



**Office of Electricity and Gas  
Markets**

**TCPR & GDPR Employment  
Cost Benchmark**

October 2006

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## 1. Introduction

- 1.1 The Office of Gas and Electricity Markets ('OFGEM') has invited The Inbucon Group (Inbucon) to tender for a project to study the cost of employment to ensure that "Consumers of network monopolies (should expect to) pay the efficient cost of providing a competitive package of pay and other benefits, including pensions ... in line with comparable benchmarks" (OFGEM's policy as outlined in DPCR4).
- 1.2 Due to the exposure that OFGEM may be subject to from the Competition Commission, if it were to carry out the project in-house, it has been necessary for OFGEM to seek independent advice on employment costs at three of the organisations that fall under its remit: National Grid (NG), Scottish and Southern Energy (SSE) and Scottish Power (SP).
- 1.3 Specifically, OFGEM has asked for an independent report on the following:
  - (a) the total current employment costs for each organisation, including salaries, benefits and national insurance;
  - (b) an assessment of the total employment costs for each organisation against the market and each other; and
  - (c) projected employment costs for each organisation for the years 2006 – 2012.

### *Data Sources*

- 1.4 The principal resources available to Inbucon are the following:
  - (a) current and projected salary and benefit costs for each company,
  - (b) existing internal benchmarking studies by the companies,
  - (c) each company's grade structure,
  - (d) job descriptions for benchmark jobs in each grade, and
  - (e) salary and benefit information from the comparator groups.
- 1.5 Our data sources also include our own Inbucon database which we have extensively used on previous benchmarking projects. The data held is checked with competitors to check and ensure that the information we utilise is in line with market data.
- 1.6 Inbucon's salary databases include the UK Survey of Executive Salaries and Benefits. This is now in its 44th year of publication and is one of the UK's most authoritative sources of executive management remuneration data. The remuneration data is analysed by job, level (rank), organisation size, business sector, geographical region and status.
- 1.7 We have also used the following data sources:
  - (a) IDS Pay and Benchmarking reports and its report on Pay in the Electricity, Gas and Water Industries 2006
  - (b) Prospect, the Engineering, Science and Management Union
  - (c) Sector Skills Development Agency
  - (d) Office of National Statistics
  - (e) The Institution of Engineering and Technology
  - (f) The Engineering and Technology Board
  - (g) HM Treasury – Forecasts for the UK Economy (August 2006)
  - (h) Bank of England – Inflation Report (August 2006)



- (i) Deloitte – Economic Review (Third Quarter 2006)
- (j) National Institute of Economic and Social Research

### ***Methodology***

- 1.8 The report has been separated into five sections, each of which covers a key OFGEM requirement. Each section has its own detailed notes on methodology however, for completeness, we have included an overview of the methodology followed for the entirety of the project below:
- (a) The project brief was refined and agreed during meetings between OFGEM and Inbucon.
  - (b) Inbucon requested data from NG, SSE and SP via OFGEM using a question log.
  - (c) NG, SSE and SP provided data in response to the logged questions via OFGEM.
  - (d) Inbucon then contacted NG and SP directly in order to clarify the responses received. In most cases this was done via telephone conversations, although a face-to-face meeting was held with NG. Inbucon has not spoken to SSE directly during the course of this project.
  - (e) Inbucon analysed the data and responses and produced this draft report.

### ***Approach – Overriding Principle***

- 1.9 We have approached this project from a holistic (or “top-down”) perspective.
- 1.10 As such, our analysis is not intended to be completely accurate at the individual or detailed level. It is not possible to do this within the scope of this assignment with the information available. Rather, we have sought to provide an independent, overall assessment of the total employment costs of the companies and general advice on employment costs for similar levels/skills in the market.
- 1.11 For various reasons, some of the responses to our initial questions were incomplete in some cases. In these circumstances we have made as realistic an assumption as possible in order to complete the report.
- 1.12 We have listed the key assumptions made in Appendix A and our data requests and the outstanding data in Appendix C.



## 2. Executive Summary

### *Current Employment Costs*

- 2.1 Based on the information provided, we have calculated estimates of the Employment Costs at each organisation for the year 2005/2006.
- 2.2 As stated earlier, we have had to make assumptions in order to arrive at these estimates in some cases. A list of the assumptions made, along with the calculations methodology, is listed in Appendix A.
- 2.3 The table below shows rounded estimates of Employment Costs at each organisation.

Current Employment Costs (2005/2006)	National Grid	Scottish Power	Scottish and Southern Energy
Base Salary	£89,940,000	£7,362,000	£4,661,000
Total Employment Costs	£148,049,000	£11,989,000	£7,289,000

### *Market Assessment*

- 2.4 In our assessment, broadly speaking, each of the organisations is in line with the market. The table below outlines our view on the market position of each organisation.

Market Assessment	National Grid	Scottish Power	Scottish and Southern Energy
Inbucon Estimate	1.025 - 1.05	0.95 - 1.00	0.95 - 1.05

- 2.5 We note that NG and SP have recently carried out detailed reviews of their reward systems and processes, and each is in the process of implementing a new grade structure with salary ranges that are closely tied to the market. Both organisations have also introduced a philosophy and system in which progression through grades is closely linked to performance and the attainment of competencies.
- 2.6 From the information available, our view is that both of the new systems are commercial in their outlook and design and consistent with good practice in the market. We should note that our comment is based on the information published in the IDS report on Pay in the Electricity, Gas and Water Industries as we did not receive information on these systems directly from the organisations.
- 2.7 However we would like to comment on the following:
- NG has selected private sector organisations with a turnover greater than £500m as its comparator group. In our opinion this is not appropriate as it includes too many organisations that are not comparable with NG (i.e. they are of a different scale to NG and/or operate in different industries). We recommend that this comparator group is reviewed.
  - Although we have concluded that NG is broadly in line with the market, some of the data provided suggests that NG may be positioned slightly above the market, in base salary terms, at the lower grades. It is difficult for us to be confident that this is the case from the information provided, however, in our opinion, it is



worth further review.

- (c) Also, Hay found in their “Report on Salary Management Policy and Practice” that, on average, Total Remuneration is at or above the market median for NG employees with a defined benefit pension, and close to the market median for NG employees with a defined contribution pension. Hay noted that the NG defined benefit pensions are above the median, when compared with all pensions in the market. We agree with this assessment based on the information provided.

### *Projected Employment Costs*

- 2.8 On average, we expect Employment Costs to increase by approximately 3.44% per annum in the next six years. We expect RPI to increase by approximately 2.42% over the same period, so, in real terms, we expect Employment Costs to increase by approximately 1% per annum over the next six years.
- 2.9 In arriving at this estimate we have taken the following into account
- (a) Base salary growth tends to be correlated with changes in the Retail Price Index (RPI). Our research shows that, historically, salary growth tends to be within 1.7% - 1.9% above RPI. We have used a benchmark figure of 1.75% above RPI for our calculations.
- (b) Allowances and overtime increase at a lower rate than base salaries. In our view, these tend to increase at a rate between 1/3 and 1/6 of the annual increase in base salary.
- (c) We have estimated that pensions and benefit costs will remain constant at each organisation over the next six years.
- (d) We concluded that there is a skills shortage in the Energy and Utilities and this may increase the salary costs for organisations within this sector. We have allowed an increase in Base Salary of approximately 3% over the next six years to account for this possibility.
- 2.10 Our projected employment costs are listed in the table below (rounded to the nearest ‘000).

Organisation	2006	2007	2008	2009	2010	2011	2012
National Grid (£)	£148,049,000	£153,038,000	£158,139,000	£163,466,000	£169,028,000	£174,836,000	£180,901,000
National Grid (% increase)		3.37%	3.33%	3.37%	3.40%	3.44%	3.47%
Scottish Power (£)	£11,989,000	£12,395,000	£12,812,000	£13,247,000	£13,701,000	£14,175,000	£14,671,000
Scottish Power (% increase)		3.39%	3.36%	3.40%	3.43%	3.46%	3.50%
Scottish and Southern Energy (£)	£7,289,000	£7,542,000	£7,800,000	£8,071,000	£8,354,000	£8,649,000	£8,958,000
Scottish and Southern Energy (% increase)		3.47%	3.42%	3.47%	3.51%	3.53%	3.57%

- 2.11 In calculating these estimates we used the following percentage increases for each year.

	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012
RPI	2.50%	2.40%	2.40%	2.40%	2.40%	2.40%	-
Wage Growth	4.25%	4.15%	4.15%	4.15%	4.15%	4.15%	-
Allowance and Overtime Growth	0.85%	0.83%	0.83%	0.83%	0.83%	0.83%	-
Skills Shortage Premium	0.42%	0.42%	0.42%	0.42%	0.42%	0.42%	-



### 3. Current Total Employment Costs (2005/06)

3.1 Detailed tables showing Current Employment Costs are included in Appendix A, however we have reproduced the headline figures in the tables below. Note that these figures are rounded to the nearest '000.

3.2 An overview of the methodology used to calculate these numbers is included on the following page.

#### NG

2005/2006											
Grade	Full Time Equivalent Employees	Total Base Salary Pay	Additional Allowances	Standard overtime	Cost of standard benefits	Car allowance	Pension cost	Bonus cost	Employee share scheme cost	Additional cost	Employer National Insurance
NGC A; TS1 and TS2	619	12,063,000	0	1,452,000	310,000	0	1,809,000	0	93,000	117,000	1,730,000
NGC B; TS3	228	5,440,000	94,000	596,000	125,000	714,000	816,000	0	34,000	43,000	876,000
NGC C; TS4 and TS5	914	25,807,000	891,000	1,769,000	503,000	4,495,000	3,871,000	0	137,000	95,000	4,219,000
NGC D; TS6	683	25,954,000	1,247,000	679,000	410,000	4,568,000	3,893,000	982,000	102,000	71,000	4,279,000
NGC Snr Mgrs; Transco Snr Mgrs	406	20,676,000	282,000	0	244,000	7,889,000	3,101,000	1,613,000	61,000	0	3,899,000
<b>TOTAL</b>	<b>2,850</b>	<b>£89,940,000</b>	<b>£2,514,000</b>	<b>£4,496,000</b>	<b>£1,592,000</b>	<b>£17,666,000</b>	<b>£13,490,000</b>	<b>£2,595,000</b>	<b>£427,000</b>	<b>£326,000</b>	<b>£15,003,000</b>

#### SP

2005/2006											
Grade	Full Time Equivalent Employees	Total Base Pay	Additional Allowances	Standard overtime	Cost of standard benefits	Car allowance	Pension cost	Bonus cost	Employee share scheme cost	Additional cost	Employer National Insurance
A10	2.1	38,000	11,000	2,000	0	0	6,000	0	1,000	0	7,000
B8	65.9	1,231,000	355,000	49,000	0	0	185,000	0	16,000	0	209,000
C6	87	1,892,000	498,000	76,000	0	0	284,000	0	21,000	0	316,000
D4	34.7	561,000	129,000	22,000	0	0	84,000	0	5,000	0	91,000
E3	29.9	1,005,000	178,000	40,000	0	44,000	151,000	50,000	8,000	0	169,000
F2	17.8	1,123,000	182,000	45,000	0	43,000	168,000	56,000	7,000	0	185,000
O5	22.1	821,000	119,000	33,000	0	29,000	123,000	41,000	4,000	0	134,000
DPC	10.4	494,000	0	0	6,000	46,000	74,000	99,000	2,000	0	82,000
PC	2.9	197,000	0	0	2,000	16,000	29,000	59,000	1,000	0	35,000
<b>TOTAL</b>	<b>273</b>	<b>£7,362,000</b>	<b>£1,472,000</b>	<b>£267,000</b>	<b>£8,000</b>	<b>£178,000</b>	<b>£1,104,000</b>	<b>£305,000</b>	<b>£65,000</b>	<b>£0</b>	<b>£1,228,000</b>

**SSE**

2005/2006											
Grade	Full Time Equivalent Employees	Total Base Pay	Additional Allowances	Standard overtime	Cost of standard benefits	Car allowance	Pension cost	Bonus cost	Employee share scheme cost	Additional cost	Employer National Insurance
SSE 1	0	0	0	0	0	0	0	0	0	0	0
SSE 2	0	0	0	0	0	0	0	0	0	0	0
SSE 3	15	242,000	28,000	81,000	0	0	42,000	0	11,000	0	45,000
SSE 4	32	608,000	59,000	160,000	0	0	111,000	0	23,000	0	106,000
SSE 5	12	256,000	22,000	59,000	0	0	53,000	0	9,000	0	43,000
SSE 6	3	72,000	6,000	11,000	0	0	15,000	2,000	2,000	0	12,000
SSE 7	10	268,000	19,000	27,000	0	0	56,000	9,000	7,000	0	41,000
SSE 8	19	571,000	35,000	23,000	0	0	106,000	26,000	14,000	0	84,000
SSE 9	33	1,112,000	61,000	24,000	0	0	220,000	61,000	24,000	0	161,000
SSE 10	17	642,000	31,000	13,000	0	0	123,000	37,000	12,000	0	93,000
SSE 11	21	890,000	39,000	0	0	0	175,000	65,000	15,000	0	127,000
TOTAL	162	£4,661,000	£300,000	£398,000	£0	£0	£901,000	£200,000	£117,000	£0	£712,000

**Overview of Methodology**

- 3.3 Current Employee Costs include estimates for salaries, benefits, allowances, bonuses, share plans and National Insurance
- 3.4 Salaries were calculated by multiplying estimates of average salary at each grade by the number of full time equivalent employees at each grade. For SSE we did not receive average salaries for each grade, so we have assumed that the grade midpoint is equivalent to average salary. We have reduced the 2006/07 SSE salary ranges by 3.75% (the 1 April 2006 pay deal increase) to make them consistent with the data used for the other organisations, which covers the 2005/06 period.
- 3.5 Benefits, bonuses and allowances for NG are based on estimates provided during a meeting between NG and Inbucon. The NG HR Contact also provided additional information after the meeting and was available for telephone conversations to clarify aspects of the data. Various assumptions were made in order to calculate the final figures – these were discussed with the NG HR Manager and are listed in Appendix A.
- 3.6 Benefits, bonuses and allowances for SP are based on estimates provided in response to questions listed in the Questions Log. A teleconference was also held between SP and Inbucon. Assumptions have been made in order to calculate the final figures – these were discussed with a contact at SP and are listed in Appendix A.
- 3.7 Benefits, bonuses and allowances for SSE are based on estimates provided in response to questions listed in the Questions Log. Assumptions have been made in order to calculate the final figures – these are listed in Appendix A.

- 3.8 Share plan costs have been calculated by Inbucon consultants using information obtained from Annual Reports and our knowledge of typical practice in similar organisations.
- 3.9 The National Insurance figures for each organisation have been estimated based on 12.8% of salary, allowances and bonus costs.



## 4. Assessment of Current Employment Costs against Market

### Overview of Methodology

- 4.1 Our original intention was to select a typical Engineering and Non-Engineering role at each grade/level within each organisation and assess (or benchmark) these against the market.
- 4.2 However, it has not been possible to do this as we have not received enough information to benchmark Non-Engineering roles against the market for each grade within each organisation.
- 4.3 Consequently, our analysis is based on the following:
- NG – Engineering roles at each grade,
  - SP – Engineering roles at each grade, and
  - SSE – Engineering roles at each grade.
- 4.4 Each benchmark role has been compared with similar or equivalent roles in:
- the Energy and Utilities market
  - the Inbucon database
- 4.5 In conducting the market assessment we have considered two different types of market data:
- Position match market data (i.e. similar roles in similar organisations). The Energy and Utilities market data is primarily position match data.
  - Job evaluation market data (i.e. roles of an equivalent size or value in similar organisations). The Inbucon data is based on job evaluations carried out for the benchmark roles and the data is drawn mostly from Electrical Engineering data sources.
- 4.6 The benchmark roles are listed in the below table.

SSE - Engineering Roles		SP - Engineering Roles		NG - Engineering Roles	
Grade	Job Title	Grade	Job Title	Grade	Job Title
SSE 1	No data supplied	Grade A10	General Duties Assistant	Grade A	Craftsperson
SSE 2	No data supplied	Grade B8	Craftsman (Overhead Lines)	Grade B	Technician
SSE 3	Semi Skilled Operative	Grade C6	Jointer	Grade C	Substations Engineer
SSE 4	Craftsman	Grade O5	Analyst	Grade D	Delivery Engineer
SSE 5	Enhanced Craftsman	Grade D4	Project Engineer	Mgrs & Specialists	Senior Engineer*
SSE 6	Team Manager	Grade E3	Team Leader (Overhead Lines)		
SSE 7	Multi skilled craftsman	Grade F2	Engineering Risk Control Section Head		
SSE 8	Design Engineer	DPC	No data supplied		
SSE 9	Second Engineer	PC	No data supplied		
SSE 10	Senior Control Room Engineer				
SSE 11	Senior Control Room Engineer**				

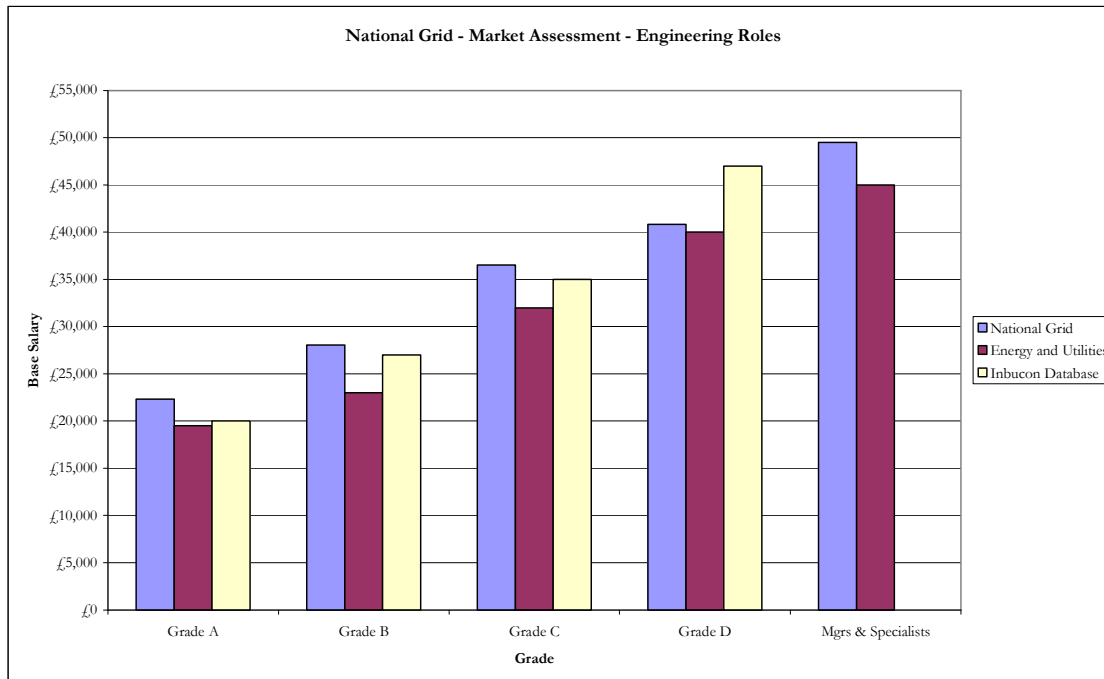
\*This benchmark was obtained from the IDS Pay in the electricity, gas and water industries 2006 survey

\*\* Not included in market assessment as this role was benchmarked at the SSE 10 grade

### Findings

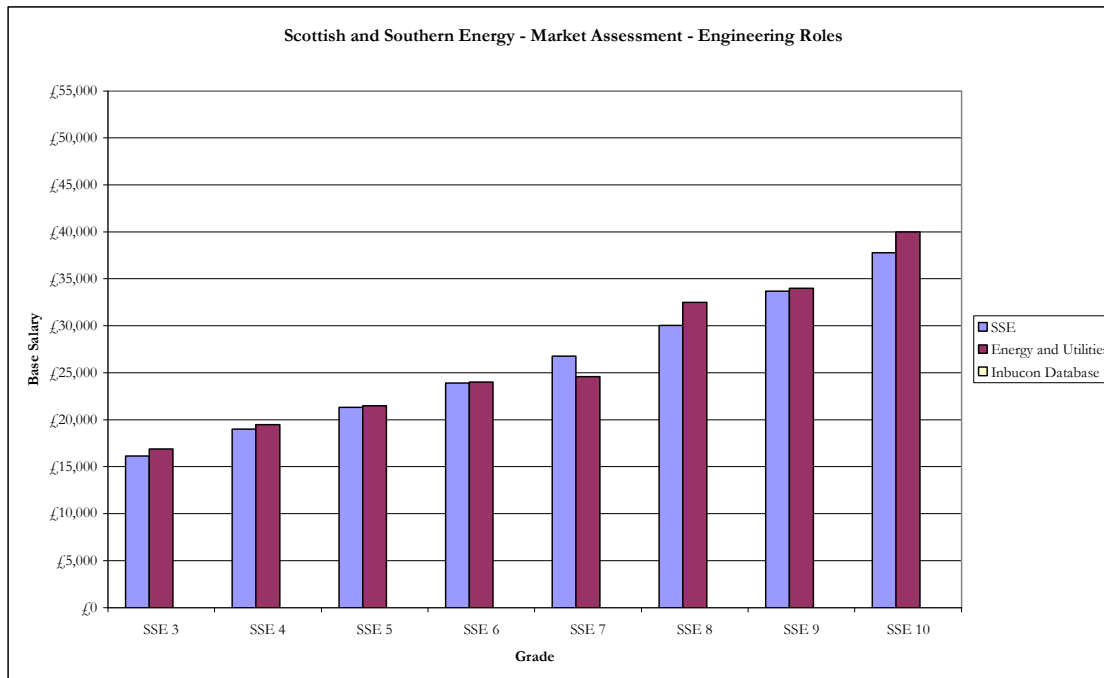
- 4.7 We have outlined the key findings for each organisation, along with some comments, on the following pages.



**NG****Comments**

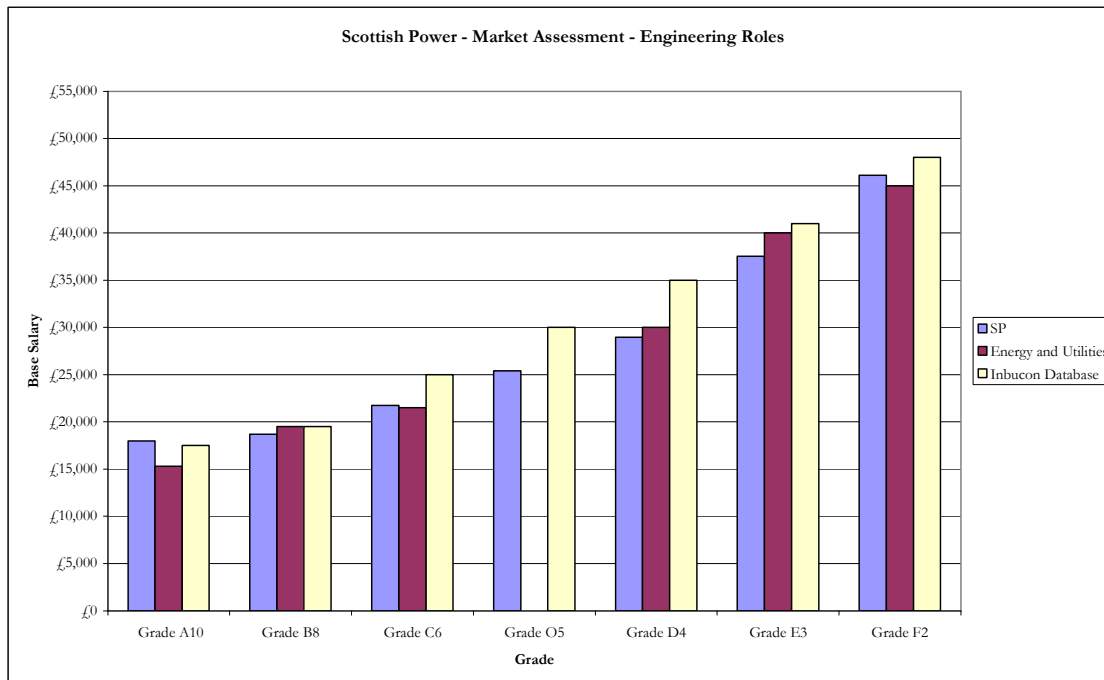
- 4.8 Typically, to be considered market competitive, we would expect pay in an organisation to fit within a range of +/- 10% of the market median (or the organisation's target market position if it is not the market median).
- 4.9 Our analysis shows that, generally speaking, NG fits within this range. So we would conclude that pay is broadly in line with the market at NG.
- 4.10 However, it is worth noting that our analysis shows that pay in the lower part of the organisation is above the market. This is consistent with the findings of the report written for NG by Hay Management Consultants (Hay), although the finding was not highlighted in that report. Note that we provide detailed comments on the Hay report in Section 6 of this report.
- 4.11 The bottom three grades are all above the market, with the second grade (Grade B) well above the market and almost at the upper quartile. We would point out that the bottom three grades comprise 62% of the total number of employees, and 48% of the total base salary costs for transmission staff at NG.
- 4.12 As stated above, our overall conclusion is that pay is broadly in line with the market, however we recommend that positions in the lower three grades are carefully scrutinised to ensure that pay is set at an appropriate level.
- 4.13 We understand that OFGEM requires a numeric estimate of the market position for each organisation. We would estimate this to be in the range 1.025 – 1.075 (i.e. approximately 2.5% - 7.5% above the market median) for NG.
- 4.14 We have not provided Inbucon market data for the Manager and Specialist grade as we did not receive a job description for the benchmark role at this grade and therefore we could not conduct a job evaluation for this role.



**SSE****Comments**

- 4.15 Generally speaking, we consider pay at SSE to be broadly in line with the market.
- 4.16 Note that we did not receive job descriptions for these roles, so we have conducted our assessment based on job titles alone. Best practice is to assess roles using full job descriptions, as job titles are not necessarily consistent across organisations.
- 4.17 As we did not receive job descriptions for these roles, we have not been able to evaluate them, and hence we have not provided data from the Inbucon database.
- 4.18 Note that we have not reported on SSE 1, SSE 2 and SSE 11. We have not reported on SSE 1 and SSE 2 because we did not receive current employment costs for them. SSE 11 has been excluded because we do not have a benchmark role for this grade.
- 4.19 Based on our analysis, we would estimate SSE, as a whole, to be within a range of 0.95 – 1.05 of the market median



**SP****Comments**

- 4.20 Generally speaking, we consider pay at SP to be broadly in line with the market.
- 4.21 We have not provided Energy and Utilities data for Grade O5. The benchmark role for this grade is an “Analyst” and we have not been able to find a position match for this role in our Energy and Utilities sources.
- 4.22 Based on our analysis, we would estimate SP, as a whole, to be within a range of 0.95 – 1.00 of the market median.



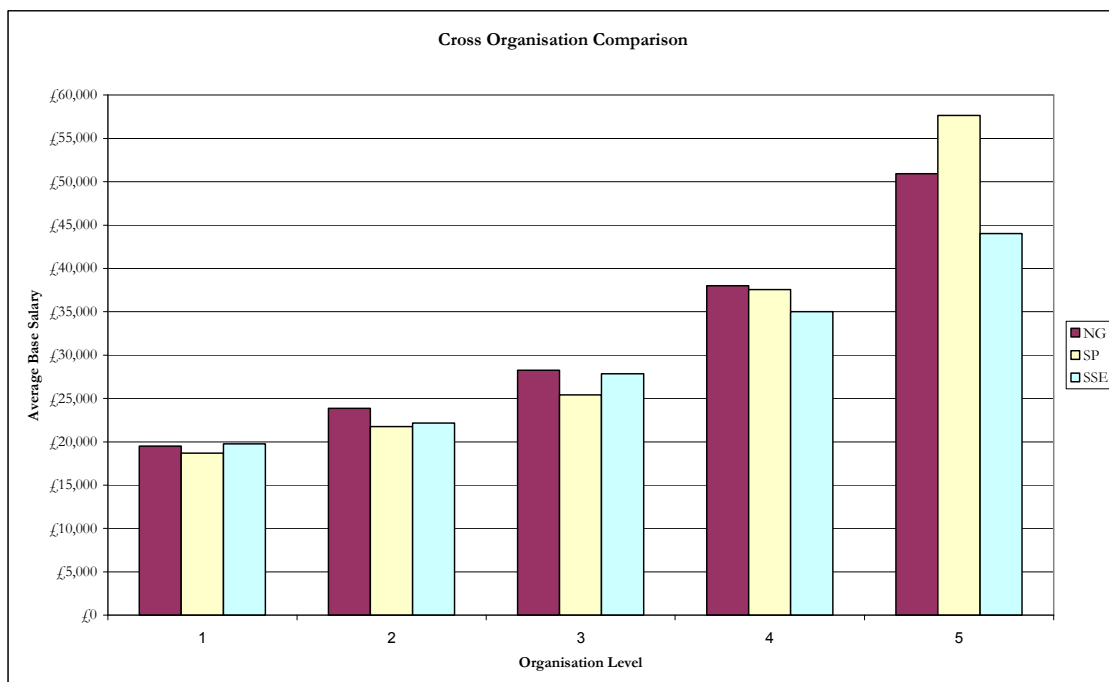
## 5. Cross Organisation Comparison

### *Overview of Methodology*

- 5.1 As part of this assignment, OFGEM asked Inbucon to conduct a cross-organisational comparison in order to establish the pay position of each organisation relative to the other ones.
- 5.2 This is a complicated task and an accurate determination of the relativities would require an in-depth job evaluation study covering all roles in each organisation.
- 5.3 We have not been able to do that as part of this assignment; however we are able to provide an estimate of what the relativities may look like, based on the information we have received from each organisation.
- 5.4 The grade structures at NG and SP are underpinned by Hay Job Evaluation points. As they are both underpinned by the same Job Evaluation system, it is possible to align one grade structure with the other (i.e. Grade A at NG is roughly equivalent to Grade B8 (Org Level 10) at SP because both are at a level roughly equivalent to 150 Hay Job Evaluation points).
- 5.5 Using this process, we aligned the NG grade structure with the SP grade structure.
- 5.6 We then analysed the SSE grade structure, using the benchmark roles, to determine the point at which each SSE benchmark role would fit into the NG structure and the SP structure. This allowed us to align the SSE grade structure with the other two organisations.
- 5.7 In doing so, we have simplified a complex process and we would caution that our findings should be treated as an estimate only.

### *Findings*

- 5.8 Our findings are outlined on the following page.



### *Comments*

- 5.9 The findings are broadly what we would expect to see:
- (a) No major differences between the organisations (this is consistent with our finding that pay at each of the organisations is broadly in line with the market).
  - (b) NG pays slightly more than the other two organisations at the lower grades (again this is consistent with our findings noted in the NG benchmarking section).
- 5.10 Another noticeable trend is pay at the senior levels at SSE seems to fall behind the other two organisations. We should note that the highest organisation level shown in the graph above, Level 5, is very senior level, and this may account for the trend. Organisation Level 5 is equivalent to the Manager & Specialist grade at NG. This is more senior than Grade F2, which is the top grade reviewed as part of this exercise at SP (we had to make an assumption to estimate what the average base salary would be at this level in SP). We did not receive any average salaries for SSE, and consequently we have used the midpoint of the salary spine for each grade. This may account for the lower SSE salary at Organisation Level 5, as it may be that employees are on individual terms at this level of seniority.



## 6. Review of Benchmarking done by Locally Appointed Consultants

### *NG Hay Reports*

- 6.1 NG provided Inbucon with two reports written by Hay: “Real Pay Growth” and “Salary Management and Practice”.
- 6.2 As noted elsewhere in the report, the NG grade structure is underpinned by Hay Job Evaluation points.
- 6.3 Job evaluation is an appropriate system to use for this purpose and the Hay system is well established and respected in the market.
- 6.4 The job evaluation points have then been linked to market data using regression analysis. Again, this is standard practice and is an appropriate mechanism for NG to compare itself with the market.
- 6.5 Hay and NG have defined the market (or comparator group) as private sector organisations with a turnover of £500m or more. The report states that one of the main reasons for choosing this comparator group is because “it is a large sample and therefore statistically robust and includes organisations of a similar scale to NG”.
- 6.6 Inbucon would have advised against using this comparator group. In our view, while taking into consideration the point about statistically robust samples, it is simply too broad a sample. NG’s comparator group includes companies like HSBC and Vodafone which are significantly larger than NG, as well as operating in different industries. Inbucon would argue that these types of companies should not be included.

***Recommendation:*** *We suggest that the comparator group is reviewed to refine it so that it includes companies that more closely match NG’s profile.*

- 6.7 The Hay report states that the target market position for NG is the market median. In our assessment this is an appropriate target position, provided the comparator group is reviewed.
- 6.8 The Hay report states that “pay policy and practice at NG is, on the whole, broadly around the median level”. Inbucon concurs with this assessment, although, as noted elsewhere in this report, we note that base pay is appreciably above the market median at some of the lower grades at NG. NG’s market position for total cash (i.e. base salary plus bonus) position is closer to the median at these grades, but, in our view, this is a reflection of higher bonus levels in the private sector than the utilities sector. If the comparator group is refined to more closely reflect the utilities sector, it is likely that this position will change and the NG roles will be slightly higher than the market under the total cash comparison as well.
- 6.9 The Hay report also analyses the NG market position in respect of Total Remuneration (i.e. base plus bonus plus benefits). The findings are that NG employees are at, or above, the market median if they are in the defined benefit pension and around the market median if the defined contribution pension is used.
- 6.10 Inbucon agrees with this assessment.

### *NG: informal benchmarking done by HR Director*

- 6.11 This data was not supplied due to confidentiality restrictions.



***SSE and SP reports***

- 6.12 We did not receive any benchmarking reports from these organisations, although we understand SP has recently implemented some significant changes to their salary structure and pay management processes.
- 6.13 SP did provide us with a spreadsheet showing Hay market data at various organisation levels. As we do not have a report or further detail on how this information is used at SP we are unable to make any further comments.



## 7. Projection of Current Employment Costs to 2012

7.1 The table below shows our Projected Employment Costs for the organisations to 2012. Note that these are rounded to the nearest '000.

Organisation	2006	2007	2008	2009	2010	2011	2012
National Grid (£)	£148,049,000	£153,038,000	£158,139,000	£163,466,000	£169,028,000	£174,836,000	£180,901,000
National Grid (% increase)		3.37%	3.33%	3.37%	3.40%	3.44%	3.47%
Scottish Power (£)	£11,989,000	£12,395,000	£12,812,000	£13,247,000	£13,701,000	£14,175,000	£14,671,000
Scottish Power (% increase)		3.39%	3.36%	3.40%	3.43%	3.46%	3.50%
Scottish and Southern Energy (£)	£7,289,000	£7,542,000	£7,800,000	£8,071,000	£8,354,000	£8,649,000	£8,958,000
Scottish and Southern Energy (% increase)		3.47%	3.42%	3.47%	3.51%	3.53%	3.57%

### Comments

7.2 On average, we estimate that Employment Costs will increase by around 3% per annum during the period 2006 – 2012.

7.3 Our model shows slightly higher increases at SSE because a higher proportion of their employment costs are salary costs rather than benefits or pensions costs. Our model assumes that pensions and benefits will remain constant over the period.

### Methodology Overview

7.4 We have applied RPI + 1.75% in our calculations for growth in base salary over the period. We have used RPI forecasts produced by HM Treasury.

7.5 We have applied an annual increase of 1/5<sup>th</sup> of the base salary increase in our projections for growth in allowances, car benefits and overtime over the period, as, in our experience, these typically increase at a lower rate than base salary over time.

7.6 We have applied an additional increase of approximately 3% in base salary to allow for possible effects of the impending skills shortage in the sector.

7.7 The table below shows these increases year-by-year.

National Grid	2006/07	2007/08	2008/09	2009/10	2010/11	2011/12	2012
RPI	2.50%	2.40%	2.40%	2.40%	2.40%	2.40%	-
Wage Growth	4.25%	4.15%	4.15%	4.15%	4.15%	4.15%	-
Allowance and Overtime Growth	0.85%	0.83%	0.83%	0.83%	0.83%	0.83%	-
Skills Shortage Premium	0.42%	0.42%	0.42%	0.42%	0.42%	0.42%	-

7.8 A detailed explanation of our methodology is included at the end of this section of the report

### Assumptions

7.9 There are some key assumptions underlying these calculations. The detail and research behind each assumption is outlined on the following pages however, for clarity we have outlined the main assumptions below:

- GDP growth will follow the pattern forecast by the Bank of England (i.e. a slight increase in 2007 and then a decrease to approximately 2.5% in 2010 – 2012).
- RPI will follow the pattern forecast by HM Treasury (i.e. a gradual decrease from current levels to a constant level of 2.4% for the period) (See Appendix B for detail).
- The correlation between RPI and wage growth will be maintained and overall



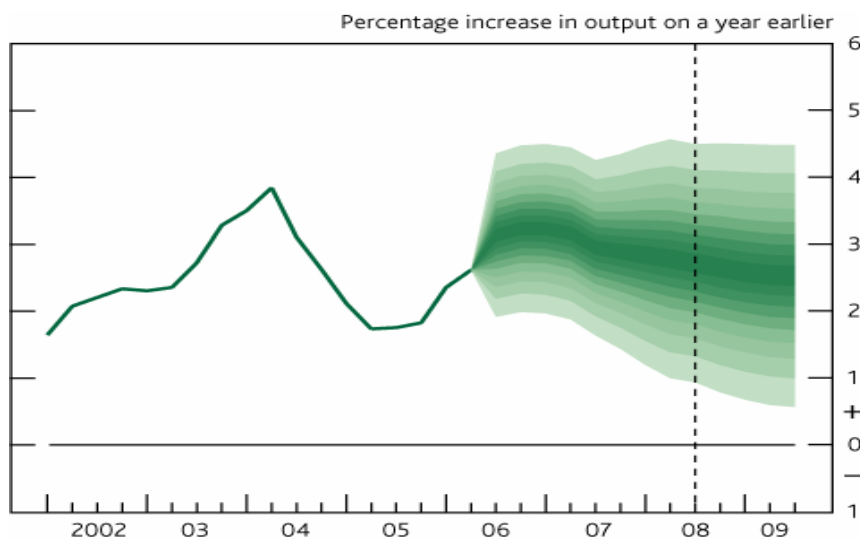
wage growth will continue to fall within a range of approximately 1.5% - 2.0% above RPI.

- (d) Pension costs will remain relatively constant in each organisation.
- (e) Employee numbers will remain relatively constant in each organisation.
- (f) The impending skills shortage in the Engineering profession will exert an influence on the wages bills of the organisations in the next six years.

### ***Research - General Macroeconomic Factors***

#### ***GDP***

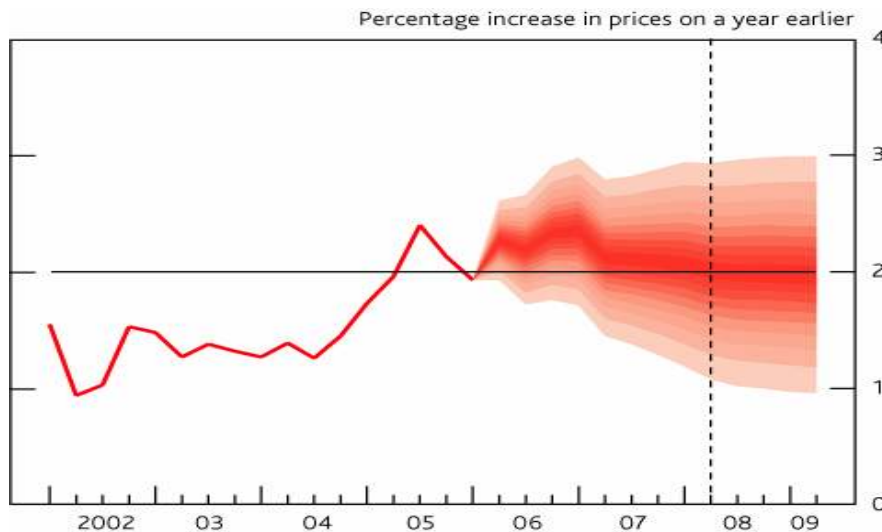
- 7.10 The most recent Inflation Report from the Bank of England (BOE) shows that output growth (or GDP) has increased in the recent past. The key factors underlying this increase are steady growth in consumer spending, a moderate recovery in investment and a small boost from net trade. These were offset by slower growth in public spending.
- 7.11 The BOE's central forecast is for GDP growth to remain around 2.5% in the short to medium term. The chart below shows the BOE growth projections to 2009. The BOE uses the "fan" chart to illustrate the likely upper and lower boundaries, as well as the probability of a particular scenario occurring (i.e. the shading). The darker shading indicates a higher probability.



#### ***Inflation***

- 7.12 We have reported on two measures of inflation in this report: Consumer Price Index (CPI) and RPI.
- 7.13 CPI is the key measure of inflation used by the government. The current target rate is 2%. Our research indicates that there is a reasonable degree of consensus amongst independent forecasters that CPI is set to remain around 2% in the long term, assuming average interest rates of around 2.5% and nominal interest rates of approximately 4.5%.
- 7.14 The BOE "fan" chart on the following page illustrates this point.





### ***RPI***

- 7.15 RPI is a key factor in determining changes in cost of living salary increases. As CPI excludes important factors such as housing costs and council tax, it is an unrealistic indicator with regard to salaries and therefore RPI will always be a more useful indicator of changes to living costs. Wage bargainers overwhelmingly use RPI as their base measure of inflation.
- 7.16 HM Treasury recently published a document summarising independent forecasts for various macroeconomic factors of the UK economy. The average RPI prediction for 2006 was 2.5% and for 2007 it was 2.4%. In the longer term, RPI (excluding mortgage payments) is forecast to drop to 2.4% (see Appendix C for the detail).

### ***Labour Market***

- 7.17 The downward trend in UK unemployment for the past 10 years has recently reversed with the unemployment rate increasing from 2.6% in 2004 to 3.0% in 2005.
- 7.18 This has not been caused by job losses, rather an even greater increase in the size of the workforce. As an example, one measure of the size of the workforce, the number of “economically active” people, increased by 1.5% last year. Put simply, there are more workers in the UK than in previous years. It is difficult to isolate the exact causes for this but it is likely to be due to a combination of the following factors:
- (a) Increased immigration (Deloitte estimated that net migration increased from 300,000 in 2004 to 470,000 in 2005 in their Economic Review for Q3 2006).
  - (b) Changes in demographics (i.e. an increase in the number of people of working age in the population).
  - (c) An increase in the proportion of the population which is either in work or actively looking for work. Deloitte estimated that this may be due to an increasing tendency amongst older workers to remain in the workforce for longer - perhaps partly be due to inadequate retirement provisions.

### ***Wages***

- 7.19 Growth in average earnings has been relatively subdued in recent times and most forecasters expect this to continue, given increases in unemployment and the relatively loose labour market at present. In addition, the National Institute of Economic and Social

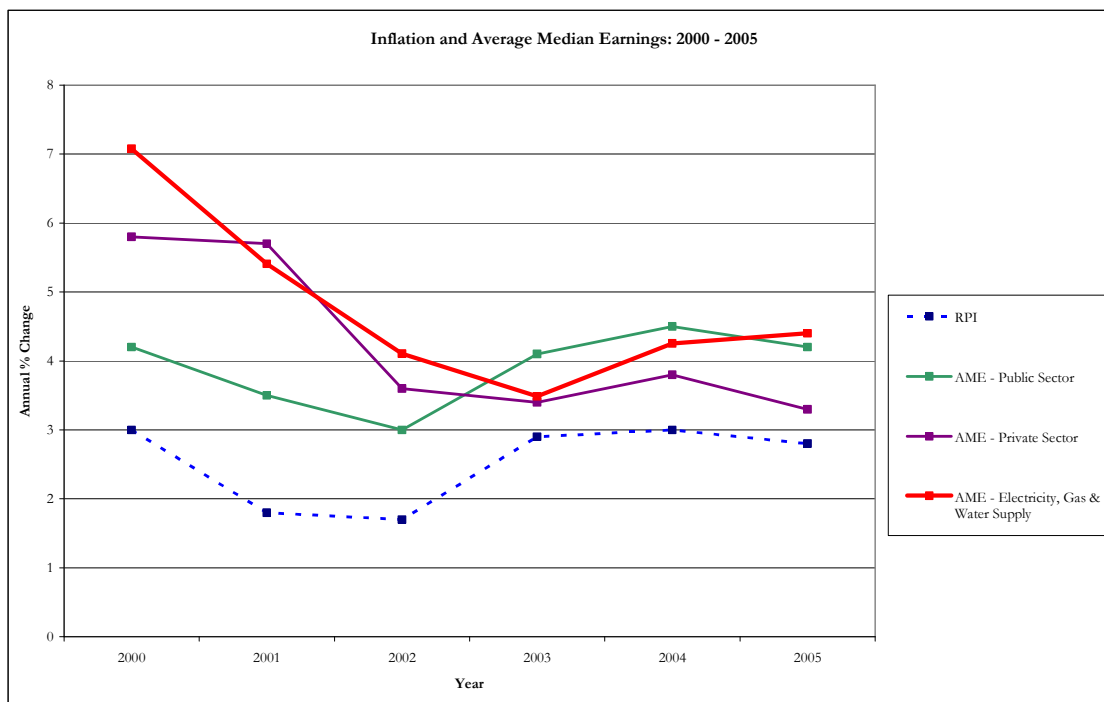


Research recently reported that increased contributions to pension schemes has raised employers' non-wage labour costs, and this is having a dampening effect on wages.

7.20 IDS recently analysed 50 pay settlements in the electricity, water and gas industries in the period April 2005 to April 2006. They found that settlements typically ranged from 3% to 4%, with a median level of 3.5%.

7.21 The chart set out below shows the changes in Average Median Earnings over period 2000:2005 based on data held by the Office of National Statistics (ONS). There are two key points that we wish to highlight:

- (a) the decrease in wage growth over the period for Energy, Gas and Water Supply (down from 7.1% to 4.4%). In addition, the ONS noted that some of the wage growth in 2004 and 2005 may be partly due to employees working longer hours, rather than increases in actual base salary. This makes sense when one considers the IDS finding of a median pay settlement level of 3.5% in 2005.
- (b) the correlation between RPI and the wages curves, reflecting the fact that many wage bargainers use RPI as their benchmark measure of inflation. Our analysis shows that, on average, wage growth was approximately 1.9% above RPI over this period. This figure is consistent with the analysis done by Hay for NG, in which they concluded that wage growth has been approximately 1.75% above RPI over the past ten years.



7.22 In terms of forecasts, the HM Treasury reports that the median wage growth estimate in 2006 and 2007 is 4.2% from a study of various independent forecasters.

7.23 The 2006 CIPD/KPMG Labour Market survey indicates that most employers expect pay rises to be in the region of 3.1% for the upcoming year and the equivalent figure from last year's survey was 4.5%.



## ***Research - Energy and Utilities Labour Market***

### ***Size of Labour Market***

- 7.24 The total number of staff employed by the Energy and Utilities industry declined by approximately 54% between 1990 and 2004 as companies adopted a more commercial outlook in response to privatisation (*Employment and Skills Study of the UK Electricity Industry – Energy and Utility Skills (EUS)*). This is mirrored by the dramatic reductions in headcount and continual reorganisation reported by NG during the same period.

### ***Demand (or Recruitment)***

- 7.25 The EUS report notes that this dramatic decline is not set to continue and total employee numbers are due to remain static, or even reduce slightly (-3%) over the next 5 years. Accordingly, future recruitment in the industry is likely to be based around replacing existing employees (when they retire or leave the industry) rather recruiting for new positions:
- (a) A Working Futures 2004-2014 Sector Report carried out by the Sector Skills Development Agency (SSDA) noted an increase in replacement demand of 32% for the Energy and Utilities Sector for the period 2004-2012, which is slightly below the level forecast for the UK as a whole (36% respectively).
  - (b) The EUS study reports a retirement rate of 2% per annum and a skewed age profile for the industry, whereby approximately 40% of the workforce is aged between 45 and 59. Again, the demographics at NG mirror this, with approximately 44% of the workforce fitting within this age range. Based on these demographics, 8% of the NG current workforce is due to be 60 or older in the next five years.
- 7.26 A recent National Employers Skills Survey found that the Energy and Utilities had more general vacancies than other sectors. However the survey also found that the hard-to-fill vacancies and skills shortage vacancies were no higher than the UK average for all industries. Of the vacancies where there is a skills shortage, the survey found that the skills shortage was typically based around communication or customer interaction, rather than technical knowledge
- 7.27 This is contrasted with the findings of the EUS study, which found that 40% of vacancies in the Energy and Utilities sector are hard to fill. The particular skills gaps were reported to be in:
- (a) Electrical power engineering
  - (b) Specialist engineering
  - (c) Management/commercial/communication

### ***Supply***

- 7.28 The Department of Education and Skills concluded, in a recent report, that the overall position for the UK in terms of Science, Technology, Engineering and Mathematics (STEM) skills is a strong one in comparison to other countries:
- (a) Graduate levels in STEM have increased (1.35m in 1997 to 2.123m in 2004 – a 57% increase).
  - (b) PHD levels STEM have also (127,000 in 1997 to 178,000 in 2004 – a 40%



increase).

- (c) In addition, big strides have been made in the Energy industry in terms of training and attainment of qualifications on courses such as NVQs. The Hay report completed for NG and the EUS report both comment on the progress that Energy organisations have made in this area in recent times.
- 7.29 However these are overall figures – we should point out that the EUS, which looked specifically at requirements for the Energy and Utilities field, noted there has been a reduction in suitably qualified Electrical Engineers (a 7% fall between 1996/97 and 2001/02) which has caused considerable difficulties for Energy organisations.
- 7.30 The Department of Education and Skills also concluded that, in general terms, supply of STEM skills is forecast to meet demand. However, it does note that there are problems with specific areas, and quotes Engineering as an example. The report noted that many graduates in this field do not enter the Energy and Utilities sector, choosing instead to work in industries such as banking and finance or business consulting.
- 7.31 This finding is supported by the EUS study which notes that the industry has a poor image amongst younger graduates (and hence finds it difficult to compete when recruiting at that level). A recent Energy and Technology Board (ETB) research report showed that up to 25% of Engineering and Technology graduates end up working in banking or business.

### ***Research - Organisation Factors***

- 7.32 We have taken the following organisation-specific factors into account when determining our methodology for these projections:
- (a) NG employee numbers are forecast to remain relatively constant (4,533 in 2005/06 to 4,583 in 2012/13). We assumed that this will also be the case for SP and SSE
- (b) Turnover figures of 3% - 4% for SP and 10% - 15% at NG over past few years.
- (c) Historic pay awards at each organisation as shown in table below

Year	Scottish Power	Scottish and Southern Energy	National Grid	
			NG	Transco
2001	2.70%	3.60%	2.85%	
2002	2.30%	1.90%	1.85%	
2003	3.00%	3.55%	3.85%	
2004	3.30%	3.30%	3.13%	4.35%
2005	3.80%	4.50%	3.50%	4.60%
<b>Average</b>	<b>3.02%</b>	<b>3.37%</b>	<b>3.45%</b>	

### ***Detailed Methodology***

- 7.33 We have used the RPI + 1.75% in our calculations for growth in base salary and cash allowances over the period.
- (a) Historically pay deals in these organisations and the industry have slightly lower than RPI + 1.75%, however, it should be noted that overall wage bills typically increase by more than the agreed pay deal (particularly in organisations with low turnover rates) due to individuals progressing through grades and salary spines as they are promoted.



- (b) We have applied a smaller increase to allowances and overtime as, in our experience, these do not increase at the same rate as salaries.
- 7.34 We have assumed that costs for benefits, pensions, overtime and bonus will remain relatively constant (as employee numbers are set to remain at the same level).
- (a) It is possible that bonus levels will increase over time as the organisations manage their fixed costs and align their reward practices with the private sector. However, if this occurs, it is likely to be offset by corresponding decreases in salary growth and overtime (which are lower in the private sector) so we have not factored this into our analysis.
- (b) Pension costs may decrease over time as more individuals move into defined contribution arrangements. However, equally, they could increase due to changes in employee demographics (e.g. as more employees on defined benefit arrangements reach retirement age). We understand that pensions are being looked at in detail as part of a separate exercise and so we have made the simple assumption that these costs will remain the same.
- 7.35 We have adjusted the total base salary bill for each organisation by approximately 3% over the period to allow for possible increases in salary necessary to attract employees to the industry due to the impending skills shortage. We have concluded that there is a skills shortage in this sector, and we estimate that it will begin to exert an influence on employment costs in the next few years.
- (a) It is extremely difficult to quantify this impact and, obviously, it will vary from organisation to organisation depending on factors such as employee demographics and recruitment and retention. We note that 8% of NG employees are due to be 60 or over by 2012 and it is possible that the replacements for these individual will be hard to find and therefore more expensive than the current incumbents.
- (b) We note that many organisations have experienced difficulties attracting young, highly skilled workers due to a negative perception of utilities by this demographic, particularly in comparison with industries like banking. It is likely that salaries will need to increase to overcome this.
- (c) However, it is also possible that many of the older individuals at NG may choose to remain in work past the age of 60 (in line with the trend noted by Deloitte's in their Economic Outlook report) thus delaying any financial impact. Or these employees may be replaced by migrants (particularly from the EU accession countries such as Poland, Romania and Bulgaria) at lower salaries than the current incumbents.
- (d) Based on the above, on balance, we estimate that the most reasonable adjustment is an increase of approximately 3% in overall salary bills over the next six years.
- (e) A brief note on the detail behind this calculation: we have applied an annual skills shortage increase of 0.42%. Due to the compound effects of applying this annual increase over a six year period, the total actual increase over the period attributable to the skills shortage is 2.92% (i.e. approximately 3%).
- 7.36 We also note that there has been a lot of consolidation in the industry since privatisation and many commentators feel that this is set to continue with the smaller UK organisations being attractive targets for larger companies around the world. We have not factored the impact of any consolidation into our analysis.



# Appendix A – Current Employment Costs – Detailed Calculations and Assumptions



**1. Identification of Current Employment Costs****National Grid****Table 1 - Estimate of Total Costs by Grade**

2005/2006											
Grade	Full Time Equivalent Employees (i)	Average Base Pay (ii)	Additional Allowances (iii)	Standard overtime (iv)	Cost of standard benefits (v)	Car allowance (vi)	Pension cost (vii)	Bonus cost (viii)	Employee share scheme cost (ix)	Additional cost (x)	Employer National Insurance (xi)
NGC A; TS1 and TS2	619	12,063,000	0	1,452,000	310,000	0	1,809,000	0	93,000	117,000	1,730,000
NGC B; TS3	228	5,440,000	94,000	596,000	125,000	714,000	816,000	0	34,000	43,000	876,000
NGC C; TS4 and TS5	914	25,807,000	891,000	1,769,000	503,000	4,495,000	3,871,000	0	137,000	95,000	4,219,000
NGC D; TS6	683	25,954,000	1,247,000	679,000	410,000	4,568,000	3,893,000	982,000	102,000	71,000	4,279,000
NGC Snr Mgrs; Transco Snr Mgrs	406	20,676,000	282,000	0	244,000	7,889,000	3,101,000	1,613,000	61,000	0	3,899,000
<b>TOTAL</b>	<b>2,850</b>	<b>£89,940,000</b>	<b>£2,514,000</b>	<b>£4,496,000</b>	<b>£1,592,000</b>	<b>£17,666,000</b>	<b>£13,490,000</b>	<b>£2,595,000</b>	<b>£427,000</b>	<b>£326,000</b>	<b>£15,003,000</b>

**Table 2 - Estimate of Costs per Employee by Grade**

2005/2006											
Grade	Full Time Equivalent Employees (i)	Average Base Pay (ii)	Additional Allowances (iii)	Standard overtime (iv)	Cost of standard benefits (v)	Car allowance (vi)	Pension cost (vii)	Bonus cost (viii)	Employee share scheme cost (ix)	Additional cost (x)	Employer National Insurance (xi)
NGC A; TS1 and TS2	619	19,488	0	2,346	500	0	2,923	0	150	189	2,795
NGC B; TS3	228	23,859	411	2,615	550	3,130	3,579	0	150	189	3,842
NGC C; TS4 and TS5	914	28,235	975	1,936	550	4,918	4,235	0	150	104	4,616
NGC D; TS6	683	38,000	1,826	995	600	6,689	5,700	1,437	150	104	6,265
NGC Snr Mgrs; Transco Snr Mgrs	406	50,926	694	0	600	19,431	7,639	3,972	150	0	2,603
<b>TOTAL</b>	<b>2,850</b>	<b>£160,508</b>	<b>£3,906</b>	<b>£7,891</b>	<b>£2,800</b>	<b>£34,167</b>	<b>£24,076</b>	<b>£5,410</b>	<b>£750</b>	<b>£585</b>	<b>£27,121</b>

**Notes:**

- (i) Added 25% of Support and Business Services FTEs to Core Transmission FTEs to arrive at final FTE figures after discussions with James Gooding. Used the organisation charts provided to derive FTE figures by grade.
- (ii) Calculated using Average Base Salary and FTE numbers supplied in Employee Reward workshop.
- (iii) Figures made up of a shift allowance of 26% of Base Salary (up to a cap of £12,810) and an annual supplement ranging from £2,255 (at Grade A) to £3,930 (for senior managers or staff at Grade D). The figures have been adjusted to reflect the estimated proportion of employees that receive this benefit at each grade (see Assumptions). *Source: IDS Pay in the electricity, gas and water industries 2006.*
- (iv) Calculated by summing average overtime rates for transmission with average overtime rates for business/shared services.
- (v) Figures are made up of estimated private medical costs. Estimates range from £500 per annum per employee at the lower grades, to £600 per annum per employee for senior managers. Estimates are based on Inbucon assessment of typical costs in the market for this benefit. We have assumed there are no other benefits.
- (vi) Used car allowance figures quoted in the Hay Report on Salary Management. The figures have been adjusted to reflect the estimated proportion of employees that receive this benefit at each grade (see 'Inputs and Assumptions'). We have not quantified the cost of perquisite cars which are received by some senior managers.
- (vii) We understand that this will be quantified in detail as part of a separate exercise. We have assumed pension costs of 15% of salary for each employee, based on the information we have received.
- (viii) Bonus estimates were calculated by summing the average award by grade to National Grid staff with the average award by grade to Transco staff.
- (ix) Share plan costs are our estimate of the cash costs associated with the sharesave plan. We have assumed an employee participation rate of 25% and all employees contribute the maximum of £250 per month. We have not include the P&L charges associated with expensing of the options as part of this plan - we estimate these would be in the region £950K based on a participation rate of 40%. We have not been informed of any executive share plans.
- (x) These figures are made up of a London weighting allowance which has been estimated at £2,072 based on an average of information quoted in the *IDS Pay in the electricity, gas and water industries 2006*. The figures have been adjusted to reflect the estimated proportion of employees that receive this benefit at each grade (see Assumptions).
- (xi) National Insurance estimate has been calculated as 12.8% of Base Salary, Allowances, Bonuses and Overtime.

\* The following employees have been excluded: Agency staff, Industrial Staff, Scheme Trainees, and Directors

## National Grid - Current Employment Costs - Assumptions

	Employee Numbers		Shift Allowance Supplement (excluding the standard 26% of salary)			Car allowances			London Weighting			Cost per employee per year for Private Medical	Overtime (£)		Bonus (£)		
	Business Services	Transmission	Annual Increment (£)	Business Services (% emps)	Transmission (% emps)	Amount (£)	Business Services (% emps)	Transmission (% emps)	Amount (£)	Business Services (% emps)	Transmission (% emps)		NG Transmission Staff	NG Business Services	NG transmission	NG Business Services	NG Transco
NGC A; TS1 and TS2	54	565	£2,255	0%	0%	£11,436	0%	0%	£2,072	0%	10%	£500	£2,558	£126	£0	£0	£0
NGC B; TS3	20	208	£2,813	0%	5%	£11,436	0%	30%	£2,072	0%	10%	£550	£2,819	£493	£0	£0	£0
NGC C; TS4 and TS5	82	832	£3,372	0%	10%	£13,182	10%	40%	£2,072	5%	5%	£550	£2,104	£224	£0	£0	£0
NGC D; TS6	81	602	£3,930	0%	15%	£16,722	40%	40%	£2,072	5%	5%	£600	£1,104	£185	£1,858	£1,730	£80
NGC Snr Mgrs; Transco Snr Mgrs	78	328	£3,930	0%	5%	£24,000	85%	80%	£2,072	0%	0%	£600	£0	£0	7.8% of salary		



**1. Identification of Current Employment Costs****Scottish and Southern Energy****Table 3 - Estimate of Total Costs by Grade**

2005/2006											
Grade	Full Time Equivalent Employees	Average Base Salary (i)	Additional Allowances (ii)	Standard overtime (ii)	Cost of standard benefits (iii)	Car allowance (iii)	Pension cost (ii)	Bonus cost (ii)	Employee share scheme cost (iv)	Additional cost (iii)	Employer National Insurance (iv)
SSE 1	0	0	0	0	0	0	0	0	0	0	0
SSE 2	0	0	0	0	0	0	0	0	0	0	0
SSE 3	15	242,000	28,000	81,000	0	0	42,000	0	11,000	0	45,000
SSE 4	32	608,000	59,000	160,000	0	0	111,000	0	23,000	0	106,000
SSE 5	12	256,000	22,000	59,000	0	0	53,000	0	9,000	0	43,000
SSE 6	3	72,000	6,000	11,000	0	0	15,000	2,000	2,000	0	12,000
SSE 7	10	268,000	19,000	27,000	0	0	56,000	9,000	7,000	0	41,000
SSE 8	19	571,000	35,000	23,000	0	0	106,000	26,000	14,000	0	84,000
SSE 9	33	1,112,000	61,000	24,000	0	0	220,000	61,000	24,000	0	161,000
SSE 10	17	642,000	31,000	13,000	0	0	123,000	37,000	12,000	0	93,000
SSE 11	21	890,000	39,000	0	0	0	175,000	65,000	15,000	0	127,000
<b>TOTAL</b>	<b>162</b>	<b>£4,661,000</b>	<b>£300,000</b>	<b>£398,000</b>	<b>£0</b>	<b>£0</b>	<b>£901,000</b>	<b>£200,000</b>	<b>£117,000</b>	<b>£0</b>	<b>£712,000</b>

**Table 4 - Estimate of Costs per Employee by Grade**

2005/2006											
Grade	Full Time Equivalent Employees	Average Base Salary (i)	Additional Allowances (ii)	Standard overtime (ii)	Cost of standard benefits (iii)	Car allowance (iii)	Pension cost (ii)	Bonus cost (ii)	Employee share scheme cost (iv)	Additional cost (iii)	Employer National Insurance (iv)
SSE 1	0	12,830	0	0	0	0	0	0	0	0	0
SSE 2	0	14,388	0	0	0	0	0	0	0	0	0
SSE 3	15	16,133	1,852	5,432	0	0	2,778	0	724	0	2,997
SSE 4	32	19,001	1,852	5,012	0	0	3,472	0	724	0	3,311
SSE 5	12	21,307	1,852	4,946	0	0	4,444	0	724	0	3,597
SSE 6	3	23,894	1,852	3,704	0	0	5,000	617	724	0	3,849
SSE 7	10	26,794	1,852	2,716	0	0	5,556	926	724	0	4,133
SSE 8	19	30,046	1,852	1,235	0	0	5,556	1,383	724	0	4,418
SSE 9	33	33,692	1,852	741	0	0	6,667	1,852	724	0	4,881
SSE 10	17	37,782	1,852	741	0	0	7,222	2,160	724	0	5,444
SSE 11	21	42,369	1,852	0	0	0	8,333	3,086	724	0	6,055
<b>TOTAL</b>	<b>162</b>	<b>£278,236</b>	<b>£16,667</b>	<b>£24,527</b>	<b>£0</b>	<b>£0</b>	<b>£49,028</b>	<b>£10,025</b>	<b>£6,520</b>	<b>£0</b>	<b>£38,686</b>

**Notes:**

- (i) Base Salary figures were calculated by estimating average salary by grade from the salary spine provided by Scottish and Southern Energy. Assumed most employees are placed around the midpoint of each grade.
- (ii) Allowances, overtime, pension and bonuses have been calculated from 2004/05 estimates provided by Scottish Power. A total figure has been apportioned into estimated costs by grade based on the proportion of employees in each grade and the proportion of employees that would typically receive each benefit at each grade (e.g. we have made minor adjustments to reflect fewer employees receiving overtime at the top grades, or fewer employees receiving incentives at junior grades). We have assumed car allowances are included in the additional allowance figures.
- (iii) No separate figures provided for standard benefits, car allowance, or additional costs. We have assumed car allowances are included in the additional allowance figures.
- (iv) Share plan costs are our estimate of the cash costs associated with the sharesave plan and the Share Incentive Plan (SIP). We have assumed employees contribute the maximum of £250 per month and employee participation rate of 25% for the sharesave plan. We obtained an employee participation rate of 48% for the SIP from the company annual report, and have assumed employees purchase shares at the maximum monthly amount (£125). We have also factored in a free share grant of 50 shares made during the year. We have not been informed of any executive share plans. We have not included the P&L charge for the options as part of the sharesave plan - we estimate these would be in the region of £50K, based on a participation rate of 40%.
- (v) National Insurance estimate has been calculated as 12.8% of Base Salary, Allowances, Bonuses and Overtime.

**1. Identification of Current Employment Costs****Scottish Power****Table 5 - Estimate of Total Costs by Grade**

2005/2006											
Grade	Full Time Equivalent Employees (i)	Average Base Salary (i)	Additional Allowances (ii)	Standard overtime (iii)	Cost of standard benefits (iv)	Car allowance (v)	Pension cost (vi)	Bonus cost (vii)	Employee share scheme cost (viii)	Additional cost (ix)	Employer National Insurance (x)
A10	2.1	38,000	11,000	2,000	0	0	6,000	0	1,000	0	7,000
B8	65.9	1,231,000	355,000	49,000	0	0	185,000	0	16,000	0	209,000
C6	87	1,892,000	498,000	76,000	0	0	284,000	0	21,000	0	316,000
D4	34.7	561,000	129,000	22,000	0	0	84,000	0	5,000	0	91,000
E3	29.9	1,005,000	178,000	40,000	0	44,000	151,000	50,000	8,000	0	169,000
F2	17.8	1,123,000	182,000	45,000	0	43,000	168,000	56,000	7,000	0	185,000
O5	22.1	821,000	119,000	33,000	0	29,000	123,000	41,000	4,000	0	134,000
DPC	10.4	494,000	0	0	6,000	46,000	74,000	99,000	2,000	0	82,000
PC	2.9	197,000	0	0	2,000	16,000	29,000	59,000	1,000	0	35,000
<b>TOTAL</b>	<b>273</b>	<b>£7,362,000</b>	<b>£1,472,000</b>	<b>£267,000</b>	<b>£8,000</b>	<b>£178,000</b>	<b>£1,104,000</b>	<b>£305,000</b>	<b>£65,000</b>	<b>£0</b>	<b>£1,228,000</b>

**Table 6 - Estimate of Costs per Employee by Grade**

2005/2006											
Grade	Full Time Equivalent Employees (i)	Average Base Salary (i)	Additional Allowances (ii)	Standard overtime (iii)	Cost of standard benefits (iv)	Car allowance (v)	Pension cost (vi)	Bonus cost (vii)	Employee share scheme cost (viii)	Additional cost (ix)	Employer National Insurance (x)
A10	2.1	17,989	5,372	720	0	0	2,698	0	240	0	3,082
B8	65.9	18,681	5,380	747	0	0	2,802	0	240	0	3,175
C6	87	21,745	5,725	870	0	0	3,262	0	240	0	3,628
O5	22.1	25,403	5,828	1,016	0	0	3,810	0	240	0	4,128
D4	34.7	28,953	5,116	1,158	0	1,260	4,343	1,448	240	0	4,856
E3	29.9	37,547	6,088	1,502	0	1,440	5,632	1,877	240	0	6,202
F2	17.8	46,125	6,663	1,845	0	1,650	6,919	2,306	240	0	7,499
DPC	10.4	47,474	0	0	600	4,380	7,121	9,495	240	0	7,853
PC	2.9	67,769	0	0	600	5,400	10,165	20,331	240	0	11,968
<b>TOTAL</b>	<b>31</b>	<b>£161,368</b>	<b>£6,663</b>	<b>£1,845</b>	<b>£1,200</b>	<b>£11,430</b>	<b>£24,205</b>	<b>£32,132</b>	<b>£720</b>	<b>£0</b>	<b>£27,320</b>

**Notes:**

(i) Calculated using average salary and FTE figures provided. Typical salaries were also provided, however these haven't been used in order to maintain consistency with the methodology applied for the other organisations.

(ii) Figures consist of shift and stand by allowances which were supplied by Scottish Power. Have assumed 40% of employees receive these allowances at F2; E3, and D4; and 60% at C6, B8 and A10.

(iii) Have assumed that, on average, overtime is 4% of base salary (based on information supplied by Scottish Power) and is payable to all employees.

(iv) Standard benefit is BUPA medical for DPC and PC employees. Have assumed that there are no other benefits.

(v) Have annualised the monthly car allowance figures provided. Have assumed 50% of employees receive car allowance at F2, E3 and D4; and 100% at DPC and PC.

(vi) Have used the 15% employer contribution figure provided by Scottish Power.

(vii) Have used the bonus figures provided. Assumed that 50% of roles receive a bonus at F2, E3 and D4. Assumed that 100% of roles receive a bonus at DPC and PC.

(viii) Share plan costs are our estimate of the cash costs associated with the sharesave plan and the ESOP plan. We have assumed an employee participation rate of 25% and all employees contribute the maximum of £250 per month for the sharesave plan. We have not included the P&L charge associated with options as part of this plan - we estimate this would be in the region of £90K, based on a participation rate of 40%. We assumed a monthly match of £50 per month and an employee participation rate of 15% for the ESOP plan. We have not been informed of any executive share plans.

(ix) No figures provided for additional costs.

(x) National Insurance estimate has been calculated as 12.8% of Base Salary, Allowances, Bonuses and Overtime.

\* Staff on Individual Contracts (IC) have been excluded

**Scottish Power - Current Employment Costs - Assumptions**

	Annual stand-by allowance* (£)	Shift Allowance (% of salary)	Proportion of employees receiving allowances	Car allowance (£)	Proportion of employees receiving car allowances	Proportion of employees receiving a bonus
F2	£2,844	20.7%	40%	£3,300	50%	50%
E3	£2,844	21.6%	40%	£2,880	50%	50%
D4	£2,510	22.5%	40%	£2,520	50%	50%
O5	£2,261	23.4%	60%	£0	0%	0%
C6	£2,555	24.3%	60%	£0	0%	0%
B8	£2,555	25.2%	60%	£0	0%	0%
A10	£2,555	26.1%	60%	£0	0%	0%
DPC			0%	£4,380	100%	100%
PC			0%	£5,400	100%	100%

\* £2,555 = £1,147.30 per week multiplied by 52 weeks divided by 3 (as assumed that employees receive this allowance one week out of every three in order to calculate a reasonable figure)



**Appendix B – Forecasts for the Economy - HM Treasury RPI Projections**

	HM Treasury Forecast (compiled from 43 independent financial research companies)					Inbucon Estimate	
	2006	2007	2008	2009	2010	2011	2012
RPI (excluding mortgage interest payments )	2.50%	2.40%	2.40%	2.40%	2.40%	2.40%	2.40%



## Appendix C – Data Requests and Outstanding Data



Data request	Comment on data request	Comment on Data Supplied		
		NG	SP	SSE
Organisation chart.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Pay scales for each band/grade.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Minimum/midpoint/average/max salaries plus any spine points.	Current and historic going back 5 years (with details of in which month the year begins).	Received (no historical average salaries)	Received	Received (no historical average salaries)
Number of incumbents in each grade (detailing numbers full time and part-time).	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Descriptors of jobs within each grade/band.	Current and historic going back 5 years (with details of in which month the year begins).	Not Received	Not Received	Not Received
Turnover rates broken down by grades.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Not Received	Estimate received
Details of any pay deals that have been agreed and are currently under discussion.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Confirmation of pay review date for each band/grade.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Details of any pay reviews given for each band/grade.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Confirmation of any reorganisations announced/anticipated for the future.	Current	Received	Received	Received
<b>Breakdown of current and historic remuneration costs</b>				
Basic salary.	Current and historic going back 5 years (with details of in which month the year begins).	Received	Received	Received
Overtime.	Current and historic going back 5 years (with details of in which month the year begins).	Partially received (best estimate)	Partially received (best estimate)	Overall estimate received
Allowances (and descriptors).	Current and historic going back 5 years (with details of in which month the year begins).	Partially received (best estimate)	Partially received (best estimate)	Overall estimate received
Value of benefits and descriptors).	Current and historic going back 5 years (with details of in which month the year begins).	Partially received (best estimate)	Partially received (best estimate)	Overall estimate received
Value of bonuses (and descriptor including level to be paid at target and max).	Current and historic going back 5 years (with details of in which month the year begins).	Partially received (best estimate)	Partially received (best estimate)	Overall estimate received
Pensions - value of contributions and description of arrangement.	Current and historic going back 5 years (with details of in which month the year begins).	Partially received (best estimate)	Partially received (best estimate)	Overall estimate received
Share awards and options (policy and historic data broken down into individual schemes).	Current and historic going back 5 years (with details of in which month the year begins).	Not Received	Not Received	Not Received
<b>Benchmarking Data</b>				
Job descriptions for ten most common roles in organisation	Current	Received	Received	Not Received
Job descriptions for an Engineering and Non-Engineering benchmark role at each grade	Current (NG and SP asked on telephone). This question was added because not enough data received in response to questions on breakdown in current and historic remuneration costs	Partially received (not enough non-Engineering roles)	Partially received	Request not made
Average salaries for benchmark roles	Current	Partially received (received some average salaries for non-benchmark roles)	Not Received	Request not made
Typical Benefits for benchmark roles	Current (question added because not enough data was received in response to breakdown in total remuneration costs)	Partially received (best estimate)	Partially received (best estimate)	Request not made



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