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PRELIMINARY BENCHMARKING STUDY

CHUGACH ELECTRIC ASSOCIATION

compared to 860 OTHER U.S. ELECTRIC DISTRIBUTION COOPERATIVES

by Lee Ann Gerhart, CPA (Texas)
for
Citizens for an Independent Chugach Electric

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Executive Summary

Purpose:

To evaluate how efficiently Chugach Electric Association is run and to make appropriate recommendations for further study and improvement of the cooperative.

Background:

Despite enjoying some of the lowest input fuel costs in the country for generating power, Chugach Electric Association retail electric rates are above the U.S. national average.

This study identifies those factors which are contributing to the apparently high rates that CEA member-owners pay. The main emphasis is on labor. Next to the cost of power, labor is an electric utility's highest cost component, and unlike taxes, labor costs are largely within management's control. While it has been known that labor rates at CEA appear to be very high compared to the open market, it was not known to what extent these high labor rates equate to productivity and organizational efficiency at CEA.

Benefits of Benchmarking:

Benchmarking compares overall organizational efficiency by evaluating the combined effects of labor rates and productivity. This permits the emphasis to move beyond salary comparisons for individual employee positions.

Co-op consumers are captive customers who cannot take their business elsewhere if costs get out of control. Market forces function imperfectly under these circumstances and benchmarking can be used by co-op members to judge how well their public utility

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*This study was performed on a volunteer basis for Citizens for an Independent Chugach Electric.

regulatory authorities are protecting their interest against the harmful effects of monopoly that can result from utility exclusive service areas.

Source of Benchmarking Data:

A computer tape was obtained from the Rural Electrification Administration (REA) providing 745 pieces of loan, operating, and financial statistics for 878 electric distribution co-ops, as reported on the 1992 Financial and Statistical Reports (Form 7).

Findings: *Payroll / Cost of Living Assessment*

Kodiak Electric Association and CEA had the highest average pay per hour of any distribution or G&T cooperative in the nation (76% and 68% above the national average). Homer Electric Association placed third in distribution pay behind Kodiak and CEA. These rankings were made on an equalized basis after cost of living adjustments and differentials between distribution and generation salaries were taken into account.

The high rate per hour paid at CEA is partially a result of both higher amounts of overtime and higher overtime rates. CEA employees worked 34% more overtime than those at the average distribution co-op. Overtime provides only a partial explanation for the higher rate per hour. If all overtime at CEA were paid at triple time and all other co-ops at only time and a half, CEA's base rate would still be $8.00 per hour higher than a comparable rate for the average distribution co-op.

Findings: *Productivity Assessment*

CEA appears to be overstaffed. Actual hours worked exceeded hours for co-ops of the same size and service area density by 12.6%, or 33 full-time equivalent employees.

Findings: *Estimated Correctable Labor Inefficiency Cost*

Combining the effects of staffing and wages is a measure of a cooperative's labor efficiency. Whether we look at payroll as a function of megawatt hours, number of customers, or distribution line miles serviced, the payrolls of Alaska's cooperatives far exceed national norms. Even after making cost of living corrections, CEA, MEA and HEA all fall in the bottom 10% of the 861 co-ops in net labor efficiency. CEA would need to reduce distribution payroll by 47% to achieve just average national labor efficiency for a co-op of its size. Striving to be in the top 10 percent or even the top quartile in efficiency would require still further cost reductions.

For G&T and distribution combined, these inefficiencies cost the ratepayers at CEA over $11 million a year -- about 12% of the retail rate of 8.1¢ per kwh (1.0¢). Future CEA management ultimately has the ability to eliminate these inefficiencies by more careful management of the cooperative.

Findings: *Estimated Non-correctable Labor Inefficiencies from Past Capital Projects*

Low labor productivity and excessive wages on past capital projects continue to be charged to the ratepayers as excess interest and amortization of the cooperative's long term debt. Such costs are now estimated to be $7 million a year. These costs are now unavoidable and are beyond any future management's ability to correct. They will continue over the life of the asset in addition to the $11 million in controllable labor inefficiencies previously described.

Findings: *Summary of All Labor Inefficiencies*

The total labor inefficiencies (both correctable and non-correctable) at CEA add up to about $18 million a year -- 18% of the retail rate of 8.1¢ per kwh (1.4¢).

Recommendations:

Results of this review indicate that CEA is clearly among the least efficient distribution co-ops in the U.S. Labor wage rates are extremely high and there appears to be substantial overstaffing. The benefits that CEA members should be enjoying as residents of a resource-rich area with the nation's lowest cost natural gas input fuel cost are not being realized. CEA retail electric rates are above the national average.

A complete audit and process review of all CEA operations (both distribution and generation & transmission) by a nationally-recognized authority with benchmarking and electric utility management and redesign expertise is warranted. It should make specific operational recommendations with an ultimate goal of achieving improvements that would place CEA in the upper quartile of co-ops nationally in the economically efficient delivery of services to its member-ratepayers.