

CUAC oral submission to the Australian Competition Tribunal – Public Consultation Forum 6 October 2016

Introduction

CUAC is a specialist consumer organisation established in 2002 to represent the views of Victorian energy and water consumers in policy and regulatory processes.

CUAC has been actively engaged in the current Price Reset in Victoria, including contributing to two submissions made during the AER's determination process as part of the Victorian Energy and Consumer User Alliance (**VECUA**), dated 13 July 2015 and 6 January 2016. Both submissions raised issues regarding the labour price growth rates proposed by the Victorian Networks.

Expanding on the VECUA submissions, CUAC would like to address the Tribunal in relation to CitiPower and Powercor's application for review of the AER's determination of the labour price growth rate for the 2016 regulatory year. The AER determined the labour price growth rate based on the average of the Deloitte Access Economics and the Centre for International Economics forecasts of the rate of change in the wage price index (**WPI**) for the Victorian electricity, gas, water and waste services (utilities) industry (**the EGWW WPI**). CitiPower and Powercor contend that the AER should instead have applied the growth rates for 2016 provided for in their existing enterprise agreements (**EAs**). CUAC wishes to specifically respond to paragraph 134.8 of CitiPower and Powercor's applications, which alleges that the labour price growth rates provided for in the EAs were efficient at the time they were struck.

CUAC will refer to a number of graphs that assist in highlighting the points made in these oral submissions (see appendix). These materials will also be appended to CUAC's written submissions to the Tribunal, which will be submitted in due course.

1) Relevant NER Provisions

CUAC does not intend to address the question of whether an Enterprise Agreement struck under the Fair Work Act is an "applicable regulatory obligation or requirement" within the meaning of rules 6.5.6(a)(2) and 6.5.7(a)(2) of the National Electricity Rules (NER) and section 2D(1)(b)(v) of the National Electricity Law (NEL). This will be a matter in contention between the parties in the proceeding.

CUAC's submissions are directed at whether CitiPower and Powercor's proposed growth rates for 2016 represent *efficient* costs of achieving the opex and capex objectives for the purpose of rules 6.5.6(c) and 6.5.7(c) of the NER. CUAC contends that the AER was correct to reject CitiPower and Powercor's proposed growth rates for 2016 as set out in the EAs, as they were inefficient at the time they were struck.

2) The Enterprise Agreements

The EAs relied upon by CitiPower and Powercor are described at paragraph 103 of their respective applications. In summary, there are three relevant EAs: a combined Powercor/CitiPower agreement with CEPU (**the CEPU EA**), a Powercor agreement with the

ASU, APESMA and NUW and a CitiPower agreement with the ASU, APESMA and NUW **(the ASU EAs)**.

Importantly, CitiPower and Powercor's applications for review are limited to the labour cost growth rate for the 2016 regulatory year, the final year of the CEPU and ASU EAs. CitiPower and Powercor do not challenge the AER's rejection of their revised proposal for labour price growth rates after the expiry of the EAs – from 2017-2020. CitiPower and Powercor's proposal for these years relied upon five-year historical average EA wage growth to forecast labour price growth. This did not take into account broader labour market conditions in the forecast period. CitiPower and Powercor did not challenge the AER's rejection of the remaining 2017-20 period.

The CitiPower and Powercor agreement with the CEPU was lodged with the Fair Work Commission on 26 September 2014. The previous 2011-2013 EA expired on 31 August 2013. Negotiations are likely to have commenced some time before 31 August 2013, perhaps around April 2013. Clearly negotiations failed to conclude by the end of 2013 and presumably were still ongoing shortly before the EA was lodged with the Commission. Based on this, negotiations for the CEPU EA are likely to have taken place between April 2013 and September 2014.

The Fair Work Commission approved both of the ASU EAs on 11 March 2014. The date of the applications is not recorded. The previous ASU EAs expired on 31 October 2013. Based on these dates, the negotiation period for these EAs is therefore likely to have taken place between approximately May 2013 and March 2014.

3) Inefficiency of the EAs

The inefficiency of the 2016 wage growth rates provided for in the CitiPower and Powercor EAs is demonstrated by a comparison with the WPI for all industries, as well as the EGWWI (utilities industry) WPI, which both Networks have accepted as an appropriate basis for the forecast for the 2017-20 regulatory years.

Specifically, the CitiPower and Powercor EAs demonstrate stable annual wage growth rates of 4.5%-4.55% from 2011 to and including 2016, while wage price indices across all industries, including the utilities industry, were declining.

Figure 1 in the bundle is a chart taken from the AER's Final Determination for CitiPower (at page 7-60), which compares the average annual wage increases in newly negotiated EAs since 1998. It illustrates the trends in EAs over time for different sectors and for the overall WPI, as measured by the ABS. It demonstrates that the WPI has declined quite dramatically since 2011 and that specific industries, including the utilities industry have also tracked downwards, albeit with a slight delay.

Figure 2 in the bundle is a chart created for CUAC by consultant Bev Hughson. It shows quarterly changes in the ABS data for WPI and EGWWI since 2008. The blue line representing ABS "Trend" for All Industries shows a declining WPI since 2008. The simple red regression line for ABS EGWWI data illustrates a similar trend.

However, an examination of CitiPower's historical EAs from 2011 shows no such decline.

Table 1 in the bundle summarises the publically available information set out in Clause 16 of each of CitiPower's EAs. These figures are similar for Powercor.

The disjuncture between WPI rates and the wage growth rates provided for in CitiPower and Powercor's CEPU EAs is illustrated in **Figure 3** of the bundle. Figure 3 compares the quarterly changes in ABS data for WPI and EGWWI with the quarterly change in the wage increases in the CEPU EA, represented by the purple line.

While it may have been reasonable to forecast higher than average wage growth in the utilities sector during the period when the 2011-13 EAs were being negotiated, the same cannot be said of the period when the 2013-16 EAs were negotiated.

As set out in Table 1, the EAs for the period 2011-13 included annual wage growth of some 4.5-5% over three years. This higher rate of wage growth in utility EAs was not unexpected given that in 2010-11 mining and related resource construction activity was still strong. In its February 2011 Statement of Monetary Policy, the Reserve Bank of Australia stated:

"Labour cost growth picked up during 2010 broadly in line with the Bank's expectation following low outcomes in the private sector over 2009. This pick-up is consistent with the strengthening in labour market conditions, and as further gradual increase in wage growth is expected as the labour market continues to tighten."

In contrast to the relatively stable outlook that preceded the 2011-13 EA negotiations, the 2013-16 EAs were negotiated in quite a different economic and wage expectation environment. In its February 2013 Statement of Monetary Policy, the RBA reported that by the December quarter 2012, the consumer price inflation index was down to 2.2% over the year. Median inflation expectations for market economists and union officials (excluding the carbon price) were in the order of 2.5% to 2.7%. Consumer inflation expectations had averaged 2% in the three months to January 2013, the lowest level since 1997. By early 2013, the WPI was closer to 3%.

Figure 4 in the bundle illustrates the extent to which WPI declined over the period post 2011.

The change in market conditions highlighted by the RBA is also supported in other public documents. The Australian Government Department of Employment produces a regular report on trends in job growth for different categories of job.

Figure 5 in the bundle illustrates the very sharp decline in the rate of job growth for electrical distribution trades workers in the five-year period to 2016 in both absolute and relative terms. This decline should have been very evident to CitiPower and Powercor negotiators in 2013. The fact that there is some 'recovery' in the 2-year figures highlights the dramatic decline in job growth for electrical tradesmen and women in the 2012-13 periods, at the time when the relevant EAs were being negotiated.

The decline of -26.4% in job growth over the last five years also contrasts markedly with the 10 year employment growth in the same sector of +29.5%.

Rapid declines in job growth in the electrical distribution workers industry to a negative rate by 2013, combined with falling inflation should have provided ample scope for CitiPower and Powercor to negotiate a lower rate of changes in nominal wages for the 2013-16 EA period.

The fact that they did not do so provides evidence that the 2013-16 EAs were not prudent or efficient at the time they were entered into.

4) Cumulative Impact of the 2016 Forecast for Consumers

To conclude, CUAC would like to highlight the cumulative impact on consumers, should CitiPower and Powercor be successful in their application for review on this ground.

CitiPower and Powercor's proposal will not only increase their 2016 revenue allowances, but will also result in increases in their revenue allowance for 2017-20.

As illustrated in **Figure 6** of the bundle, the cumulative impact of the AER's forecasts in real dollar labour cost growth for 2016 and for 2017-20 is 4%. CitiPower and Powercor's revised proposal before the AER suggests a cumulative growth in real dollar labour costs of 14%.

If the existing EAs are used as the basis for forecasting growth rates in 2016 and the AER's forecasts growth rate is used after that date, as contended for by CitiPower and Powercor, then the cumulative growth in real dollar labour costs is 9%. This is significantly higher than the AER's cumulative outcome of 4% real increase in labour costs over CPI growth.

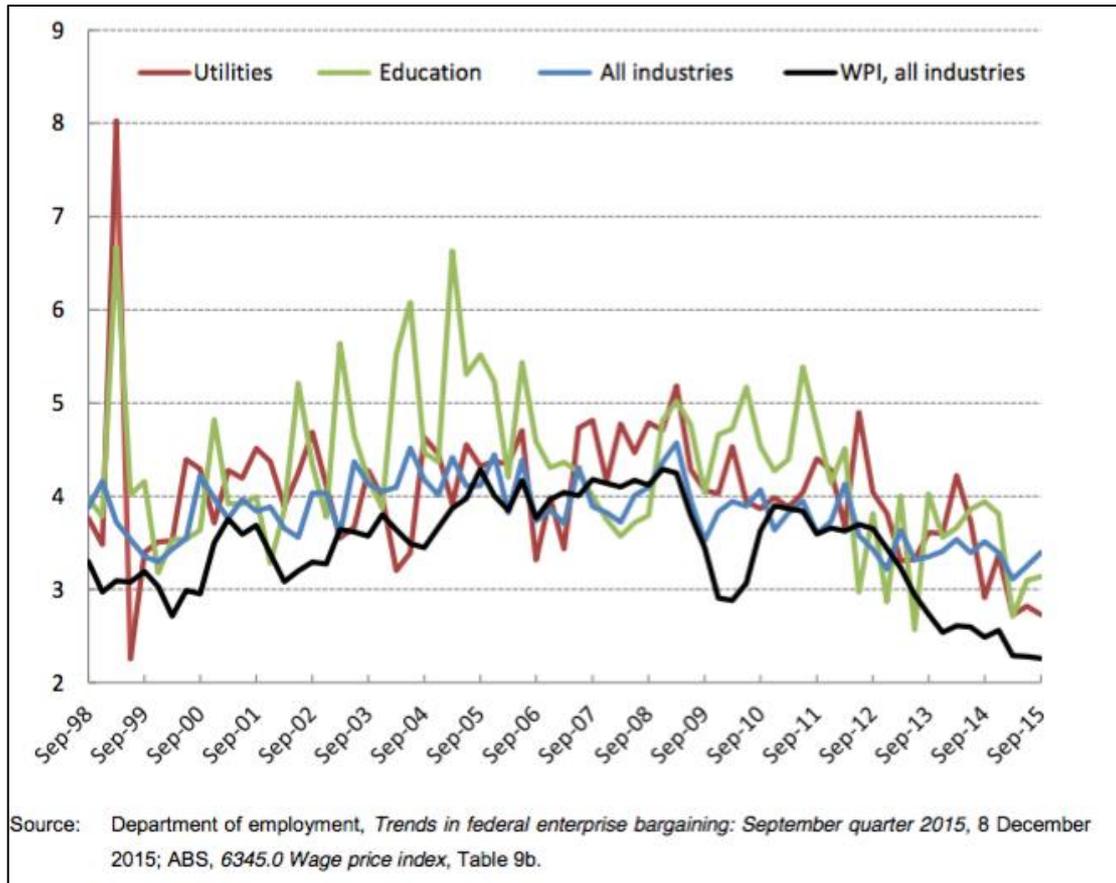
In other words, using the 4.52% nominal labour cost growth rate in the current EAs for 2015 and 2016 (over base year of 2014) leads to an increase of 9% in real dollar labour costs from 2014 base year by the end of the regulatory period.

CUAC therefore submits that a decision in favour of CitiPower and Powercor's contentions will allow both Networks to recover significantly more than is necessary to recover efficient labour costs over each of the five years.

CUAC thanks the Tribunal for the opportunity to present at today's forum. CUAC will provide short written submissions to the Tribunal on this issue for the Tribunal's further consideration.

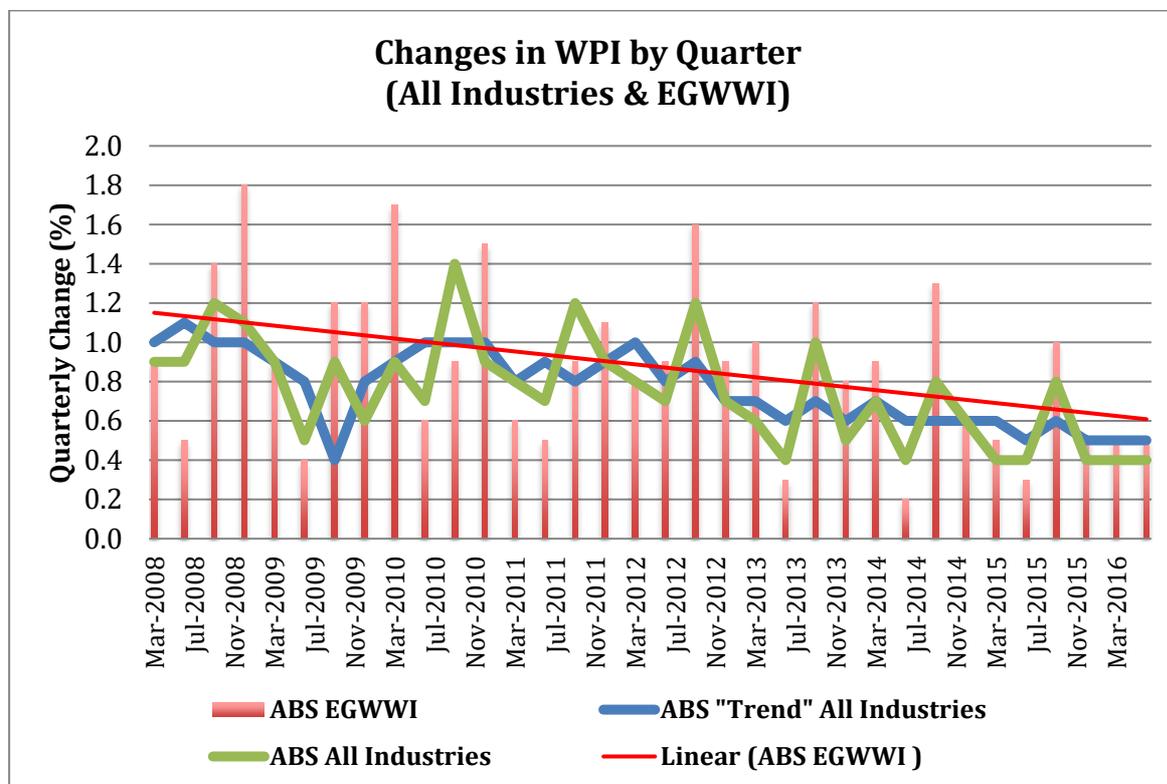
Appendix

Figure 1: Average annual wage increases in newly negotiated enterprise agreements (per cent)



Source: AER, CitiPower Final Decision, Attachment 7, Figure B.1, p. 7-60; Powercor Final Decision, Attachment 7, Figure B.1, p. 7-59.

Figure 2: Labour price growth trend (ABS quarterly WPI data)



Sources: ABS Statistics Report No 634501: Table 9b, “Ordinary Hourly Rates of Pay Excluding Bonuses by Industry, Original (Quarterly Index Numbers) & Table 1, “Total Hourly Rates of Pay Excluding Bonuses: Sector, Original Seasonally Adjusted and Trend”.

Note: ABS provides quarterly “trend” data for “Total Hourly Rates for All Industries” but does not provide this trend data for industry sector EGWWI). The ABS states that the “trend is a measure of the underlying direction of a series”.

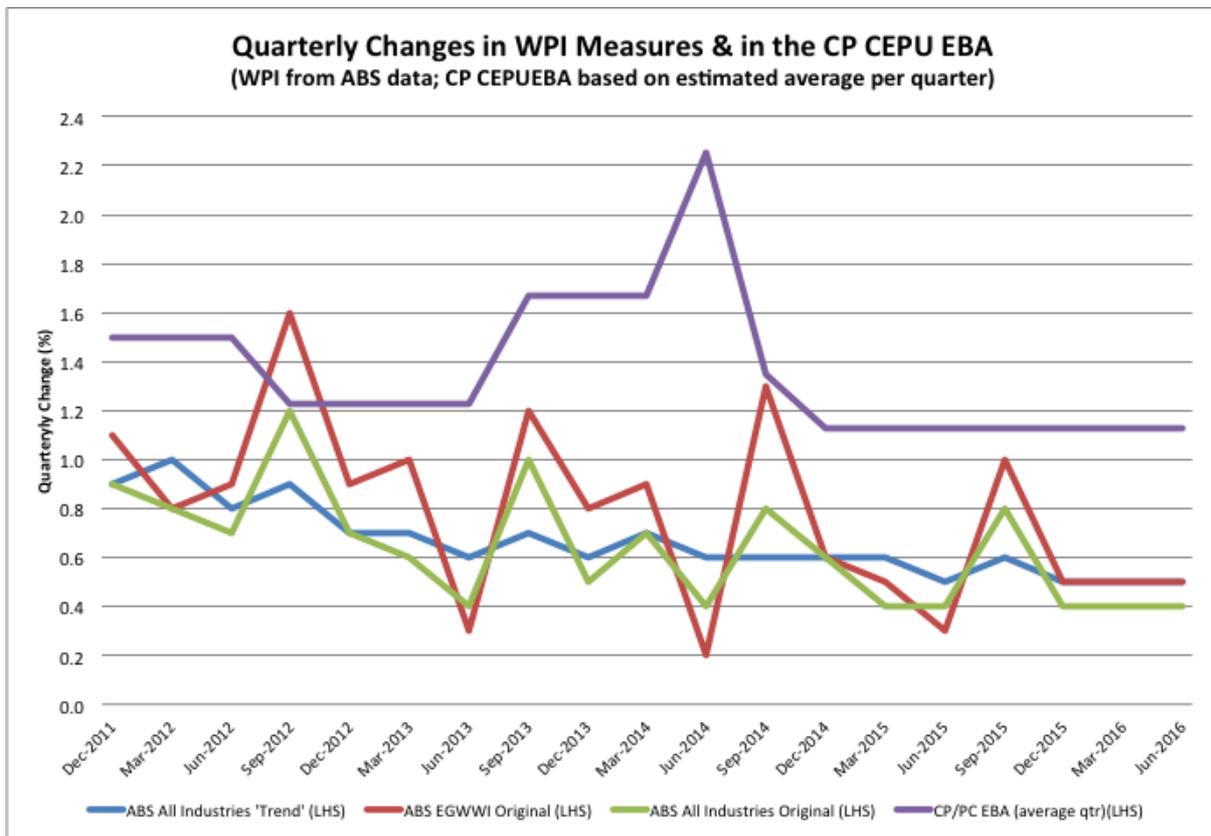
A detailed explanation of the AER’s trend data can be found at <http://www.abs.gov.au/AUSSTATS/abs@.nsf/Lookup/6345.0Explanatory%20Notes1Jun%202016?OpenDocument>

Table 1: Annualised percentage wage growth rates under CitiPower's EAs (nominal \$ increases)

	CEPU 2011-13	ASU 2011-13	CEPU 2013-2016	ASU 2013-16
Year 1	4.5%	4.5%	4.55%	4.5%
Year 2	4.5%	4.5%	4.55%	4.5%
Year 3	5.0%	4.5%	4.55%	4.5%
Cumulative	14.66%	14.12%	14.28%	14.12%

Sources: Citipower Pty (CEPU) Enterprise Agreement 2011; Citipower (ASU; APESMA; NUW) Enterprise Agreement 2011; Powercor Australia Ltd/CitiPower Pty & CEPU Enterprise Agreement 2013-16; Citipower (ASU; APESMA; NUW) Enterprise Agreement 2011.

Figure 3: Quarterly changes in WPI and the CEPU EA

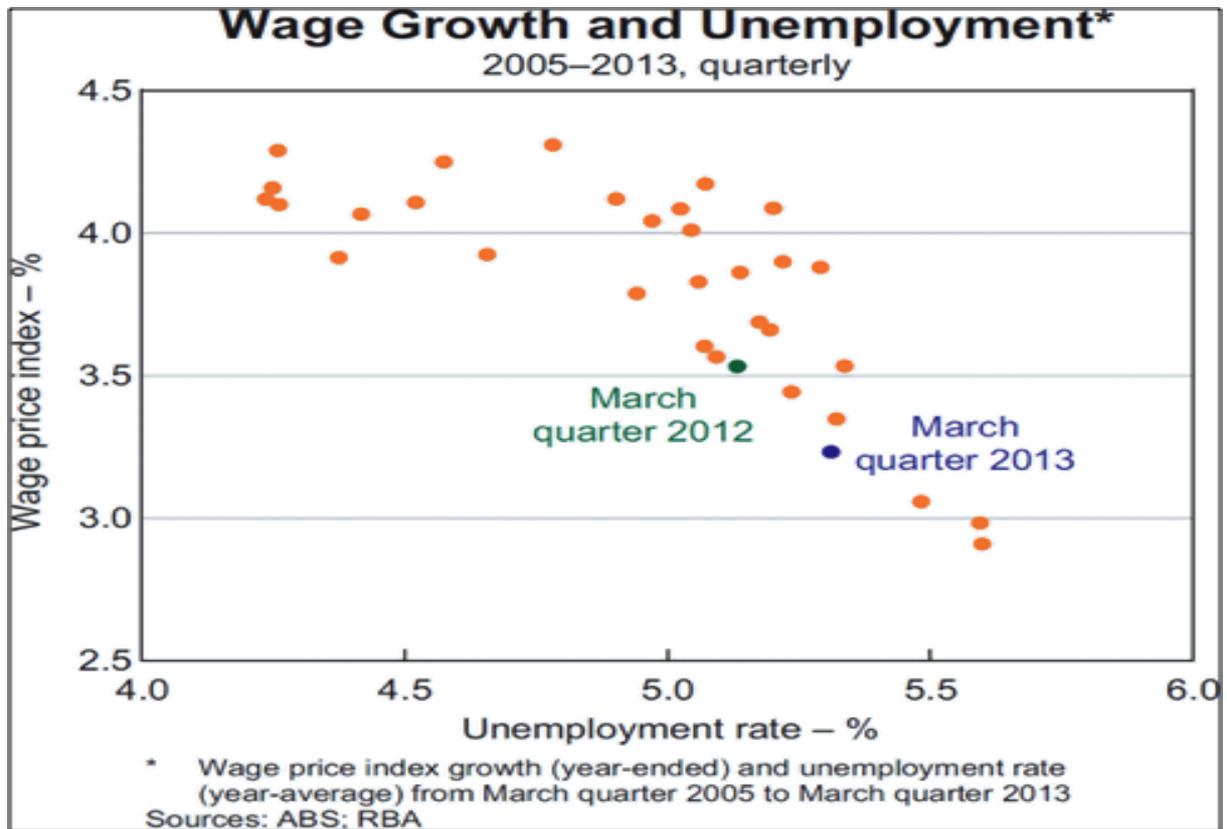


Sources: ABS Statistics Report No 634501: Table 9b, “Ordinary Hourly Rates of Pay Excluding Bonuses by Industry, Original (Quarterly Index Numbers) & Table 1, “Total Hourly Rates of Pay Excluding Bonuses: Sector, Original Seasonally Adjusted and Trend”.

CitiPower, “Rate of Change – MOD 1.39 CP Labour Escalation – Jan 2016, xlsx.”

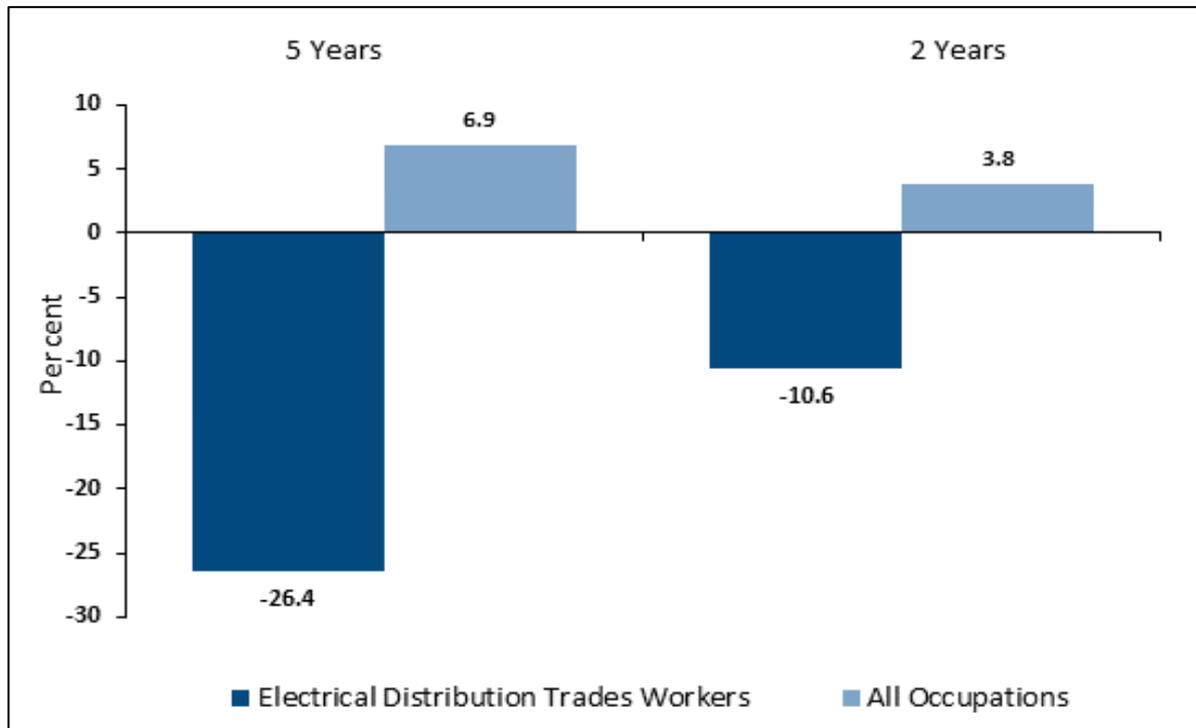
Notes: CP quarterly EA figures are estimated based on CP CEPU agreements for 2011-13 and 2013-16 and the timing of the wage increases in each agreement (as provided by CP in the above spreadsheet). The “spike” in the CEPU data is because the CP EA increased by 2.25% in May 2014 and 2.25% in August 2014. Prorating results in a full 2.25% increase being allocated to one quarter only.

Figure 4: The slowing in wage growth (All Industries WPI)



Source: RBA, Statement of Monetary Policy, August 2013. Graph B1

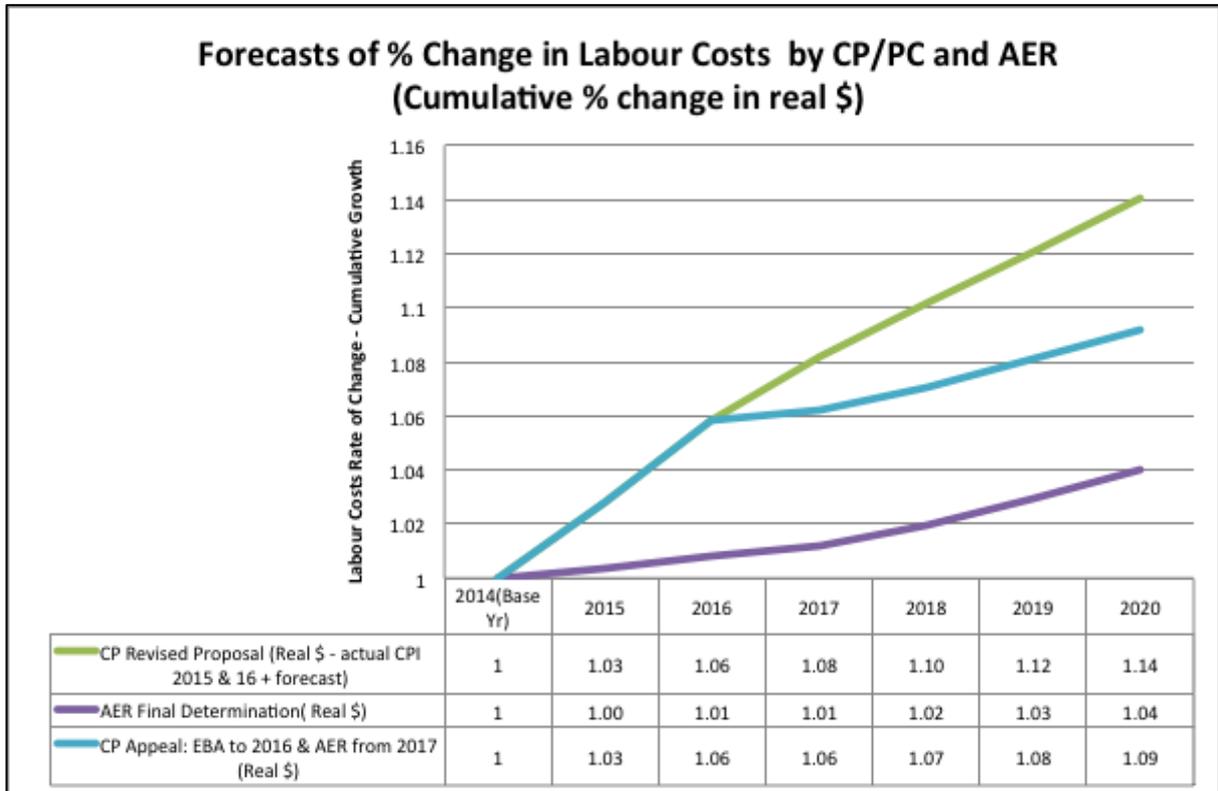
Figure 5: Recent Job Growth for Electrical Distribution Trades versus all occupations



Source: Australian Government, Department of Employment, Job Outlook. Accessed September 2016.

<http://joboutlook.gov.au/occupation.aspx?search=industry&tab=stats&cluster=&code=3422&graph=EG>

Figure 6: Forecasts of Labour Growth Costs by CP/PC and AER (Cumulative %)



Source: AER Final Determination, Citipower – Rate of Change –MOD 1.39 CP Labour Escalation – Jan 2016.xlsm (updated CPI for 2015-2017); CitiPower – Standard Control –MOD 1.36 CP Opex Consolidation – Jan 2016.xlsm

Note (i): CP Appeal based on CP current EA figure for 2015 and 2016 of 4.52% and AER FD forecast for 2017-2020. 4.52% is the nominal labour cost growth in the current EAs, the weighted annualized average of the CEPU and ASU agreements.

Note (ii): Table should be considered indicative of the trends as assumptions by AER and CP for 2015 estimated and updated inflation figures for 2015, 2016 and 2017 used to convert EA nominal growth to real growth.