

Unlocking service company value

The U.S. electric and gas utilities industry is transforming rapidly and on multiple fronts. For utility executives, the top-of-mind issues that will require substantial investment over the near term include disruptive technology, changing environmental regulations, and grid modernization among others.

In response to these challenges, some utility executives are starting to reexamine their back office as a means to unburden their rates. They want to free up much needed headroom for today's pressing challenges and also recognize that if they could start with a clean slate, their operating models today might look quite different.

In recent years, leading organizations outside the utilities industry have adopted Global Business Services (GBS) as a means to further optimize and transform their back office operations. For newly constituted organizations especially, the future resembles a virtual network of business process and information technology partners often combined with the capabilities of a global shared services center (SSC).

Through the results of the 2015 Global Shared Services Survey, Deloitte has observed a sharp climb in SSC global expansion with 60% of respondents also indicating that their SSCs are multifunctional. At the same time, productivity increases remain consistent from the 2013 survey at around 8% despite the concerted shift abroad. Continuous improvement is often hard-wired into the culture, and the average payback is 2.3 years.

These results represent a complicated slate of opportunities for utility executives. A move towards GBS will require a rethink of their service companies, where centralized services are delivered in a regulated utility construct. Historically, service companies have not been a store of value-added or continuous improvement, but rather, they focus on compliance-oriented operating objectives:

- Properly aligning costs between operating companies and service companies
- Developing correct and efficient cost allocation methodologies
- Promoting rate case readiness to determine allowed rates of return



In addition, the operating scope of service companies is incredibly diverse and varies greatly across the utilities industry. To a large extent, the scope of services for services companies evolves over the course of many years according to local regulatory allowances. While a review of regulatory filings reveals that there is a common belief among utility executives that their service company costs are correctly and efficiently allocated, they employ a wide range of approaches to both direct and indirect rates for jobs, projects and functions.

A centralized service company provides services such as: administrative, managerial, financial, accounting, recordkeeping, legal or engineering services, which are sold, furnished, or otherwise provided (typically for a charge) to other companies in the same holding company system

Service Company Defined by FERC

In 2008, the Federal Energy Regulatory Commission (FERC) required service companies to adhere to a set of standard chartered accounts as well as uniform record retention through a readily accessible cost allocation system. One might expect compliance with the rule to drive additional standardization. However, the scope of service companies is still often specific to the utility and their local regulators.

Innovating through GBS

Outside the utility industry captive service centers are becoming stores of innovation. This is happening because GBS executives are choosing to harbor high value-add capabilities, while outsourcing around the periphery of their businesses. This allows executives to experiment with new and/or adjacent services, infrastructure, skill sets and other capabilities, while retaining the best for their organizations.

From this vantage, utility executives have an opportunity to assess the value their service companies provide in not only carefully accounting affiliated utility operating company costs but also in combining assets, capabilities and enablers for future growth. Figure 3 depicts the “right shift” in GBS value and innovation. A Growth Platform can be viewed as a different set of mutually reinforcing capabilities, which form the foundation for sustainable competitive advantage,

when applied against a series of related and structurally attractive value creation opportunities.

The mutually reinforcing capabilities of a service company are the talent, processes and infrastructure that come together to provide value-added services at a reasonable cost to the business — in this case, the utility operating companies.

More broadly, utility executives can apply these capabilities to value creation opportunities outside the service company. For example, they could outsource service company talent in finance transactions, customer service and process improvement for a new solar leasing business. Processing the high volume of leasing contracts, payments and master data requires skills learned in service-based roles. If the venture proved effective, this capability could be integrated into the core of a captive center.

Service companies across the industry already provide a wide range of services from leasing office space to digital wireless communications in addition to traditional IT shared services, legal, finance and accounting services. This diversity provides a range of capabilities not commonly seen in electric and gas operations.

Figure 3: GBS shift “right” to business value and innovation³

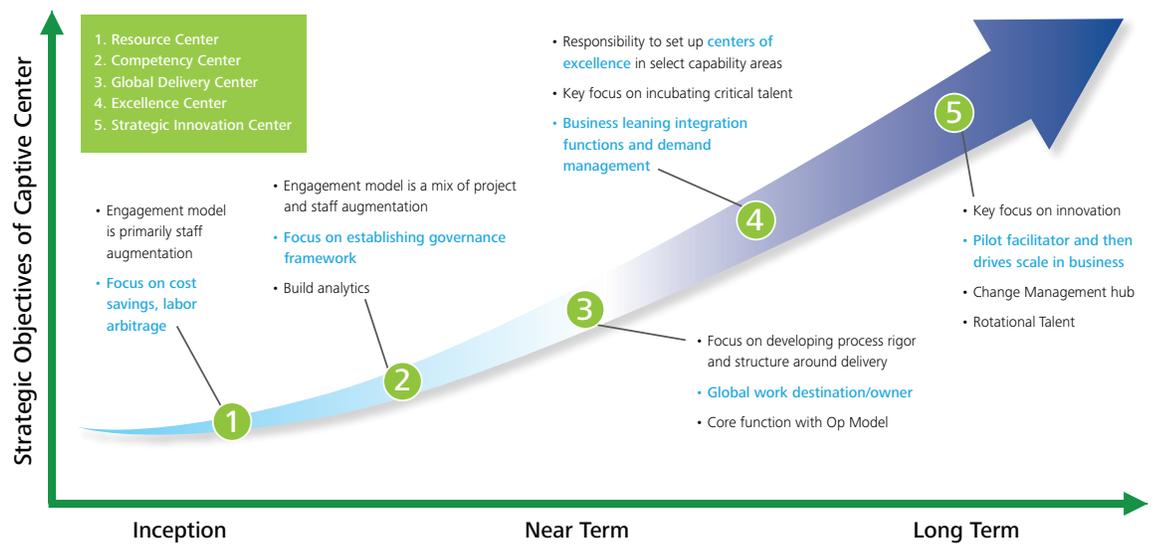


Figure 2: 2x3 process split matrix

		Method of adding value	
		Low cost/defined transactional service level	Strategic knowledge based
Relationship to the business	In-Market (Local)	1. In-market site support <ul style="list-style-type: none"> Distributed to location(s) for local service needs Required for local input/data capture or local programs including (where required) regulatory, statutory reasons Manual or end-user intensive 	2. In-market business partnering <ul style="list-style-type: none"> Aligned with function/unit Line/management focus Knowledge & know-how transfer Decision/action intensive
	Centralized (Regional)	3. Regional/divisional transaction processing <ul style="list-style-type: none"> Consolidated organization with some proximity to the region/division Operational focus Standardized services Process intensive Could cover countries or regions 	4. Regional/divisional business partnering <ul style="list-style-type: none"> Expertise focus — ability to leverage skills regionally “Best practice” development Issue/knowledge intensive Organized by regional with some proximity to the region/division
	Centralized (Global)	5. Global low cost processing/BPO <ul style="list-style-type: none"> Consolidated organization Operational focus Standardized services Process intensive Could cover countries or regions 	6. Corporate center of excellence <ul style="list-style-type: none"> Expertise focus — ability to leverage skills globally “Best practice” development Issue/knowledge intensive Organized globally

Applying the GBS framework to service companies

Utility executives can enhance their service companies by increasing standardization and furthering consolidation. A recent effort undertaken by a global non-utility company recognized over \$100M in annual savings by moving finance, hr, procurement, IT and real estate work to a multi-function SSC. In addition to the cost savings, the SSCs are helping to enable continued global expansion across over 90 countries. End-to-end process reconfiguring around a conceptual GBS model was central to the design.

There are two common models. The first is Shared Services — where certain activities and processes are delivered from a captive shared location. The second is Outsourcing — where a business process outsourcer delivers the activities and processes.

With increasing frequency, a third model is Virtual—where the suite of steps in a single process is delivered by multiple groups across locations.²

Regardless of the model chosen, the specific principles remain the same: standardization, consolidation, process enhancements and automation. While seemingly straightforward, the path to achieving these principles in practice is often long and complex. Figure 2 depicts process splits from transactional to knowledge services by relationship to the business in a general context.

Notice the extent to which location is a driving factor in determining GBS structures. While the utility industry certainly faces particular constraints in terms of location strategies, 2008 FERC rules are helping to facilitate regional complexity into the utility business model as more shared services are provided across state, regional and international borders.

Utility executives also have an opportunity to reassess the desired outcomes of their charge-back methodologies. The opportunity is less about moving from allocation to direct charging, and more about whether charges achieve either low-cost or strategic objectives. Designing both location

strategy and charge-back methodologies in a GBS context will help utility executives better position their businesses for the future.

Conclusion

The utility industry is on the cusp of disruptive change. As a result, the utility business model that has generated stable shareholder value for over 80 years is under pressure. This is unfamiliar territory for an industry whose focus has traditionally centered on providing safe and reliable electricity at a reasonable cost.

The centralized service company can play a pivotal role in the evolution of utility holding company systems. FERC has aided the industry with clarity around specific service company rules. As a result, additional regional complexity can be introduced into the utility business model and more shared services can be provided across state, regional and international borders.

As utility executives test opportunities to enhance their service company operations, incorporating leading practices in GBS can both enhance consumer protections and enable a platform for future growth. A few areas that present opportunities are location strategies, new charge-back methods and an assessment of assets, capabilities and enablers to provide future energy-related services.

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Endnotes

- ¹ Deloitte conducted a review of FERC form 60 and financial statements for the top 20 U.S. utilities by revenue.
- ² Shared Services Handbook Hit the Road. Deloitte MCS Limited. 2011.
- ³ My GBS Strategy is "Cloudy." John Tweardy. Deloitte Shared Services, GBS & BPO Conference. 2014.

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