

# Northern Ireland Electricity – Transmission and distribution price controls 2012-2017

Submission by Prospect to the Competition  
Commission

**May 2013**

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## **Introduction**

1. Prospect is a trade union for professionals throughout the UK. Our members are engineers, scientists, managers and specialists in areas such as defence, energy, environment, heritage, shipbuilding, telecoms and transport. In the energy sector we represent scientists, engineers and other professional and specialist staff in the nuclear and radioactive waste management industries, the wider electricity supply industry and, increasingly, also in the gas industry. We are the largest union in the UK representing professional engineers. Our members are engaged in operational and technical management, research and development, and the establishment and monitoring of safety standards.

2. Prospect views with great concern the price control determination issued by the Utility Regulator for Northern Ireland in response to Northern Ireland Electricity's (NIE) Price Control Submission, RP5. Whilst respecting the Devolution Settlement, it is worth noting at the outset that Northern Ireland will be affected by Westminster's proposals for electricity market reform (EMR). It is therefore important that the Regulatory framework is flexible enough to encourage investment in new plant, new techniques and new skills in the region. The operation of smart grids will be crucial to reducing the carbon intensity of the UK economy. Investment in staff and skills will be crucial to delivering progress.

3. We would emphasise that the Regulatory framework should support energy policy objectives and not inhibit them. To comply with its stated aim of operating in the public interest, the Regulator should therefore focus more on medium to long-term security of supply and environmental issues, and less on the traditional approach focusing on cost minimisation and asset sweating.

4. In our opinion any expectation that labour costs in particular can be maintained at or below inflation over the next 5-year period is simply unrealistic. This view arises not simply from what may be the conventional expectation that a trade union would seek to raise labour costs to further the interests of their members, but rather because it is contrary to the evidence of the growing recruitment and retention challenge for skilled engineers. Securing the skills pipeline is equally as important as securing the right financial framework. We have been contacted by many of our members who already feel that the current salaries offered by NIE are out of step with the rest of the energy sector and are now becoming increasingly disillusioned following the assessment outlined in the Regulator's initial proposals, which was confirmed in the final price control determination.

5. Prospect set out our concerns in our submission to the Regulator's consultation on its Initial Determination in July 2012. We also invited the Regulator to meet with Prospect Officials to further discuss our submission. However the Regulator declined to respond to this invitation and dismissed many of our comments without providing any further data to support the conditions that remained in its final determination. Prospect therefore welcomes the opportunity to make this submission to the Competition Commission and believes that the following points should be considered during its investigation.

## **Demand for engineering skills**

6. Within the local Northern Ireland market, there has been an increase in the number of companies who require experienced power engineers. The recent market opening has offered the opportunity for many new energy supply companies to enter the market. Such companies are very keen to secure ex-DNO staff, whose experience is seen as invaluable to secure as much market share as possible. The introduction of smart grid technology within the UK has encouraged electrical engineering companies to enter the marketplace in order to take advantage of the opportunities created for supplying new equipment. One such company, Kelvatec, is actively approaching NIE staff in order to secure their invaluable experience. The arrival of DONG Energy to the Belfast Harbour estate has created further competition for engineering resources. Indeed a number of our members in NIE have already been approached regarding future employment opportunities. We are also aware that SONI have an on-going requirement for additional experienced engineering staff. A number of NIE staff have been approached and have subsequently left NIE for SONI.

7. The entire UK energy sector is facing a huge challenge with the availability of skilled resources. Some £200bn is required in new energy infrastructure over the coming decade, requiring a doubling of the annual rate of energy investment: The largest network upgrade in over half a century will be facilitated by the considerable uplift in the OFGEM allowance for infrastructure rebuild during DPCR5. But delivery depends also on companies' ability to source a sufficient and appropriately skilled workforce. The Energy and Utility Sector Skills Council has identified evidence of skills shortages and gaps and increasing demand for skilled engineers across the UK, and the National Skills Academy for Power has highlighted the urgency of this challenge, noting that 4 out of 5 employees in the sector is set to retire in the next 15 years. This position is compounded by difficulties in attracting graduate engineers, amidst cross-sector competition for their skills, including an estimated £100 billion investment in the off-shore renewable industry by 2020. This competition for resources has required energy companies to review salaries and incentives both for recruitment and retention. Prospect notes that out of a recent intake of apprentices by NIE, only 50% remained with the company having completed their training, chiefly due to enhanced salaries available to them elsewhere. Having spent considerable time and money on training these new engineers, NIE simply could not provide the level of remuneration to retain them in-house. It is in this context that we are concerned for NIE and its ability to retain the appropriate skilled resources over the coming years.

8. In the past companies like NIE and other DNOs have been able to retain staff because of the perceived benefits of job security. NIE has always been seen as an area of secure employment and we anticipate that this will remain so. However, despite the economic downturn, the energy sector is experiencing unprecedented levels of demand for skilled resources. Job security is therefore becoming anchored around the employee's skills and experience rather than the company that they work for. There is already evidence within NIE's workforce that this is a factor: some skilled and experienced staff have left the company for relatively short term contracts.

9. Therefore within the energy sector RPI is no longer an appropriate benchmark for the retention of existing staff. In practice, real price effects are already having

an impact in the energy sector with many companies offering more attractive packages in order to secure the skills they need. The desire to employ DNO trained staff is becoming increasingly prevalent as it is well recognised that such staff are amongst the best trained within the industry.

10. In response to these issues in our submission to the consultation on the Initial Determination, the Regulator claimed that such movements in the job market have not had a large impact on NIE's business. Prospect believes that if the conditions of the final price control determination stand, the number of employees attracted away from NIE can only rise. In addition, the Regulator should not simply focus on the number of employees moving from NIE to competitors, but the calibre of those employees and the subsequent cost to the business of replacing highly skilled and experienced engineers. NIE having the ability to attract and retain skilled staff is firmly in the public interest; without this NIE will be left with a serious deficiency in skills to operate its business. The outstanding performance of NIE's workforce in restoring power to consumers during the severe weather events in March 2013 and previous winters has shown that alongside reductions in employee numbers from approximately 3000 at privatisation down to 1300 today, NIE has managed to bring about huge efficiencies whilst retaining a dedicated and highly skilled workforce able to maintain the level of service the consumer expects.

#### **Regional variations in pay**

11. In response to our submission to the consultation on its Initial Determination, the Regulator has stated that in its benchmarking exercise it has found that weighted average wages for "professional" and "skilled trade" occupations as recorded in the Annual Survey of Household Expenditure (ASHE) (*sic*) were 10% lower in Northern Ireland than the UK average, and therefore took the view that NIE's wages should be 10% lower than the UK average for DNOs. Prospect questions whether the correct data was used, as it recognises the correct data set to be the Annual Survey of Hours and Earnings.

12. It would be fallacious to assume that a regional pay approach could or should be applied in the context of benchmarking salaries for skilled engineers working for a DNO. Official data confirms that pay varies according to employment sector, age and experience as well as skill level. Research recently undertaken for Prospect by the independent pay analysts at Incomes Data Services confirms that pay for many highly skilled workers is determined by the UK labour market or, in some cases, internationally. Energy companies operate in a world market, with many workers travelling to secure high reward contracts. Conversely, Prospect has evidence of an inability to recruit skilled engineers in areas where pay is being held down.

13. These pressures are already evident in NIE as increasing numbers of highly skilled engineers travel to GB and further afield to secure very attractive contracts. In our submission to the consultation, Prospect questioned the assumption in the Regulator's Initial Proposals that salaries within NIE are above the average in Northern Ireland, and stated that using these average figures is misleading and meaningless. The Regulator responded that they were not convinced by new information that any uplift should be applied. We strongly challenge the subsequently quoted proposal of a 10% gap in salaries for engineering roles at this level. Robust pay comparisons depend on accurate job matching, and any statements that are not transparently based on such evidence should be

discounted. Prospect has carried out a comparison between National rates and Northern Ireland pay rates in manufacturing and primary sectors and for the whole economy. Generally speaking median pay rates are a more reliable guide for pay comparisons, because it removes the extremes. What the data shows is only a small pay gap of up to a few per cent exists at the median level at higher salary bands. The gap for the average is slightly higher; this suggests that the extremes in national pay rates are higher in manufacturing and primary industry sectors. However looking at similar level pay rates for the whole economy, Northern Ireland has a pay lead.

14. Overall what the data shows is that there is no evidence to support the Regulator's case that pay rates for NIE's specialist engineering roles should be 10% lower in Northern Ireland compared to the UK market. Prospect believes that objective benchmarking with comparable roles in a UK market has not been carried out and that, unless corrected, the price control conditions will impact negatively on NIE's capacity to retain skilled employees in the future.

### **Pension Costs**

15. We understand that the Regulator has a legitimate interest in ensuring that pension costs are managed efficiently. We broadly supported the pension principles adopted for RP5 though we expressed concerns about the concept of legally avoidable costs. We made a number of points on the treatment of pension costs to the Regulator in the wake of the Initial Determination and were pleased to see that many of these were incorporated in the allowances given in the final price control determination.

16. The key remaining area of difference on pension costs between Prospect and the Regulator is in the treatment of early retirement costs. The Regulator decided to apply an adjustment of 50% to the cost of providing enhanced pension benefits on early retirement that were not funded at the time. An aligned adjustment was proposed for RP5.

17. The factor of 50%, while lower than the 100% underpinning the draft determination is higher than the factor that applied for RP4 or the factor that Ofgem applies.

18. The Regulator states that the choice of the factor is a pragmatic one. However there is no justification provided in the final determination for increasing the factor to 50%. In the absence of any supporting evidence the increase in this factor must be considered to be arbitrary and unjustified.

19. The Regulator does recognise that an element of efficiency was achieved from early retirement exercises and that consumers benefited from this.

20. It is important to consider the scale of the workforce change that was achieved. Overall headcount has reduced since privatisation from about 3,000 to about 1,300. This reduction was accomplished without disrupting service delivery or without instigating industrial relations issues in what is a highly unionised industry. The scale of efficiency savings could not have been achieved without recourse to early redundancy for some staff and the terms governing such departures were governed by contractual entitlements that predated privatisation. Given the scale of the

headcount reduction Prospect would argue that there was more than "an element of efficiency" achieved in the regulated operations. Overall we believe the Regulator has not made a case for increasing the proportion of these costs that should be disallowed.