



2016–2020 Price Reset

**Appendix B
Labour cost efficiency**

April 2015

CitiPower
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1 Labour cost efficiency

The key to ensuring labour cost efficiency is the efficient organisation and management of labour.

We have a flexible labour force which is sourced through a diverse range of contractual arrangements.

Flexibility in our labour resources enables us to optimally utilise our labour and thereby minimise the risk of labour stranding following large-scale or skill-specific projects.

We continuously review the optimal mix of labour arrangements to ensure we have the most cost effective mix, given prevailing market conditions.

We ensure our employees and contractors have strong incentives to work together to deliver electricity distribution services safely and efficiently.

Our labour rates are set at the efficient level to ensure we attract and retain high quality, highly skilled employees and contractors necessary for the efficient delivery of electricity distribution services for our customers.

We do not consider that the labour data available is of sufficient quality and consistency to enable benchmarking of labour costs across distributors.

1.1 Efficient utilisation of labour

The most significant driver of overall labour cost is the quantity and quality of labour employed. While per unit labour costs are a contributing factor to overall labour costs, the key to ensuring labour cost efficiency is the efficient organisation and management of labour to minimise the risk of under-utilisation and under-performance.

1.1.1 Diverse labour contracting arrangements

To achieve optimal labour utilisation, we have structured our labour force to provide flexibility in managing labour resources. We have the following types of labour contracts:

- internal labour—these are permanent employees who provide the base level of labour required to provide a base level of labour services. To operate sustainably over the long term we must ensure we have secure access to a sufficient quantity of labour with the skills and knowledge required to deliver the minimum level of network and corporate services;
- resource partners—these are third-party businesses, for example Lend Lease and Electrix, that provide additional labour services on an as needs basis. We utilise our resource partners to manage increased workloads that may arise for specific work programs. Resource partners are identified through a three yearly market testing process; and
- contractors—we utilise contractors for skill-specific work including electrical work, fault response, metering works, civil works (i.e. digging works), traffic management, design work and vegetation management. We have different contractual arrangements with our contractors, ranging from longer term contracts with third party businesses, such as Daly's Constructions Australia and Powercables, to project-specific arrangements with individual Registered Electrical Contractors. For example, we used Registered Electrical Contractors in the Advanced Metering Infrastructure rollout.

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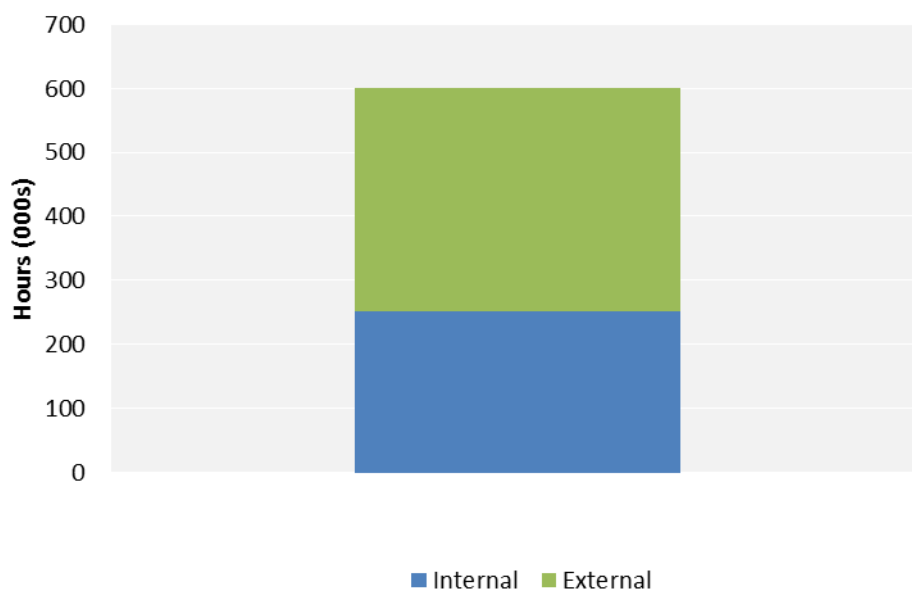
The range of different labour sources available to us provides the following key advantages:

- reducing the risk of labour stranding following large-scale or skill-specific projects; and
- enabling focus on the effective management of our internal labour which is core to the operation of the network.

For example, for the Metro and CBD security of supply projects we installed 7.1km of new 66kV underground sub transmission feeders between two inner city zone substations and Brunswick Terminal Station. These works were delivered with resource partner Daly’s Constructions Australia. Daly’s Constructions assisted with the provision of labour resources and heavy excavation plant to undertake the physical construction work as well as supplementary underground cable design resources, project management and community liaison resource. This demonstrates that we are able to utilise external parties for work requiring specialised skills and equipment. This means that we do not need to employ these specialised skills on a permanent basis or purchase equipment that is not required for regular network activities.

Figure 1.1 provides the proportion of internal and external labour utilised for the delivery of field services in 2014. Field services include for example, connection services, asset replacement and maintenance, construction of lines, cables, substations and terminal stations and network surveying and design. In 2014, 42 per cent of field services work hours were provided from internal labour and 58 per cent from external labour.

Figure 1.1 Proportion of labour utilised for the delivery of field services in 2014



Source: CitiPower analysis

We continually review the share of labour sourced through each of the above arrangements to assess the mix which provides the most cost efficient option at a given point in time. The optimal mix of labour arrangements changes over time given changing market conditions and changes in skill requirements.

1.1.2 Optimal use of labour resources

To ensure the optimal use of our labour resources, whether sourced internally or externally, we:

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- undertake long term project planning to ensure that projects are efficiently phased to maximise the use of our labour and to ensure we have the necessary skills available to resource the projects. We hold a database on employee skills to ensure each project is appropriately resourced with the required balance of skills. We advise our contractors of future projects to ensure sufficient supplementary and complementary labour will be available. Our long term resource planning mitigates the risk of short-term labour shortages or excesses which is a very important aspect of cost efficiency and project delivery;
- set key performance targets. For our internal labour we set performance targets in relation to safety, absenteeism, overtime and delivery. Performance against these metrics is assessed at the group level and is tied to employee bonuses. This system creates positive incentives for employees to work together to achieve safe and efficient outcomes. We also set key performance targets for our contracted labour, the targets depend on the nature of the engagements;
- use hand held technology in the field to optimise labour time. We find that hand held technology in the field improves resource allocation and reduces administration time; and
- promote employee engagement in training and development. We offer employees a comprehensive range of training and development programs to refresh, expand and strengthen employee skills. This ensures our employees are provided with the tools to maximise their potential.

1.2 Labour cost benchmarking

As noted above, the utilisation of labour has the single largest impact on overall labour costs. In addition, our labour rates are efficient given the prevailing labour market conditions. As discussed in chapter 7, we negotiate strongly to achieve market reflective labour price growth rates. We consider our labour rates are set at the efficient level to ensure we attract and retain high quality, highly skilled employees and contractors necessary for safely and efficiently delivering electricity distribution services for our customers.

We note that any comparison of labour costs using data sourced from the category analysis Regulatory Information Notice (**RIN**) is not appropriate because our initial review of the labour data and basis of preparations (**BoPs**) indicates that the data are not comparable across distributors. For example:

- our labour costs are reported inclusive of ordinary time, overtime, superannuation, allowances, bonuses and other labour related overheads such as training costs.¹ Approximately 38 per cent of our total labour costs relate to on-costs and other costs. Some other distributors however have reported the data based on only some of these aspects of labour costs. For example, Endeavour Energy's BoP states that it has excluded overtime, allowances, bonuses, incentive payments and superannuation contributions.² While many of the other distributors' BoPs are not clear as to which labour costs have or have not been captured in the data, the significant variation across distributors in terms of average salary and average labour rate provides strong evidence that reporting is inconsistent. It is notable that the data suggests the lowest average labour rate is approximately half of the highest and the lowest average salary is 40 per cent

¹ Our labour costs are reported inclusive of all of the costs required to be included in accordance with the definition of labour costs set out on pages 52 and 53 of the attached Category Analysis Regulatory Information Notice, dated 7 March 2014.

² Endeavour Energy, *Basis of Preparation, AER Category Analysis RIN*, p.55.

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lower than the highest. These results are clearly unrealistic. It is also notable that there are no similarities in labour rates or average salaries of distributors operating in the same State. As distributors in the same State compete for labour, more similar labour rates and average salaries would be expected; and

- we have reported our productive labour time based on actual time confirmed hours for field labour and assumed a 7.5 hour day for office-based workers excluding non-working days (i.e. taking account of annual leave, sick leave, other leave or public holidays which is non-productive time). Some of the data reported by other distributors suggests that productive labour time is based on either substantially more than a standard 7.5 hours a day and/or no allowances have been made for non-working days. For example United Energy's BoP states it has assumed a working day of 7.6 hours³, however United Energy's total productive hours are on average 1,952 per average staff level (**ASL**). Consequently, it is clear that there is an assumption that employees work at least five days a week, 52 weeks a year which clearly cannot take account of non-working days. Similarly, Endeavour Energy's BoP states that it has calculated its productive work hours assuming 52.17 weeks per year which clearly makes no allowance for non-working days.⁴ Further, we note that given annual leave entitlements of four weeks per year and around 11 public holidays there are only 230 working days per average year. Given an average working day of 7.5 hours, we would consider productive hours reported above 1,724 per ASL to be highly questionable (even this would require no employees to take other forms of leave such as sick, bereavement, long service or other personal leave).

Given the difference between our reporting approach and that of other distributors, it is likely that our labour costs may appear relatively high while our productive labour hours may appear relatively low. The differences in reporting of labour costs and productive labour time compound when the data is used to compare labour cost per productive hour. Consequently, the labour data reported in the Category Analysis RINs is not of sufficient consistency to provide meaningful comparisons of labour rates across distributors and should not be used for benchmarking purposes.

Further, we note that many of the BoPs clearly indicate that the labour data has been estimated and in some cases caution is advised in the use of the data for comparative purposes, for example by Essential Energy.⁵

³ United Energy, *Category Analysis RIN - Basis for Preparation*, June 2014, p. 45.

⁴ Endeavour Energy, *Basis of Preparation, AER Category Analysis RIN*, p. 57.

⁵ Essential Energy, *Basis of Preparation Response to Category Analysis RIN*, p. 45.