issues constitutes a reason to question the overall validity of the arrangements made between BC Hydro and ABS. In some cases, the issue has arisen as the relationship has matured and the utility's use of ABS' services has opened avenues to review its overall opportunities to realize its initial objectives. In other cases, we suggest that BC Hydro is simply in the process of addressing start-up issues that, in our experience, normally arise in new arrangements of this kind.

Nonetheless, we consider these issues to be of a serious nature. A separate section in subsequent pages of this report will be devoted to each one of them and final sections will suggest action steps that we consider BC Hydro should take to mitigate any negative effects.

8. FINALIZATION OF A PRICING MODEL

When the outsourcing arrangements with ABS were first implemented, BC Hydro had not completed its pricing model. A transitional model was put into place to serve for the first year of the contract. Hydro has informed us that work to complete the final model is scheduled to be completed by March 31st 2004 and final pricing will be implemented on the first anniversary of contract signing.

We will review the impact of both pricing models in following paragraphs.

The Transitional Pricing Model

In the transitional pricing model currently being used, the price categories are very broad. For instance, the utility incurs monthly charges based on volume of "population" in the following areas:

- an all inclusive charge per account for all call centre and customer-care functions,
- a separate all inclusive charge per account for billing and collection services,
- a charge for each e-mail address used,
- a charge for ABS support of each laptop,
- etc.

There are currently 18 such "population-based" cost items and charges are effectively fixed at a top-line unit level, the gross amount changing only when the population increases or decreases.

There are another 22 pricing categories that are "usage-based," for instance a charge for every supplier invoice processed and for each megabyte used per month for

memory consumed by the utility’s e-mail service. Lastly, there are 8 “fixed-fee” price categories and 12 price categories that attract either a negotiated fee or some other activity-related cost.

Examples of charges incurred by BC Hydro are shown in Figure 5, which contains columns for ABS prices and the fully loaded cost to the utility. In this figure:

- The fully loaded cost includes the ABS charge, and
- The “ABS Cost” shown in the figure reflects the guaranteed savings committed to by ABS in relation to 2002/03 costs

Figure 5 – Examples of transitional prices

Cost Element	Category	Basis	ABS Cost (\$)	Fully Loaded Cost (\$)
Call centre, customer care	Population	Per acct/mth	Redacted	1.23
Billing , receivables	Population	Per acct/mth	Redacted	1.80
Meter reading	Population	Per acct/mth	Redacted	1.09
E-mail address	Population	Per acct/mth	Redacted	18.13
Laptop support	Population	Per acct/mth	Redacted	438.31
Supplier invoice processed	Usage	Per invoice	Redacted	14.42
E-mail memory use	Usage	Per 20mb/mth	Redacted	1.86
Application maintenance	Fixed	Per hour	Redacted	99.05

Final volumes of cost unit usage for the first year of the outsourcing contract will not be available until April 2004. In the absence of definition of final volumes, it is impossible for DLAI to assess the impact of the transitional pricing model that the utility has decided to use. However, given the fact prices charged by ABS are based on fiscal 2002/03 costs, BC Hydro will pay more in aggregate for any use of population-based units over the volumes experienced in that year, if volumes have increased. For example, 8,000 new customers for the utility at the start of any contract year will result in additional ABS customer care charges of <Redacted> over currently projected charges for that year.

It is important to note that, if there is under-use of any population- or usage-based units, BC Hydro will pay only for the units used. If such under-use causes the annual total of the MAS obligation not to be met for services covered by the MSA, the utility can bring costs incurred for other ABS or Accenture services under the umbrella of the MAS. It can accrue such “MAS credits” over the ten-year term of the contract.

Use of population-based pricing also calls into question the appropriateness of incremental charges for over use. For instance, is it reasonable for ABS to charge <Redacted> per year for customer care services for each new customer? ABS’ own incremental cost of processing one such customer, using an existing call centre with

spare capacity, is not likely to approach \$12 per year. Is it therefore reasonable for BC Hydro to absorb close to 100% of a notional incremental cost to ABS?

BC Hydro has undoubtedly incurred incremental costs under the transitional pricing model. For instance, the number of customers has increased along with the population of the province. We have been told that approximately 8,000 new customers have been added in the current year. DLAI has calculated that this has resulted in additional monthly costs for each of each new customer as shown in figure 6. However, to date, these additional costs have been absorbed under the MAS. We understand that similar incremental costs have been incurred in other “population-based” categories where volumes have increased.

BC Hydro recognizes that there is an issue concerning incremental costs and is currently working to eliminate inequities.

Figure 6 – Incremental customer-care costs

Cost Element	Monthly Loaded Incremental Cost	Gross Annual Incremental Cost
Call centre, customer care	Redacted	Redacted
Billing, receivables	Redacted	Redacted
Meter reading	Redacted	Redacted

Like the transitional price structure, the MAS is based on fiscal 2002/03 costs. BC Hydro was very close to its target regarding charges against the MAS at the end of December 2003. This fact suggests that, despite incremental additional costs, application of the transitional pricing model will result in savings when compared to costs that would have been incurred in the first year, had the outsourcing contract not been in place. In fact, if the MAS continues to be matched the guaranteed savings of 5.35% of 2002/03 projected costs will be realized.

In the context of projected fiscal 2003/04 costs therefore, the transitional pricing model can be expected to be effective. The issue then becomes that of projection of the impact of the final pricing model.

The Final Pricing Model

The principles of the final pricing model were specified in the MSA and are shown in Appendix F. It is our understanding that the emphasis on pricing in the final model will still continue to be set largely at the all-inclusive levels used in the transitional pricing model. Flat rates will still be set for primary functions and will be population-based to a large degree. However, price bands based on volumes will be developed for each price category and this should to some extent mitigate the incremental costs sometimes incurred in the first year of the outsourcing contract.

BC Hydro maintains that consistent unit-pricing principles will be followed in the final model, but DLAI is unable to confirm that this will be the case, since the model is not yet complete. However, we find it reasonable to assume that the end result will at worst closely resemble the original pricing design, since major change would necessitate re-negotiation of many clauses in the MSA and this outcome is not sought by either party.

Notwithstanding this comment, we consider it necessary to reiterate our belief that BC Hydro should not necessarily simply build on the transitional price categories to set final prices. We believe each price category should be examined, along with proposed price bands, to determine overall effectiveness and value to the utility. BC Hydro should use the results of this examination to achieve the best possible pricing arrangement with ABS.

Purely as an example of the potential dollar impact of the volume bands contained in the pricing model, we have taken examples of monthly charges for unit use from another of our clients whose information is in the public domain. This client has outsourced its customer care functions and uses outsourced call centres to serve a client base roughly equivalent in size to BC Hydro.

We have used the price of a call to a customer service representative (CSR) as the basis of our example. The price of such a call for our client is on a sliding scale of charges, based on minimum and maximum usage levels, similar to the arrangement that we understand will be chosen in 2004 by BC Hydro.

Figure 7 shows the impact of call volume fluctuation on this client for four typical periods in 2001. The clients target range for calls was 220,000 to 270,000 per period.

Figure 7 – Impact of Call Volume Fluctuation

	Unit Price (cents)	Spring	Summer	Fall	Winter
Number of Calls (000)		277	221	319	520
Discount Below Target	(.30)				
Within Target Range	10.51		Yes		
Premium Above Target	.25	Yes		Yes	Yes
Period (three month) Unit Charge (\$000)		\$2,711	\$2,061	\$3,384	\$5,517

Using this model, the utility paid over \$14 million for CSR calls in the year. Had it initially set its maximum target range as little as 10,000 calls per period higher, it would have saved over \$130,000 in the year on this single service category alone.

We do not suggest BC Hydro will set its unit prices at comparable levels or experience such pronounced seasonable volume fluctuation. However, this table is nonetheless valid in terms of demonstration of one potential impact of the final unit pricing model expected to be chosen by BC Hydro. It demonstrates the care that must be taken by the utility to model its pricing alternatives in order to measure potential impact.

A number of BC Hydro's final service unit charges will be based not on transactions such as a call to a call centre but rather on the number of units that ABS could be expected to provide. Examples of this type of charge might be number of network servers maintained, number of employees on the payroll etc. These charges pose another dimension of contract management for BC Hydro. Again using the example of network servers, the utility's project management group will have to ensure that existing servers are optimally utilized and resist unnecessary proliferation in the LOB's.

Given the existence of a ten-year contract with ABS, BC Hydro will also need to consider a number of other external variables in designing the final pricing model. For instance:

- **Electricity re-sellers (aggregators) may enter the marketplace.** We understand the opening of the electricity supply market can be allowed under the new BC Energy Policy. If this happens, it could cause BC Hydro to lose a significant part of its revenue base while having to maintain records and provide some services for the customers who have switched to the re-seller. This circumstance has occurred in other provinces where the energy market has been opened to competition.

If these circumstances were to occur in British Columbia before 2012, pricing based on a monthly cost-per-customer could become extremely unattractive. It is possible that customer revenue could be lost while the full cost of customer service continues.

DLAI believes the impact of providing only partial service to customers has to be evaluated by BC Hydro before finalizing its final pricing model. Flexibility to adjust to such a situation has to be built into the model to protect the utility to the greatest extent possible.

- **Price decreases will likely continue to occur in the technology marketplace.** This should make replacement hardware and software cheaper for ABS to maintain. We suggest that BC Hydro should ensure flexibility in its final pricing structure to allow it to benefit to a meaningful extent from such cost reduction. Flat monthly charges based on 2003/04 costs to support each unit supported by ABS will not achieve such flexibility in DLAI's opinion.

- **Competitive pressures and new entrants may force outsourcers to reduce prices as a whole.** BC Hydro is protected to some extent in this regard because the MSA forces ABS place its prices in the best quartile following a benchmarking process to be carried out in 2006 and subsequent years. ABS also has to honour a “most favoured customer” clause in the MSA.

To enable these contract clauses, we believe the utility should ensure that its new pricing model lends itself to direct benchmarking against other utilities.

- **Under the transitional pricing model, BC Hydro may be paying more than other utilities for some of ABS’ services.** BC Hydro should benchmark its new pricing model against that of other outsourced utilities as part of the final model evaluation process.

DLAI believes that the final pricing model should not be introduced until such time as the impact of all of these variables has been formally assessed and maximum flexibility built in to address future technology and marketplace changes. The utility cannot be expected to achieve total protection from present and future market conditions. It should however be confident that all realistic scenarios have been evaluated before it becomes committed to a price tariff.

In summary, DLAI believes that BC Hydro should assess the impact of its final pricing model against both direct charges from ABS and possible changes in the energy and technology marketplaces over the 10-year term of the contract. Only when the impact of all reasonable variables has been assessed should the model be finalized.

If it is to control its future costs effectively, it is essential that BC Hydro implements the optimum pricing model in 2004. From that point on it will also need to manage its use of service units very carefully in order to ensure it is receiving the best terms possible and to protect itself against repetitive overages. This will be increasingly difficult over the ten-year timeframe of the Accenture contract, when many aspects of service unit use, and therefore cost, are likely to be affected by circumstances outside the utility’s control.

9. RATIONALIZATION OF SERVICE LEVEL METRICS

Under the terms of the MSA, BC Hydro and ABS are committed to negotiate standards for levels of service against which ABS’ performance will be measured. These are referred to in the contract as the “service level metrics.”

The service level metrics may, at BC Hydro’s discretion, be associated with “demerits.” These set financial penalties to be levied against ABS if the supplier does not meet the minimum level of acceptable service. Continued non-performance on ABS’ part could lead, as a last resort, to cancellation of the contract for service. Demerits have been applied by BC Hydro to every category of service provided by ABS.

When used together, metrics and demerits provide a strong tool by which BC Hydro can measure and to some extent control ABS' performance under the outsourcing contract. Under the current transitional arrangements with ABS, the utility is using this level of control effectively in DLAI's opinion. On a monthly basis, service levels are reported and ABS' performance is evaluated by the utility. BC Hydro reports that its level of control has been tested to the extent that some instances have been identified where service levels have not been acceptable. Where this has occurred, corrective measures have been taken.

As we commented in our interim report, when the ABS contract was signed by BC Hydro, performance metrics were in base-line form. Work to refine these measures has proceeded in the intervening nine months and the utility introduced an initial set of more comprehensive metrics in October 2003, with a final set of measures being implemented in April 2004.

The October metrics, known as the "six-month metrics," are now in place and form the present base for reporting by ABS on its monthly service levels. The number of service level metrics and demerits are currently broken down as follows:

- 83 service level metrics have been defined in total.
- 24 demerits have been assigned in total, of which:
 - 13 demerits relate to customer care functions.
 - 8 demerits relate to IT services
 - 3 demerits relate to other service categories

Even using these "six-month metrics" as a base, BC Hydro has more metrics in total than any other DLAI client. This is not surprising, given the scope of the outsourcing contract. However, it has fewer customer service metrics than most of our previous clients, and customer care makes up nearly half of the total value of the contract.

In our firm's experience, at the start of a relationship it is common for any utility outsourcing some of its functions to wish to measure as many aspects of the outsourcer's performance as possible. In the early months of an outsourcing arrangement, it is proper to review all aspects of service delivery so that improvements can be initiated where necessary. However, such micro-measurement entails significant reporting responsibility for the supplier (for which the outsourcer pays) and considerable time spent by the outsourcer in reviewing reports, refining responses and managing the implementation of change.

In our opinion, the relationship between BC Hydro and ABS has now matured to a point at which, instead of automatic implementation of further service metrics in April 2004, a review of all metrics should be initiated. This review should include both "six-month" and "twelve-month" metrics. The objective of such a review should be to assess each of the measures defined and establish the overall usefulness of each measure on the basis of benefit.

In this context, benefit can be defined in terms of criteria such as:

- criticality of service,
- maintenance of service levels,
- control of cost,
- impact on the customer,
- etc.

The outcome of such a review should be to arrive at a set of core measurements by which BC Hydro can best manage ABS' performance without onerous reporting requirements and within the most effective project management process.

A further major factor in any review of service metrics must be the mapping of each category of service to corresponding service prices. When the new pricing model has been developed by BC Hydro, it should be used as a base for the review of metrics to ensure that cost control of key elements of service has indeed been maintained.

We have been made aware that ABS is suggesting that the number of metrics should be reduced. We support such a suggestion so long as the final list of measurements is based on the benefit to BC Hydro, rather than convenience to its supplier.

10. CONTROL OF FUTURE COSTS

It is DLAI's opinion that, over the ten-year term of the outsourcing arrangement, BC Hydro will incur significant costs outside the contract with ABS, but related to the services which ABS provides.

Both parties to the utility's outsourcing contract recognized this probability and BC Hydro built flexible conditions into the MSA designed to help achieve cost measurement and control to the extent possible. However, these conditions do not change the fact that it remains BC Hydro's responsibility to control future costs, as it has done in the past.

When examining the potential extent and timing of future costs it is important to realize that:

- Investment in processes, systems and technology designed to serve stakeholders in BC Hydro will continue to be a continuous process, as it has been for many years. The outsourcing arrangement sought to control then-present costs, not obviate the need for future investment.
- Some future costs that will be incurred by the utility while the outsourcing contract is in place can properly be considered to be outside the scope of that contract.
- Many of these costs would have been incurred by BC Hydro irrespective of outsourcing,

- Under any arrangement as comprehensive as that between ABS and BC Hydro it is unrealistic to think that all possible future costs can be predicted prior to contract signing, and
- BC Hydro is not contractually committed to make any additional investment unless it chooses to do so.

Notwithstanding these facts, future investments required to be made by the utility are likely to be significant.

To demonstrate potential impact, DLAI has identified what it considers to be potential major sources of future cost to BC Hydro in Figure 8, which also contains DLAI’s opinion regarding the potential dollar impact of such costs. In preparing the figure, we have considered potential costs of \$5 million to \$10 million over a ten year timeframe to be a “medium” impact.

Figure 8 – Sources of future costs

Source of Cost	Likelihood of Occurrence	Potential \$ Impact
• Overspending on ABS-delivered support services	High	Low
• Change orders	Certain	Medium/High
• CIS maintenance and/or improvement	Certain	Medium/High
• Other system maintenance activities	Certain	Medium
• New systems or technology implementation	High	High
• Process change	Medium	Low/Medium
• Marketplace change	Medium	High

A number of costs from these sources are already occurring in the first year of the outsourcing agreement. For instance:

- Nearly \$1 million in change order costs had been incurred by end-December 2003 and approximately another \$1.1 million had been approved.
- The new CIS, made operational in the last days of December 2003, had only a one-month performance warranty from ABS. Significant change orders to modify the system are now under review and on-going maintenance beyond February 2004 will undoubtedly be necessary. BC Hydro’s current estimate of the cost of this support is \$3.525 million.

- Increases in server capacity and data storage requirements have led to additional charges to BC Hydro. The utility’s costs in the first nine months of the contract have amounted to approximately \$302,000 in this category.
- New or replacement systems are being considered for at least two LOBs, at a budgeted cost still to be determined.

DLAI does not suggest that these additional costs are unjustified. In fact, we have no means of determining whether or not this is the case and were not required to do so under our terms of reference. They do however illustrate the potential extent of future costs to the utility outside the services specified in the outsourcing agreement.

DLAI believes it to be imperative that BC Hydro formally controls such additional costs. We also believe that the utility already has many of the processes in place to do so, since decisions to make future investments are little different from those used in the past despite the presence of a new outsourcing arrangement.

We do believe however that a number of new factors may influence the utility’s performance in this regard. These are described in succeeding paragraphs.

Reliance on the Flexibility of the Minimum Aggregate Spend (MAS)

The costs implicit in the MAS are reproduced from the outsourcing contract in Figure 9. The “savings” figures relate to the difference between 2003/04 costs for the services included in the MSA and those that were projected by the utility for matching operations if 2003 costs remained constant and the outsourcing contract had not been signed.

Figure 9 – MAS and guaranteed savings

Year	MAS	2003 Costs	Guaranteed Savings	Percentage Savings
2003	147,356	155,691	8,335	5.35
2004	137,984	155,691	17,707	11.37
2005	131,300	155,691	24,391	15.67
2006	126,822	155,691	28,869	18.54
2007	Redacted	155,691	Redacted	Redacted
2008	Redacted	155,691	Redacted	Redacted
2009	Redacted	155,691	Redacted	Redacted
2010	Redacted	155,691	Redacted	Redacted
2011	Redacted	155,691	Redacted	Redacted
2012	Redacted	155,691	Redacted	Redacted
Total	1,284,374	1,556,910	274,536	17.63

It should be noted that the MAS obligation will reduce each year to reflect the savings guaranteed by ABS. The MAS amount for 2004/05 will be approximately \$10 million less than that for the current year, as shown in Figure 9. This number will be further reduced when BCTC assumes its own portion of costs and the savings guaranteed in the MSA.

In considering the implications of the MAS it is important to note that it represents the base **obligation** BC Hydro assumes to pay for ABS' services. It in no way represents a maximum cost to the utility. Thus, although the utility's obligation reduces over ten years, the actual charges invoiced by ABS do not necessarily do so, and are in fact very likely to increase.

For example, if 2004/05 charges from ABS are the same as those projected to be incurred by BC Hydro in 2003/04, the utility will in fact over spend against the MAS by approximately \$10 million. Even if 2004/05 costs are not exceeded in subsequent years, the same principal applies in subsequent years. The impact of this principal is demonstrated in Figure 10. All sums shown in this Figure are expressed in million dollars.

Figure 10 – Spending versus obligation

Year	Obligation (MAS)	2003/04 Estimated Costs	(Under)/Over Obligation
2003	147,356	146,000	(1,356)
2004	137,984	146,000	8,016
2005	131,300	146,000	14,700
2006	126,822	146,000	19,178
2007	Redacted	146,000	Redacted
2008	Redacted	146,000	Redacted
2009	Redacted	146,000	Redacted
2010	Redacted	146,000	Redacted
2011	Redacted	146,000	Redacted
2012	Redacted	146,000	Redacted

DLAI believes that BC Hydro will find it difficult to consistently reduce its actual charges from ABS over a ten-year period. It is likely therefore to spend considerably more than its MAS obligation as the life span of the contract advances.

Notwithstanding the impact of this projection, if it can reduce ABS' charges, BC Hydro does have the possibility of defraying some of its future additional costs because of its ability to offset these costs against under spending on the MAS. The outsourcing contract allows the utility to "fill-in" the cost of additional services purchased from ABS or Accenture to offset such under spending. Offsets may be

accrued from year-to-year during the ten years of the arrangement. For instance, suppose the cost of ABS-delivered support services in a year amounts to \$3 million less than the MAS, and CIS maintenance costs amount to \$5 million in the same year. In these circumstances, \$3 million of the CIS-related costs can be credited to the MAS spend and the remaining \$2 million accrued for similar consideration in future years.

BC Hydro expects to spend approximately the obligated MAS amount (\$147 million) on ABS-delivered support services in 2003/04 and there is likely to be little room to fill-in the cost of any additional activities. Credits for all additional costs incurred with ABS or Accenture in the current year will therefore have to be carried forward, though invoices from ABS for these services will have been paid.

It is fair to say that guaranteed savings described in the outsourcing contract are reflected in the declining obligation of the MAS. However, additional costs for ABS or Accenture services can only be included under the MAS if the actual cost of contracted services reduces significantly. DLAI considers this to be an unlikely event, given the relative stability of the utility's cost structure and growth trends in the province. DLAI therefore believes it to be safe to assume that BC Hydro's opportunity to defray future costs under the MAS will not be great. In fact, we believe such opportunity will effectively disappear over time if demographic trends continue. In approving and controlling future costs, DLAI believes BC Hydro should largely discount such a possibility.

Impact of Incremental Costs

Under the final pricing model we have been told BC Hydro will implement in 2004/05, there will still be many population-based prices. These will continue to be based on the carve-out of original costs by Deloitte and Touche. Thus, adding one new laptop computer or one more customer will involve payment of a fixed cost based on the cost of servicing that transaction in 2002/03. Such an arrangement causes us to raise a number of questions. For instance:

- Is a charge of \$438 per month reasonable for a new laptop, which is likely to be much less expensive to maintain than its older equivalents and certainly will cost less to support than its older counterparts?
- Is an incremental charge of <Redacted> per month reasonable to add a new customer, when all infrastructure and services to similarly serve 1.8 million customers is already in place?

Figure 11 on the next page shows a top line analysis of the additional cost to BC Hydro and ABS of adding a new customer, and demonstrates the incremental cost implications.

Figure 11 – ABS cost of adding a new customer

Function	Incremental Cost to BCH Under Transitional Pricing Model	Assumed Incremental Cost to ABS
Read meter	Redacted per read	Minimal
Bill and manage receivable	Redacted per customer per month	Minimal (e.g. postage, bank charge)
Customer contact	Redacted per customer per month	Minimal, uses existing capacity

Depending on the utility’s definition of pricing bands, the effect of incremental costs could be mitigated to some extent. However, such mitigation is not certain. DLAI believes BC Hydro must take formal measures to ensure that such costs do not in themselves become a future charge on BC Hydro, outside the scope of the MSA.

Awareness of the “Country Club Syndrome”

Using the analogy of a country club, the MAS establishes an annual price that BCH (the club member) is obligated to pay ABS (the club) whether or not the club’s services are used. If services are not used in the normal course of events, and the obligation cannot be entirely offset, the club allows the member to fill in other services purchased from the club to meet his committed annual payment.

The member thus becomes predisposed to use additional services of the club as a first-resort, because he is paying for them anyway. To “save money” the club, knowing the members situation, may deliberately seek to identify such additional services for his use. The member is possibly less diligent than usual about the overall cost and value of those services.

Such a predisposition on BC Hydro’s part could cause it to use Accenture and ABS resources on a cost-avoidance basis rather than on the basis of solution quality or value-for-money. This could cause the utility to incur future costs that are higher than necessary. DLAI suggests that, wherever possible, the worth of additional services should be measured by BC Hydro on an overall-value basis, based on competitive tendering. The utility should resist any tendency toward default service provision.

This issue will be discussed in more depth in Section 12 of this report.

Management of the Strategic Position of Accenture and ABS

Accenture and ABS between them now own the technology, the human resources and the processes needed to service BC Hydro under the outsourcing agreement. They

are therefore strategically best positioned to provide the majority of the additional services the utility will require throughout the next ten years.

This relationship with BC Hydro as a client affords both ABS and Accenture the opportunity to secure additional revenue because of their ownership position, particularly from “routine” change orders and technology based work. The MSA does allow the utility to go to tender for additional services, but Accenture and ABS will usually occupy the “inside track” for much of such work.

Accenture is traditionally not the lowest cost provider of services in the marketplace. Further, ABS has limited incentive to reduce the utility’s costs unless it also improves its own revenue stream. The impact of the pre-eminent position of these companies in servicing BC Hydro will have to be carefully managed by the utility. Again, DLAI suggests that, wherever possible, the worth of additional services should be based on competitive tendering.

Again, this issue will be discussed in more depth in Section 12 of this report.

Despite its exposure to additional costs, BC Hydro is of course in complete control of their extent. In the last analysis, it does not have to approve additional spending unless it chooses to do so.

Nonetheless, DLAI believes that significant future cost will be incurred by BC Hydro. We feel the utility will need to exercise continual vigilance in respect of such costs in the context of the ABS relationship. It must also recognize that few, if any, new costs will ultimately be accommodated within the MAS and seek other ways to minimize its investment within the constraints of the outsourcing contract.

11. ACHIEVEMENT OF SAVINGS

The business case supporting the outsourcing decision was first presented to the Board of Directors of BC Hydro in late 2002. It was approved by the board at that time.

The business case has since been amended by the utility to reflect emerging service variables and a new version was finalized in October 2003. DLAI has been told that the new version of the business case is considered to be a working paper and has not been re-presented to the board because it does not change the fundamental costs and benefits of the outsourcing arrangement.

Both the original and the amended business cases set out the anticipated costs of the arrangement with ABS and measure these against comparable costs that would have been incurred in the absence of an outsourcing arrangement. Both documents then establish the anticipated savings from the ABS arrangement and articulate the overall benefits

expected. Such savings were anticipated from a number of sources and were enumerated in a number of areas, including:

- Savings guaranteed by ABS in respect of support services specified in the MSA, when measured against fiscal 2002/03 costs. These savings amount to \$274 million over the life of the contract, but relate to continuation of present costs of service and not those that will actually occur;
- Savings accruing to BC Hydro because of its decision to outsource the final development stages and implementation of the new CIS to Accenture. These savings are largely attributable to risk avoidance;
- Savings on new technology achieved through rationalization of service provision;
- Placement of BC Hydro's service cost in the best quartile following 2006 benchmarks, or continuation of the present MAS if this is favourable to the utility;
- Savings on the cost of human resources through transfer to ABS of commitments relating to approximately 1,600 staff.

Over the ten-year term of the contract, it is safe to assume that BC Hydro will closely monitor the costs of the outsourcing arrangement. It is less certain that similar monitoring will be applied to the verification of savings.

In DLAI's opinion, such measurement is desirable since it can be used as the context for decisions on future spending and ultimately renewal of the ABS contract. Achievement of projected savings is also likely to be a subject of on-going review by regulatory authorities.

12. PRESERVATION OF BC HYDRO'S FREEDOM OF ACTION

For the foreseeable future, BC Hydro is committed to use systems, processes and technology approaches supported by ABS. These systems will serve a significant number of LOBs within the utility. BC Hydro no longer has the organization or staff to support future development or upgrading of those services that have been outsourced, so it cannot itself provide alternative solutions to those provided by ABS.

It is worthwhile to consider the impact of this situation under three headings.

New Developments

ABS and Accenture effectively own the outsourced functions, technology facilities and resources. Quite reasonably, they control access to them by outside suppliers. However, the MSA allows BC Hydro to tender for a range of development services and ABS is required to allow the chosen supplier access to its networks and technology. Two projects have recently been tendered and the responses are under consideration. If a third party supplier is chosen in either case, ABS' level of co-operation will be tested.

Improvement of Systems

In general terms, since it is already maintaining hardware and software relating to systems, ABS has the “inside track” in terms of maintenance and improvement projects. As time passes and ABS’ skill set increases with expanded knowledge of the systems and processes concerned, the strength of its position will also increase. It is likely to strenuously resist outside organizations intruding on its position. In this context, there has already been some resistance to the utility’s use of other outside organizations to provide software and technology services to the LOBs.

On-going Support of Technology Facilities

Based on our reading of the contract, responsibility for support of existing technology rests entirely with ABS. BC Hydro does not have any opportunity to assume even part of such responsibility without negotiation of major change to the MSA. Such change might have offsetting negative implications to the utility.

DLAI believes that, in terms of services offered under the outsourcing agreement, BC Hydro’s future freedom of action is constrained. The utility recognized this potential situation before the contract with ABS was signed, but felt the attendant risk was justified because of the positive financial aspects of the arrangement and suppliers’ leading edge position in the service and technology fields. It is now incumbent on Accenture and ABS to retain this position, and DLAI believes that the companies have many reasons to do so, in addition to a wish to service BC Hydro.

However, ABS’ resolve to act in BC Hydro’s best interests may be influenced by the fact that it has only limited incentives to improve BC Hydro’s performance. For instance:

- It has no contractual need to spend on any process improvements unless such improvement is to ABS’ full or partial benefit. *For example, why would ABS improve receivable collection times if it involved more cost to itself, even though BC Hydro’s revenue stream would be improved?*
- It need not seek to reduce volumes in areas where it is paid on the basis of use. *For example, why would ABS optimize networks to reduce the number of servers, when its income is based on numbers in use?*

Of course, BC Hydro can itself identify such improvements. However, they can only be implemented by mutual agreement and the extent of ABS’ “push-back” has not yet been tested.

DLAI believes that BC Hydro should immediately implement a number of policies designed to protect its freedom of action within the outsourcing arrangements. These might include the following:

- A policy requiring BC Hydro to go to tender for additional major services wherever practical, rather than defaulting to ABS or Accenture. This tendering should include maintenance and improvement as well as new development. To DLAI's knowledge, such a policy has already been established by the utility.
- Constant monitoring and protection of the utility's position, through formal, independent review of major decisions relating to the engagement of service providers under the outsourcing arrangements.
- A requirement to ensure formal measurement of new products and services based on quality, cost and value; rather than convenience or supplier pressure.

In short, BC Hydro should protect its independent position by strenuously resisting any attempt by ABS or Accenture to "lock-in" the utility as a customer beyond the extent of the outsourcing agreement.

13. COMPLETION OF CULTURAL CHANGE

We understand that all employee transfers from BC Hydro to ABS are now complete. Most new ABS employees have been working in their new roles for over nine months and, even though some still have a contractual right to relocate back to the utility, the new organization is to all intents and purposes final.

Unfortunately, physical transfer does not automatically signal commitment, either to the new organizational structure or to the new environment that has been created. Indeed, experience shows that many transferred employees will have adopted a "wait-and-see" attitude to their personal status.

Under the outsourcing arrangements, 1,600 persons have opted to move from the public to the private sector, with all of the challenges this entails. Despite the new environment, most of these employees are continuing to carry out duties and accept responsibilities that are virtually identical to their old situation. At the same time, those persons "left behind" in the LOBs are also carrying on with previous activities, with the exception of the fact that those who transferred are now operating at arms length and have to be treated as a supplier rather than a colleague.

In this situation, it is not surprising that the signatories to the outsourcing arrangements report that they are experiencing organizational culture shock. This has manifested itself in a spectrum of reactions ranging from confusion about relative responsibilities to a case of arbitrary changing of service level reporting mechanisms by ex-Hydro employees now working for ABS.

Despite these problems, DLAI believes the both ABS and BC Hydro have achieved much in the nine months since outsourcing began. Based on our prior experience, confusion about the roles of customer and supplier are common in such situations and will inevitably improve as the new relationship matures.

We understand that the parties are still in process of implementing a formal change management process in an attempt to address outstanding issues. We support this initiative and consider that all reasonable measures to complete cultural change are being taken. As discussed in the next section of this document, we also believe a timely completion of the transition stage of the relationship will have a positive affect on the employees and organizations concerned.

14. COMPLETION OF TRANSITION

BC Hydro, and presumably ABS, made a decision early in 2003 to treat the first year of operations under the outsourcing agreement as being one of transition. As previously reported, the utility is operating under a transitional pricing model and transitional service level metrics as this document is being written. Two pillars of the agreement from the utility's point of view are therefore incomplete.

There is a formal transition plan and, based on our examination, it is being followed. Indeed, its final tasks are nearly complete. However, in the absence of resolution of timing for incomplete tasks, particularly in respect of the pricing model, it is difficult for us to determine exactly when the transition phase will finish. There also appears to be no automatic triggering mechanism for such an event.

This lack of certainty appears also to be an issue with many of the LOBs with whom we have talked in the course of our assignment. To some of them, transition status indicates that BC Hydro is not entirely committed to outsourcing, or to its current provider. It gives some stakeholders the impression that even fundamental aspects of the arrangements are still subject to discussion and change. It is sometimes interpreted as providing an opportunity to modify contracted procedures to suit individual circumstances.

In our experience, such uncertainty leads to questions from uninitiated stakeholders such as:

- The overall status of the ABS relationship – *“is it still in a state of flux?”*
- The rules governing the consumption of ABS services – *“will the rules change in the near future?”*
- The prices being charged and the level of service being provided – *“are these likely to improve/get worse when the deal becomes firm?”*

In short, prolonged transition leads to uncertainty about the utility's overall commitment to the outsourcing arrangements as a whole and the impact it has on the LOBs.

DLAI believes there is much to be gained from a decision to end the transition phase directly the pricing model issue is resolved and service level metrics have been finalized.

Such a decision, and a publicized conversion to a permanent arrangement, should have a major positive effect on the level of commitment by LOBs and on the hastening of permanent culture change.

15. SUMMARY OF DLAI'S RECOMMENDATIONS FOR ACTION

Despite the identification of the issues described in previous sections of this report, DLAI believes that BC Hydro has achieved a commendable level of success in the first nine months of its implementation of the outsourcing arrangements with ABS. While precise measurement is impossible, we believe it has progressed at a rate not matched by many of our previous clients undertaking similar projects.

However, progress has to be maintained and current levels of service have to continue to be provided or improved. Costs have to continue to be controlled and value to both internal and external stakeholders realized. In this context, we believe we have justified a series of immediate actions that we believe BC Hydro should take to ensure continued success. These are:

- Rationalize performance metrics to point where they are significantly biased towards benefits to the utility and its ratepayers,
- Evaluate the new pricing model against not only improvement of previous cost structures but also potential impacts of marketplace changes,
- Before finalizing new pricing structures, compare the results for reasonableness by benchmarking against other utilities,
- Prepare now for 2006 pricing and service level benchmarks by collecting comparable data and variables on current internal performance,
- Carefully manage future costs, both inside and outside the scope of the outsourcing arrangement, in the content of benefit and value,
- Measure the success of the arrangements as a whole by comparing actual performance to the savings projections made in the original business plan.
- Preserve the utility's freedom of action to the greatest degree possible, particularly in light of ABS and Accenture's favourable position versus other potential suppliers,
- Bring the transition stage of the project to a reasonably speedy conclusion to send a signal of permanence to the organization as a whole, and
- Continue with change management initiatives so as to speed the process of necessary culture change.

16. CONCLUSION

We believe that presentation of this final report completely fulfils the terms of reference for our work with BC Hydro. We will be very pleased to discuss any of our findings and opinions with the utility at any time. We will also be pleased to make a presentation on

our conclusions and the contents of our reports to the BC Utilities Commission should this step be required.

In closing, we would like to thank BC Hydro for entrusting us with this very important assignment and reiterate our gratitude to those persons at the utility and other organizations who assisted us with our work.

Douglas Louth
President

DOUGLAS LOUTH ASSOCIATES INC.
March 2004

Appendix A

PROFESSIONAL PROFILE OF DOUGLAS LOUTH

Douglas A. Louth, CMC President

Doug Louth is a Certified Management Consultant who has been actively engaged in the utilities industry since 1959 and has participated in major projects in North America, Europe, Africa, Asia and Australia. Until the fall of 1996, he was the partner responsible for Deloitte & Touche's utilities consulting practice in Western Canada. While still under partial retainer from this partnership, he formed his own company to provide utility clients with specialised services in the use of technology and process improvement, particularly in the area of customer care.

Some of Mr. Louth's significant utilities clients include **Westcoast Energy, BC Hydro, the Egyptian Electricity Authority, BC Gas, Enbridge, Pacific Northern Gas, the Abu Dhabi Water and Electricity Authority (ADWEA) in the United Arab Emirates, Centra Gas BC, BC Telephone, Bord Gas in Ireland and the Gujarat Electricity Board in India.** He has carried out a number of assignments for the BC regulatory authority, the **BC Utilities Commission** and was the Director of Information Systems for the **Central Electricity Generating Board in Great Britain.** He is currently providing a range of services related to use of modern processes and technology, management strategy and improved customer service to major power and gas utilities entering the new competitive environment in North America and overseas.

Representative Consulting Engagements

Mr. Louth served as the team leader on a project for the Gujarat Electricity Authority in India, the object of which was to restructure the financial, technology and customer service functions. This project was specifically designed to allow the company to prepare itself for a deregulated environment, while at the same time significantly improving its level of financial control over expansion of its operations.

He worked as the project director of a major assignment to justify, select and install new business practices, systems and processes in twelve new entities that emerged from privatization of the Abu Dhabi Water and Electricity Authority (ADWEA) in the United Arab Emirates. This assignment included definition of operating principles and process needs for new organizations involved in generation, transmission and distribution. He carried out gap analysis in relation to existing business practices and organization, set out a short term implementation plan, defined technology needs and new processes, tendered on behalf of the client for new systems and services, selected vendors and organized and oversaw the implementation process.

For the Egyptian Electricity Authority, London Drugs, Future Shop, BC Ministry of Health, BC Gas, Expo 86, BC Ministry of Municipal Affairs and BC Ministry of Transportation and Highways, he was responsible for both leadership and direct consulting on separate long range procedure and technology planning assignments;

He led a recent project for the Egyptian Electricity Authority in Cairo, the objective of which was to develop a long-range information technology plan. The plan covered upgrading and revitalization of all systems running within the organization, following the merger of generation, transmission and distribution functions. The scope of the project included not only replacement of hardware and systems architectures, but also improvement of processes from point of generation to customer delivery and reorganization of the corporate information technology functions.

He was responsible for a major assignment at BC Gas, a privately owned utility operating throughout the Pacific coast, which involved the establishment of short and long term plans, including establishment of the feasibility and business case, for implementing enterprise wide systems for the financial, work management and personnel functions. This project later involved selection of the necessary packages and the definition of related process improvements.

For the Asian Development Bank, he was engaged to assist the bank in the evaluation of potential aid projects in India and South-east Asia. These assignments involved the investigation of feasibility of project completion, assessment of proposed work plans, validation of projected benefits and assessment of the recipient country's proposals to resource the projects.

For BC Gas, he carried responsibility for monitoring of the development process and assurance of quality of a major customer information system being developed by a third party supplier;

He was Director of Information Systems for the Central Electricity Generating Board in Great Britain, where he was responsible for the day to day operations of a systems group of over 200 staff.

Mr. Louth played a key role as project director for Westcoast Energy in Vancouver, to replace customer information systems in two of the company's wholly owned gas utilities. He was responsible for future technology planning, monitoring and overall quality assurance of the complete systems installation process. The scope of his work ranged from review of the original business cases, through implementation planning, software specification and selection, implementation and testing, to installation of the finished product.

He was responsible for a number of shared services feasibility studies for Pacific Northern Gas and Centra Gas BC, two smaller gas utilities who are pursuing opportunities to cut costs by sharing services ranging from bill printing, remittance processing and financial services to pipeline capacity, accounting and operational systems.

For a major energy producer, he selected and directed the installation of a purchasing and inventory control system that covered over 1 million separate items. This system was implemented on three large computers serving 23 warehouse locations;

For a working committee established under the auspices of the European Economic Community, Mr. Louth acted as First Chairman during a study to determine the potential uses of common computer systems in European utilities, manufacturing and distribution industries;

For a number of private and public organizations, he has led teams that were responsible for all aspects of quality assurance in respect of systems being developed and installed by either in-house or contracted resources. These clients ranged from provincial government and utilities to the travel industry;

For a Royal Commission investigating the effectiveness of the information services of a major Canadian railroad, Mr. Louth acted as an expert consultant and witness.

He acted as Project Manager for major systems implementations for organizations as diverse as the Government of BC, Lufthansa and Swissair, the Abu Dhabi Water and Electricity Authority, a major Canadian department store, and a major BC fruit juice manufacturer;

For a European consulting firm, he was Deputy Director of a research program engaged in research and development of advanced information processing concepts, techniques and technology;

For the Governments of the former Soviet Union and Czechoslovakia, he studied and recommended possible uses for commercial data processing techniques in state controlled consumer goods outlets; For a Vancouver based software house, he carried day-to-day responsibilities for the operation of a large and diverse series of systems design, systems engineering and programming projects in Western Canada.

Mr. Louth is an acknowledged expert in the reengineering of business processes, the strategic use of technology, project management and quality assurance of sophisticated and complex projects, and the design and implementation of new processes and systems. He has participated as a guest speaker on these topics at a variety of conferences in Canada, the USA, Asia, Europe and Australia and is a frequent guest on radio and TV.

Appendix B

SYNOPSIS OF THE OUTSOURCING ARRANGEMENTS

The following text has been extracted and edited from DLAI's interim report dated May 10, 2003. It is repeated here in order to provide context to the final findings contained in previous sections of this document.

The Essence of the Outsourcing Arrangement

The outsourcing contract became effective on April 1 2003. It committed BC Hydro to use ABS' services for a ten year period.

The contract encompassed the transfer of transaction responsibility for seven functions that affect six lines of business (LOB) in BC Hydro. Figure B.1 shows the functions that were transferred and the lines of business affected.

Figure B.1 – Transactions and LOBs affected

Transactions to be Transferred	Lines of Business Affected
<ul style="list-style-type: none">• Customer Care	<ul style="list-style-type: none">• Generation
<ul style="list-style-type: none">• Technology Services	<ul style="list-style-type: none">• Distribution
<ul style="list-style-type: none">• Human Resources	<ul style="list-style-type: none">• Transmission
<ul style="list-style-type: none">• Financial Services	<ul style="list-style-type: none">• Engineering Services
<ul style="list-style-type: none">• Purchasing	<ul style="list-style-type: none">• Field Services
<ul style="list-style-type: none">• Disbursements	<ul style="list-style-type: none">• Powerex
<ul style="list-style-type: none">• Other Support Services	

The key features of the outsourcing contracts and the related organizational arrangements were summarized in sections of this interim report. This commentary was not intended to be an exhaustive analysis of the details of the arrangements put in place on April 1 2003. Rather, it concentrated on those elements of the contract that influence the opinions expressed in both the interim and final reports.

Brief History of the Outsourcing Concept

We have been told that BC Hydro first considered the concept of outsourcing a number of its non-core functions in 2001. Many other utilities had already taken this route and most had achieved success in controlling their cost of operations while maintaining overall control of the functions outsourced. BC Hydro decided that the concept was worthy of detailed evaluation in the context of its own operations.

BC Hydro concluded, rightly in our opinion, that caution had to be exercised in exploring such an option and detailed due-diligence had to be carried out before any

outsourcing took place. We were told the utility therefore undertook a structured process aimed at first establishing the overall feasibility of the outsourcing approach and then finding the best qualified service supplier if justification was established.

To this end, we understand BC Hydro followed a structured due-diligence process for the next two years. The overall objective of this process was to arrive at an informed conclusion. We have been told that information was sought from all qualified suppliers in the marketplace that the utility was able to identify. Each was offered an equal opportunity to tender for BC Hydro's business. The process of selection involved not only in-house resources but also objective, qualified outside consultants.

DLAI was not involved in the due-diligence process, but we have been told that its key features were:

- Internal examination of the feasibility and desirability of such an approach and identification of likely areas of business that would lend themselves to outsourcing.
- Issuance of a request for proposal to sixteen organizations considered to be qualified to provide service.
- Evaluation of first proposals to a point at which a shortlist could be established. Accenture and Cap-Gemini emerged from this evaluation as short-listed suppliers.
- Engagement of Deloitte and Touche to "carve-out" the costs of functions that might be outsourced in order to determine a cost base for any outsourcing contract.
- Contact with, and visits to, previous customers of the short-listed suppliers and detailed examination and analysis of the implications of their proposals.
- Issuance of a request for final proposals to the short-listed candidates.
- Evaluation of final proposals.
- Selection of Accenture as the best qualified supplier.
- Engagement of BMO Nesbitt Burns to carry out due diligence on Accenture's present performance and future objectives.
- Negotiation of detailed contract terms with Accenture designed to protect BC Hydro's long-term interests.

To reiterate, DLAI did not play any role in the process outlined above. We have however reviewed some of the key documents produced by BC Hydro in order to get a perspective of the process that was followed in selecting Accenture. Our work has also benefited from review of information provided by Deloitte and Touche and BMO Nesbitt Burns, and interviews with those who carried out the work.

The Outsource Organization

The outsourcing agreement with Accenture created two significant new entities that are expected to provide the necessary service to BC Hydro and its customers, namely:

- Accenture Business Services (ABS). This is a new Vancouver-based company created by Accenture Inc. It will serve as the primary provider of the services for which it is contracted to BC Hydro for the next ten years. It is to this organization that BC Hydro will transfer approximately 1,600 of its present staff. Virtually all of ABS is owned by Accenture Inc. The only other owner of interest in ABS is BCHSAC, which purchased 100 Class A shares with a face value of \$1, representing BC Hydro's founding partnership interest in ABS.
- BC Hydro Services Asset Corporation (BCHSAC). This was established as a new entity wholly owned by BC Hydro. It will hold hardware and software assets already owned by BC Hydro but now needed by ABS to provide contracted services. BCHSAC will continue to hold software assets on BC Hydro's behalf for the ten-year duration of the contract. Hardware assets will be depleted as they become obsolete over the ten-year period and will be written off at that time. New and replacement hardware will be purchased by ABS and will be owned by ABS from that point.

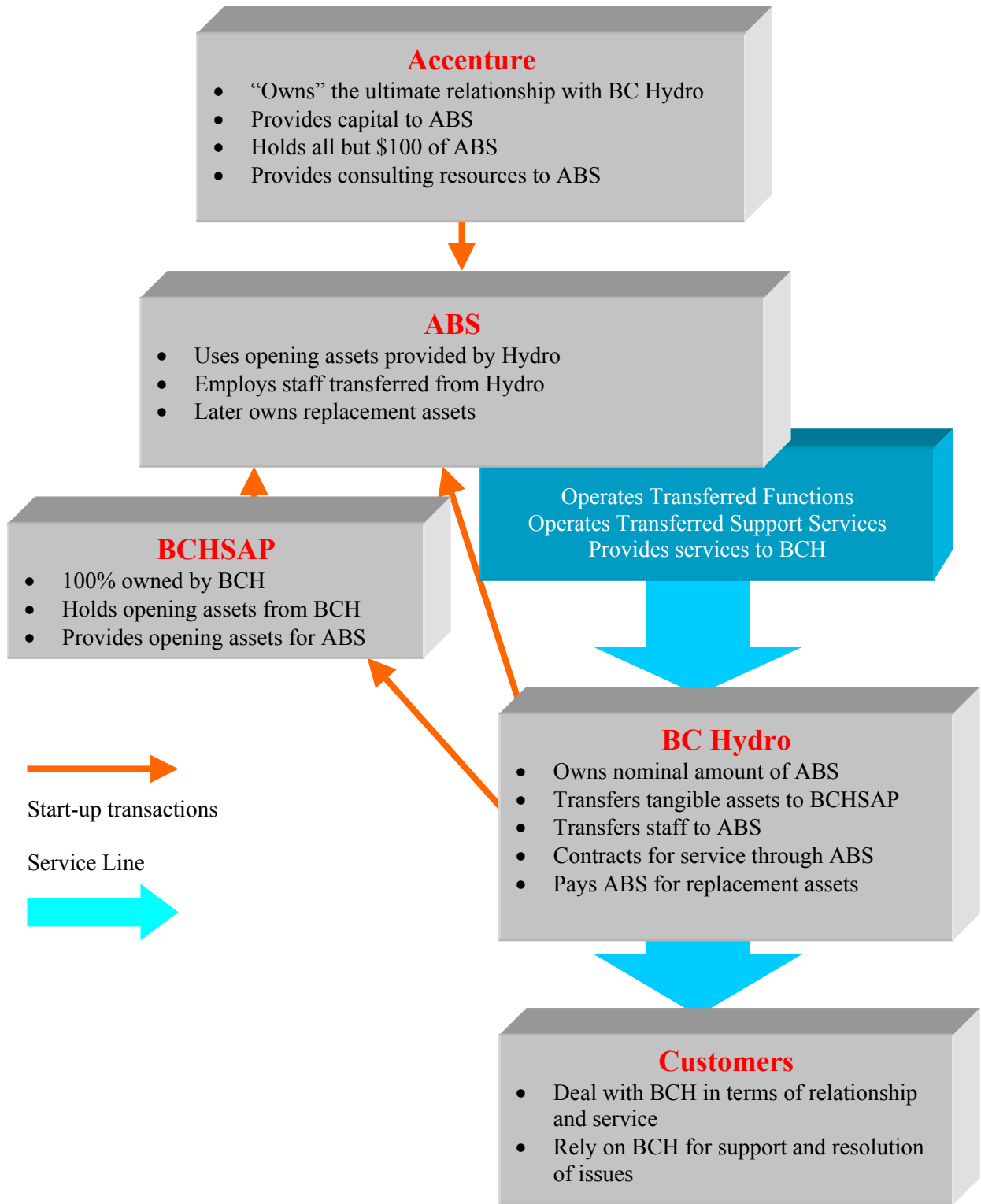
Together with BC Hydro, these organizations form the nucleus of the organizational framework of the outsourcing arrangements, which is shown graphically in Figure B.2 on the next page.

It can be seen from this arrangement that BC Hydro has not transferred any of its core assets to ABS or to any other outside organization as part of the outsourcing contract. Nor has it invested in the new ABS organization, beyond token participation as a partner in ABS to secure its position as a founding partner. To this extent, this particular arrangement is more limited from an asset transfer perspective than others DLAI has been asked to examine.

Material control of the relationship still rests within BC Hydro and the utility's relationship with its customers is preserved. Continuation of the level of service to these customers remains assured at the same or better quality than that currently provided. It is fair to say that ABS is simply providing a service to the utility under the arrangements that have been established.

At some time in 2004, part of the outsourcing contract will be assigned to BC Transmission Company (BCTC) when that company becomes active. It is DLAI's understanding that BCTC will assume responsibility for those costs it incurs with ABS and will inherit prorated parts of the minimum aggregate spend to which BC Hydro is currently committed and its portion of the guaranteed savings committed to by ABS.

Figure B.2 - The outsourcing organization



Primary Functions to be Outsourced

Under the terms of its arrangements with ABS, BC Hydro outsourced transactional responsibility for seven primary business functions on April 1 2003. These functions and the process elements affected are shown in Figure B.3.

The “other support services” shown in this Figure are supplementary services to those primary functions outsourced. The numbers shown in the budget column are those “carved out” by Deloitte and Touche as being 2003 costs directly related to the functions being outsourced to ABS.

Figure B.3 – Functions to be Outsourced

Function	Process Elements	2003 Budget [\$000]
Customer Care	Function, Processes and Systems	54,700
Technology Services	Westech and NCS Services	66,352
Human Resources	Transaction Processes and Systems	7,826
Financial Services	Customer-related Functions, Transaction Processes and Systems	2,905
Purchasing	Function, Processes and Systems	1,469
Disbursements	Function, Processes and Systems	3,088
Field Services	Function, Processes, Office Space Management and Some Systems	15,720
Other Support Services	As required	3,631

We confirmed with BC Hydro that the total 2003 budget for transferred services amounted to \$155,691,000 as shown in this figure.

As Figure B.3 shows, the major impact of the outsourcing agreement falls within the areas of customer care and technology services. Transactional responsibility in both functions was literally transferred in its entirety to ABS. Responsibility for technology services previously provided internally to the Distribution LOB also passed to ABS.

ABS also took responsibility for Building Office Services. This part of the arrangement means that ABS is responsible for management of office space and maintenance of 61 existing buildings throughout the province.

All lines of business in BC Hydro use the services of ABS to support the other functions outsourced. For instance, Human Resources services and payroll are provided by ABS to all LOB’s, as well as access to the financial system and services.

A further general impact on the LOB's was felt with the transfer to ABS of responsibility for technology services, largely those services previously provided by NCS and Westech. For these lines of business within BC Hydro, responsibility for hardware, software, network and systems support transferred to Accenture on April 1 2003.

Although responsibility for the operation of Westech passed to Accenture under the outsourcing contract, BC Hydro remains liable for the cost of services that Westech is currently providing to a small number of existing outside customers. We have been told that these services relate mainly to software development and support contracts.

Though the staff responsible for the fulfillment of these contracts has transferred to ABS, the contracts remain with Westech. It is estimated that BC Hydro will incur costs for fulfillment of these contracts. We understand that these costs are estimated to amount to approximately \$3 million per year for the first three years of the outsourcing agreement. BC Hydro will receive the revenue accruing from completion of the contracts. The utility's estimate is that revenues will at least match costs over the three year period.

Limits to Responsibilities Outsourced

When considering an outsourcing arrangement, we were told that BC Hydro wished to retain full control of its operations while:

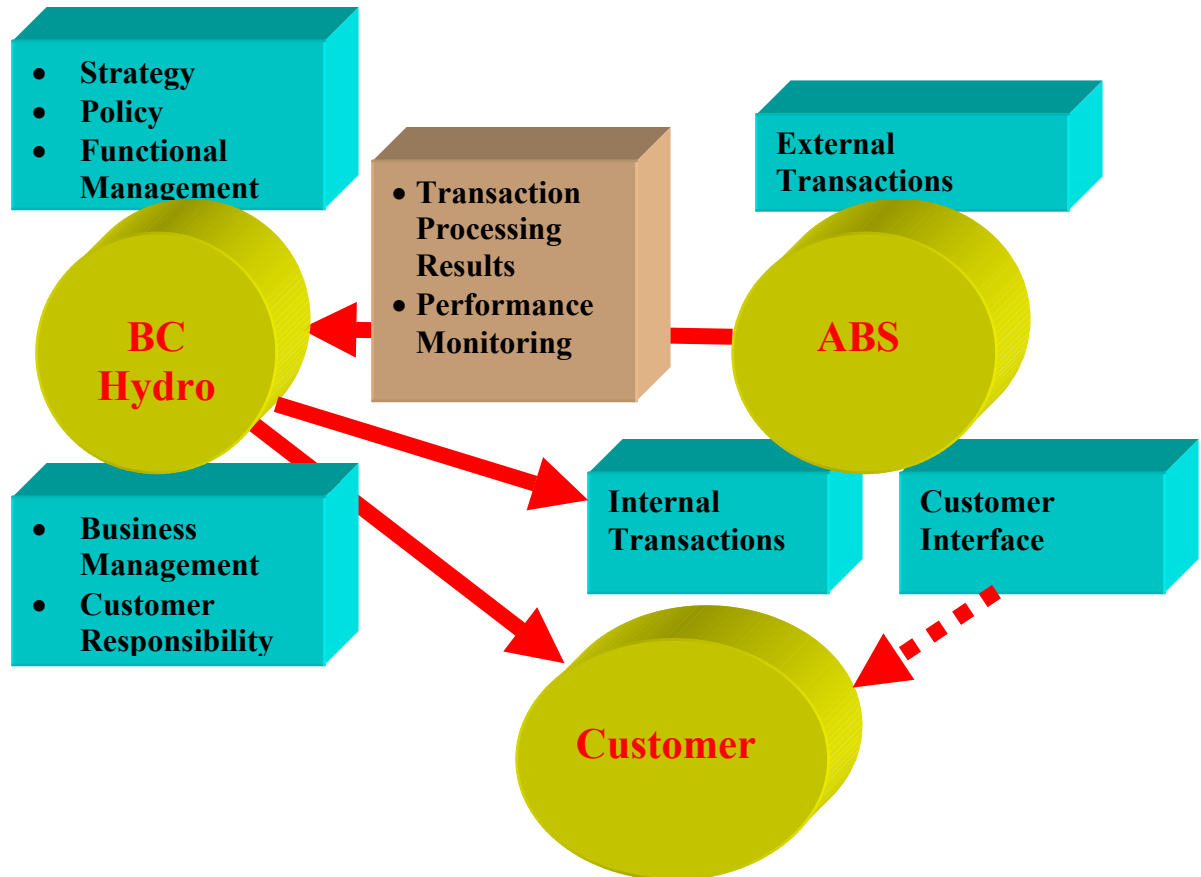
- Improving its operational processes, procedures and performance,
- Achieving some immediate cost savings,
- Controlling its costs in the long term,
- Mitigating its risk in terms of high technology costs that were foreseen in the immediate future,
- At least maintaining the conditions of employment and opportunities for its employees, and
- Maintaining or improving its levels of service to its customers

The utility believes it has achieved these objectives through the outsourcing arrangement with Accenture.

In order to understand the outsourcing agreement, it is necessary to fully appreciate the respective roles of BC Hydro and ABS. It has to be stressed that ABS is simply providing a transaction processing service to support the utility's business activities. Responsibility for control and strategic-level management of all transferred functions continues to rest with the utility. In particular, BC Hydro continues to set policy for all of the functions covered by the outsourcing agreement and is fully responsible for policy implementation.

Figure B.4 is a graphic representation of the relationship between BC Hydro, ABS and the utility's customers as created by the outsourcing contract.

Figure B.4 – Outsourcing Relationships



Other Outsourced Functions

A new CIS, based on the SAP software product, has been under development at BC Hydro for some time. Known as the Northstar project, this development became the responsibility of Accenture on April 1 2003.

BC Hydro will no longer be liable for development and implementation cost overruns under the outsourcing agreement. Further, BC Hydro will receive repayments of up to <Redacted> million of its prior investment in Northstar if Accenture is successful in marketing use of the CIS product to other North American utilities. The actual return to BC Hydro will depend on the number of new customers ABS is successful in converting to the Northstar system.

The Minimum Aggregate Spend

In DLAI’s opinion, the cornerstone of the outsourcing contract is the concept of the minimum aggregate spend (MAS). Under this concept, BC Hydro guarantees ABS a minimum cash flow resulting from the services ABS provides. The utility is committed to spend the MAS amount on ABS’ services for the ten-year term of the contract. The range of services included within the MAS can be varied at BC Hydro’s discretion, the overall dollar impact of the MAS may not.

We understand that the MAS has been calculated on the basis of payment of the 2003 cost of those services being transferred, less guaranteed savings. These savings represent the difference between the MAS and BC Hydro’s estimated 2003 costs of operating the transferred services.

We assume that ABS expects to realize at least offsetting savings on its own account from two sources, namely improvement of the service processes in the new environment and sale of similar services to other customers. However, the charges to BC Hydro implicit in the MAS are not dependent on such ABS savings being realized and, based on our understanding of the contract, BC Hydro is not contractually at risk in this regard.

The Minimum Aggregate Spend is built into the outsourcing contract at the levels shown in Figure B.5. This shows both the MAS and the related guaranteed savings. It can be said to be BC Hydro’s cornerstone commitment to the implementation of the outsourcing arrangements. All dollar amounts shown in Figure B.5 are in \$000.

Figure B.5 – MAS and guaranteed savings

Year	MAS	2003 Costs	Guaranteed Savings	Percentage Savings
2003	147,356	155,691	8,335	5.35
2004	137,984	155,691	17,707	11.37
2005	131,300	155,691	24,391	15.67
2006	126,822	155,691	28,869	18.54
2007	Redacted	155,691	Redacted	Redacted
2008	Redacted	155,691	Redacted	Redacted
2009	Redacted	155,691	Redacted	Redacted
2010	Redacted	155,691	Redacted	Redacted
2011	Redacted	155,691	Redacted	Redacted
2012	Redacted	155,691	Redacted	Redacted
Total	1,284,374	1,556,910	274,536	17.63

The Importance of Service Units as the Basis of ABS’ charges

Notwithstanding the implications of the MAS, the outsourcing contract stipulates that the actual monthly charges invoiced to BC Hydro by ABS will be based on the number of “service units” used by the utility.

In its simplest form, a service unit can be equated to a particular outsourced transaction, e.g. a customer call to the call centre, production of a bill, receipt of a customer payment etc. Other service units relate to numbers of units served by ABS, e.g. number of network servers maintained, number of employees on the payroll etc. The contract calls for estimates of anticipated minimum, average and maximum unit volumes to be set, and a unit price range to be applied to these categories. The maximum price is referred to in the contract as the “ceiling price” while the minimum price is the “floor price.”

At the time this report was prepared, unit prices and anticipated unit volumes had not been finalized. Based on information provided to us by both parties, it is expected that multiplying unit prices by expected usage and aggregating the result should equate to the value of the MAS. However, we have been unable to confirm that this is the case.

Actual billings to Hydro will be a function of the cost of service units actually used, multiplied by the applicable unit price within the price range. If BC Hydro uses more units than the maximum in any particular month, it will pay for excess usage at the marginal cost above the ceiling price. If it uses fewer units than the minimum estimate, the MAS will still apply. However, if consistent under-use occurs, BC Hydro may add additional services to the outsourcing contract to bring service costs up to the MAS level.

Potential Sources of Cost Reduction

The outsourcing contract identifies a number of opportunities for BC Hydro to reduce its costs of service in addition to the guaranteed savings. Specifically, ABS is committed to:

- (Redacted)
- (Redacted)
- (Redacted)
- Return up to \$30 million of CIS costs already incurred by BC Hydro in connection with the Northstar project, if the same CIS is chosen for use by other utilities outsourcing customer care services to ABS.

From our examination of the contract, we have determined that these opportunities for BC Hydro are not subject to any Accenture approval process. They will automatically apply when the qualifying conditions occur.

Human Resource Arrangements

Approximately 1,600 employees of BC Hydro transferred to ABS on April 1, 2003. We have been assured that their conditions of employment were unchanged when the transfer took place. We also understand that initially they were expected to carry out basically the same functions as before the transfer, using the same desks and the same workstations and supporting the same processes.

Subsequent to agreement with the union representing the affected workforce, the OPEIU, all employees eligible for transfer were offered the opportunity to elect to move to ABS or exercise other rights, basically severance, early retirement or continuation of employment with BC Hydro.

Contract Management of ABS by BC Hydro

The outsourcing contract contains a number of mechanisms for BC Hydro to exercise control over the execution of the arrangements through:

- Definition of standard service level metrics for each outsourced functional area and the use of these metrics to monitor ABS' performance. Where performance consistently falls below the established standard, BC Hydro can apply "demerits" to ABS which effectively delay payments against the MAS,
- Orders for improvement to service where these are necessary. The contract contains specific provision for establishment of a change order process,
- Active participation in regular benchmarking activities as described earlier, and
- The use of defined exit clauses in the contract that allow BC Hydro to withdraw for either convenience or cause.

BC Hydro has put in place a contract management governance strategy and organization. This organization is responsible for definition of service level measurements beyond the limited set being used at the outset; determination of the need for change orders and overall monitoring of ABS' costs and level of performance.

All of the opinions expressed by DLAI in previous sections of both the interim and final reports are set in the general framework of the outsourcing arrangements described above.

Appendix C

WORK PLAN FOR PHASE TWO OF THE ASSIGNMENT

The work plan shown below was originally drawn up on January 23, 2003. As the work progressed, it was further refined on February 3 and March 6, 2003 during discussions between BC Hydro and DLAI.

The work steps have remained basically unchanged throughout, but the emphasis of the tasks was adjusted to coincide with the priorities that emerged during DLAI's work. In this context, start and end dates shown below are actual dates.

Start Date	Target End Date	Task	Notes
FINAL REPORT PREPARATION			
Oct 20	Oct 20	Initial meeting to review and approve work plan	
Oct 21	Oct 24	Meet with BC Hydro managers to review status of Accenture contract and experience to-date. Identify issues for investigation.	Topic areas stated in text on preceding page
Oct 21	Oct 24	Assess impact of emerging regulatory requirements	
Oct 27	Oct 29	Develop approach to address issues and finalize work plan	
Oct 30	Oct 31	Agree expanded work plan with BC Hydro management	
Nov 3	Dec 5	Carry out critical reviews in each area identified in text on preceding page	Depth depends on level of issue remaining
Nov 21	Dec 10	Carry out critical reviews in any other areas needing further examination.	

Start Date	Target End Date	Task	Notes
Nov 21	Dec 12	Re-assess impact of regulatory requirements	
Nov 28	Jan 19	Prepare and present draft findings	Two week pause for holiday season
Jan 20	Feb 15	Prepare draft of final report	
Feb 16	Feb 16	Review draft with BCH and make any justified changes	
Feb 17	Feb 28	Consolidate and document final opinion on Accenture arrangements	
Oct 20	Project End	Contingency, admin, progress discussions, report production etc.	As needed

Appendix D

LIST OF DOCUMENTS REVIEWED IN SECOND PHASE

Document Name	Dated	Status [see note 1]	Source
• Master Services Agreement (the MSA)	31 Jan 2003	Executed Version	BCH
• Attachments and Appendices to the MSA	Various	Executed Versions	BCH
• Overall Status of BC Hydro's Relationship with ABS	6 October 2003	Prepared for DLAI by Ms. Rosalie May	BCH
• Quarterly Status Reports, Including Comparison of Actual Spend vs. MAS	End-June, Sept and Dec, 2003	Final	BCH
• Issues Outstanding Log	16 Oct 2003	Final	BCH
• Project Transition Plan	17 Oct 2003	Final	BCH
• BCH Spending Projections [on ABS services]	17 Oct 2003	Working Papers	BCH
• Table of Base Unit Prices Charged by ABS	13 Aug 2003	Working Paper	BCH
• Pricing Process and Products and Services Price List	29 Aug 2003	Working Paper	BCH
• Asset and Support Loadings to ABS Services	29 Oct 2003	Presentation	BCH
• Service Level Reports	Through 6 Oct 2003	Final	ABS
• Audit Plan	13 June 2003	Plan	BCH Internal Audit
• Change Order Process and Tracking	17 Oct 2003	Final	ABS
• ABS Invoicing Process	Undated	Draft	BCH
• Service Level Demerit Model	17 Oct 2003	Final	BCH
• Service Level Metrics	17 Oct 2003	Final	BCH
• Service Availability Report	17 Oct 2003	Final	BCH
• Revised Business Case	12 Nov 2003	Final Draft	BCH
• Northstar Project Charter	30 Aug 2002	Final	BCH

Document Name	Dated	Status [see note 1]	Source
<ul style="list-style-type: none">Northstar Budgets and Progress Reports	Various	Working Papers	BCH
<ul style="list-style-type: none">Excerpt from CIS Business Case	Undated	Working Paper	BCH
<ul style="list-style-type: none">Internal Audit Report – ABS Customer Care Payment Services	12 Aug 2003	Final	BCH
<ul style="list-style-type: none">Program and Contract Management Report	4 Sept 2003	Final	PriceWaterhouseCoopers

Notes:

1. Status of document shown is that reported to DLAI by BCH
2. Many of the documents reviewed in the first phase of our assignment were also referenced in the second phase of our work

Appendix E

LIST OF INTERVIEWEES IN SECOND PHASE

BC Hydro

Ms. Bob Elton
Ms. Jay Grewal
Ms. Bev van Ruyven
Mr. Jack Bachman
Mr. John Banks
Ms. Nancy Deare
Ms. Pat Howard
Mr. Len Hughes
Mr. Clement Li
Mr. Christopher Eng
Mr. Warren McKay
Ms. Michelle Madsen

Ms. Rosalie May
Mr. Gary Sherlock
Mr. Bob Steele
Mr. Richard Stout

Accenture (ABS)

Mr. John Iyck
Mr. Lawrence Dudson

Appendix F- Principle of the Unit Pricing Model

