



Water

SA Water Regulatory Determination 2020: Guidance paper 1



Overview of SA Water Regulatory Determination 2020

November 2018

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Related reading

This Guidance Paper should be read in conjunction with the Framework and Approach paper and other Guidance Papers released by the Commission for SA Water Regulatory Determination 2020. Those papers and other information about SA Water Regulatory Determination 2020, are available on the Commission's website:

<https://www.escosa.sa.gov.au/industry/water/retail-pricing/sa-water-regulatory-determination-2020>

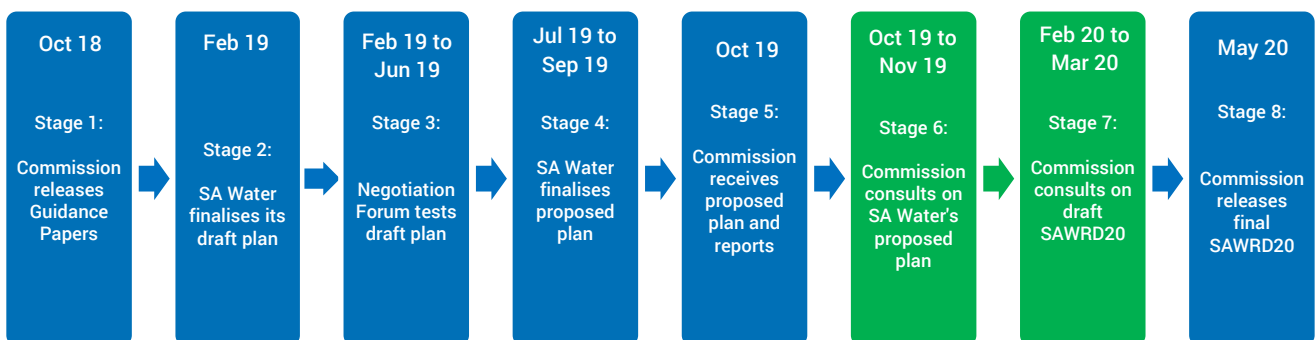
Timing for this review and upcoming consultation opportunities

While the Commission remains responsible for making the final regulatory determination, which will require SA Water to provide the water and sewerage retail services valued by customers for the lowest sustainable cost, the review process will involve multiple opportunities for stakeholders to be involved prior to that final determination.

Input from a diverse range of stakeholders is important, as it helps the Commission to make better informed and more inclusive decisions. The Commission will therefore draw on the full range of evidence provided by all stakeholders in making the final determination.

The timing of the key stages in SA Water Regulatory Determination 2020 are illustrated below, with the Commission's key consultation stages shown in green.

SAW RD20 review timeline



SA Water Regulatory Determination 2020 (SAW RD20) will set maximum revenues and minimum service standards for SA Water's drinking water and sewerage services, as well as setting pricing requirements for other miscellaneous retail services, to apply from 1 July 2020 to 30 June 2024.

SAW RD20 will challenge SA Water to:

- ▶ provide water and sewerage services at the lowest sustainable price for the quality and reliability levels valued by customers, and
- ▶ have in place sound long-term asset management, operating and financing strategies, which support the provision of those services for customers of today and tomorrow.

Those intended outcomes are consistent with the Commission's primary objective of protecting the long-term interests of consumers with respect to the price, quality and reliability of essential services.

Purpose of this document

In July 2018, the Essential Services Commission (**Commission**) established its framework and approach for SA Water Regulatory Determination 2020 (**SAW RD20**), which is intended to deliver the lowest sustainable prices for the services that SA Water's customers value.¹

This is the first of a series of Guidance papers released by the Commission to explain the requirements, methodology and process that will apply to SAW RD20.

This paper provides:

- ▶ an explanation of why SAW RD20 is important for customers of SA Water
- ▶ a description of the overall regulatory context (not limited to the Commission's regulatory role) within which SAW RD20 is to be made
- ▶ an overview of the Commission's current approach to regulating SA Water
- ▶ a summary of SA Water's performance under the Commission's regulatory framework since 2013
- ▶ an explanation of why the Commission is seeking broad-based evidence which it can draw on when making SAW RD20
- ▶ information on how the SAW RD20 process will allow stakeholders to get involved and provide that evidence
- ▶ an overview of the contents of the Guidance Papers, and
- ▶ a proposed approach for evaluating the effectiveness of SAW RD20.

The Commission's July 2018 Framework and Approach paper sets out the process that will occur over the coming two years leading up to the making of SAW RD20. A key element of the initial stages of that process is the release of this suite of Guidance Papers. The Guidance Papers are intended to inform all stakeholders of the Commission's initial positions, principles, requirements, methodology or guidance on matters relevant to the determination.

¹ SA Water Regulatory Determination 2020, Framework and approach, July 2018, available <https://www.escosa.sa.gov.au/projects-and-publications/projects/water/sa-water-regulatory-determination-2020-framework-and-approach>

This will allow stakeholders to focus their resources on issues that will ultimately matter for consumers, rather than discovering (and responding to) the Commission's positions only towards the end of the process. Importantly, SA Water is to take into account the matters set out in these papers when preparing its initial business plan, which will form the basis of consultations with its customers, stakeholders and other participants in the lead up to the making of SAW RD20.

Why is SAW RD20 important?

Since 2013, the Commission's economic regulation regime, established under the Water Industry Act 2012, has been effective in supporting SA Water's delivery of lower-priced and more customer-focused services. Under that regime, SA Water has delivered real revenue and price reductions to customers, maintained service levels and improved its asset management capability. SA Water's drinking water and sewerage revenues are now approximately \$110 million per annum lower than the annual revenue outcomes in 2012, in real terms.

The next stage in the ongoing economic regulatory process will be the making of a new regulatory determination to take effect in July 2020 (**SAW RD20**). The Commission will be determining the revenue controls and the service standards to apply to SA Water's customers from 1 July 2020 to 30 June 2024. In particular, it will set:

- ▶ customer service standards that are based on consumers' preferences, reflecting the service levels that customers are willing to pay for, and
- ▶ SA Water's maximum revenues for drinking water and sewerage services based on the efficient costs of providing those services, and consistent with the service standards set by the Commission and other regulatory obligations.

SA Water will continue to be responsible for setting prices that must be consistent with the revenue controls.

The Commission has established a framework for SAW RD20 that will:

- ▶ put customers' interests and the consumer voice at the centre of the regulatory process
- ▶ provide opportunities for the early identification and resolution of issues and provide up-front clarity on regulatory issues
- ▶ obtain an earlier and wider range of evidence on matters relevant to the determination – particularly customer views – and to maximise the potential of existing bodies and knowledge bases (including other regulators and the Commission's and SA Water's consumer advisory committees)
- ▶ embed SA Water's focus on ownership of its performance, the customer relationship and engagement and obtain a wider range of views to deliver a regulatory business plan to apply from 1 July 2020 (business plan) that meets customers' expectations, and
- ▶ introduce direct customer testing and negotiation into the preparation of SA Water's draft business plan, in a constructive approach, including through the use of a Negotiation Forum.

SAW RD20 operates within a broader policy framework

SA Water is a government-owned provider of water and sewerage services. Its primary role is to source, treat, distribute and sell drinking water and non-drinking water, and to remove, treat and dispose sewage from homes and businesses.² Those essential services are highly regulated, including service level and revenue regulation by the Commission.

² Appendix 1 contains further information about SA Water and its functions.

The Commission undertakes its role as economic regulator within a broader legislative and policy framework. A summary of the key entities involved in the regulation of SA Water is provided in Table 1.

Table 1: Entities involved in the regulation of the water industry

Entity	Overview of role within the water industry	Relevant legislation
Minister for Environment and Water	Administers the Water Industry Act, and is responsible for non-regulatory instruments (eg schemes) and appointing water industry entities.	Water Industry Act 2012
Treasurer	Sets licence fees for water industry entities, issues Ministerial directions and Pricing Orders.	Water Industry Act 2012
Essential Services Commission of SA	Regulates customer service standards for the sale and supply of water and sewerage retail services. Establishes average customer service and reliability service standards for water and sewerage retail services and assesses the prudent and efficient costs for delivery of water and sewerage retail services. Regulator for the third party access regime.	Essential Services Commission Act 2002 Water Industry Act 2012
Environment Protection Authority	Regulates the environmental impact of water businesses.	Environmental Protection Act 1993
Department of Environment and Water	Regulates state water resources, and other natural resource management matters.	Natural Resources Management Act 2003
SA Health	Regulates public health requirements for providing drinking water supplies.	Safe Drinking Water Act 2011
Office of the Technical Regulator	Regulates safety and technical matters.	Water Industry Act 2012
Consumer and Business Services	Responsible for administration of the Australian Consumer Law, covering consumer protection and fair trading, in South Australia. Regulates the relationship between landlords and tenants for the payment of rates and charges for water and sewerage services. Regulates the professional conduct of plumbers.	Competition and Consumer Act 2012 Residential Tenancies Act 1995 Plumbers, Gasfitters and Electricians Act 1995
Department of Human Services	Develops customer hardship and concession policies.	Water Industry Act 2012
Energy and Water Ombudsman SA	Handles complaints of customers of water retailers that have joined the scheme.	Water Industry Act 2012 Corporations Act 2001

The South Australian Government develops public policy in relation to public health, the environment, technical standards, safety and social welfare policy, all of which have an impact on SA Water.

It is the role of independent regulators, such as the Commission and the Environment Protection Authority (EPA), to make decisions on matters assigned to them by Government.

While, through its regulatory determinations, the Commission determines the efficient expenditure required by SA Water to meet its regulatory obligations, it does not decide whether government policies that impact on water and sewerage prices are appropriate or correct. Nor does the Commission make decisions about the governance of SA Water, as that is a matter for SA Water and its shareholder, the South Australian Government.

Further, the Commission's role is limited to an assessment of the efficient costs of providing essential services; it does not extend to an assessment of an individual customer's capacity to pay for essential services. The South Australian Government makes decisions about social policy, including policies designed to assist customers to meet the costs of accessing essential services.

SA Water makes the day to day commercial decisions about the operations and investments required to deliver water and sewerage services that meet its regulatory obligations. SA Water is also responsible for setting the prices that apply to customers, although those prices must meet the requirements of the Commission's determinations. (This is explained in more detail in Guidance Paper 2 – Revenue regulation and pricing principles.)

Consumer and industry advocates also have an important role to play, through understanding and representing or reflecting the views of their constituencies in consultation and engagement processes. They may also advocate for changes where their constituents' interests are not being met (for example, in relation to the price/service offerings being provided by SA Water). In the SAW RD20 context, these participants will have an enhanced function – notably through the Consumer Experts Panel - providing both early and direct challenge to SA Water in order to better capture the value that they provide to the regulatory system.

Legal requirements for SAW RD20

The Commission's determination must be consistent with the legal requirements of the Water Industry Act 2012 and Essential Services Commission Act 2002. The Water Industry Act 2012 allows the Commission to establish customer service standards and price regulation for water and sewerage retail services provided by SA Water; the Essential Service Commission Act 2002 provides the formal legal powers for making the determination.

In making SAW RD20, the Commission must have, as its primary objective, the protection of the long-term interests of consumers with respect to the price, quality and reliability of essential services.³ It must also have regard to various other legislative requirements and objectives that guide it. Those objectives generally focus on the principles of economic efficiency which, when applied to SA Water, mean that the Commission encourages it to maximise the potential of its resources and seek continuous improvement in areas of service that its customers value.

Given the long-term nature of SA Water's assets, the Commission's regulatory determination must have a long-term focus. It must recognise the need for SA Water to provide regulated services for present and future generations. Setting revenues to recover the lowest sustainable cost for a given level of service seeks to achieve the outcome where SA Water has sufficient revenue to efficiently deliver the services valued by customers, in the long-term. The Commission is not seeking to deliver low prices in the short-term at the expense of long-term service delivery. That would be inconsistent with the Commission's requirement to protect the long-term interests of SA Water's customers.⁴

In fulfilling its price regulation function (which can include setting revenues, pricing principles and other forms of regulation), the Commission must ensure that:

- ▶ wherever possible the costs of regulation do not exceed the benefits, and
- ▶ its decision takes into account and clearly articulates any trade-off between costs and service standards.⁵

³ Essential Services Commission Act 2002, section 6(a).

⁴ See section 6(1) of the Essential Services Commission Act 2002.

⁵ Essential Services Commission Act 2002, section 25(5).

The Commission's approach to SAW RD20 will meet those requirements by:

- ▶ establishing service standards that are based on consumers' preferences, reflecting the service levels that customers are willing to pay for, and
- ▶ setting drinking water and sewerage revenues to reflect the prudent and efficient cost of providing those services at the determined standards and in accordance with the obligations set by other regulators of SA Water.

A full description of the legal framework for SAW RD20 is contained in the SAW RD20 Framework and Approach paper.⁶

Current regulatory approach

SA Water provides three broad classes of regulated retail services:

- ▶ drinking water retail services
- ▶ sewerage retail services, and
- ▶ excluded retail services, which comprise the sale of recycled water, connection services, trade waste services and other miscellaneous retail services.

SA Water provides other services that are not retail services, eg water quality testing services provided to other businesses on a commercial basis. Those services are not subject to regulation by the Commission.

The Commission has previously made two regulatory determinations for regulated retail services, in 2013 and 2016.⁷

The regulatory determinations for the drinking water and sewerage retail services involved:

- ▶ setting the maximum revenues that SA Water could recover from its customers for those services
- ▶ making a consumer protection code to deal with matters such as billing requirements, flexible payment arrangements, limitations on disconnections of customers for non-payment and other contractual matters, and
- ▶ establishing a set of minimum service standards to maintain the reliability of SA Water's networks, its responsiveness to service interruptions and other customer service issues.

The regulatory determinations for excluded retail services involved:

- ▶ requiring SA Water to set prices for those services in a transparent manner and consistent with specified pricing principles, which focus on prices being reflective of efficient costs, and
- ▶ establishing minimum service standards for connection services.

The Commission will continue to regulate the three broad classes of retail services that SA Water provides, on the basis that SA Water will continue to be the monopoly water and sewerage retailer for most South Australians.

⁶ See Appendix 1 of the Commission's July 2018 Framework and Approach paper, available at <https://www.escosa.sa.gov.au/ArticleDocuments/1172/20180702-Water-SAWaterRegulatoryDetermination2020-FrameworkandApproach-Final.pdf.aspx?Embed=Y>.

⁷ Information about those determinations is available on the Commission's website at <https://www.escosa.sa.gov.au/industry/water/retail-pricing/sa-water-regulatory-determinations>.

The process that the Commission has used to make its past determinations has involved:

- ▶ SA Water preparing and submitting to the Commission a regulatory business plan setting out its proposed service levels, expenditure and revenues for the next regulatory period, informed by customers' views
- ▶ public consultation on SA Water's business plan, to inform the Commission's determination
- ▶ the Commission reviewing SA Water's business plan and submissions made in response to it and releasing for public consultation a draft Regulatory Determination, and
- ▶ the Commission considering submissions to its draft Regulatory Determination before preparing and releasing a final Regulatory Determination.

Further information about the Commission's current approach to regulating SA Water's drinking water and sewerage revenues and prices for excluded services, including its proposed approach for SAW RD20, is discussed in Guidance Paper 2 – Revenue regulation and pricing principles.

The Commission's current approach to setting SA Water's service standards, including the proposed approach for SAW RD20, is discussed in Guidance Paper 3 - Service standards.

The Commission's current approach has delivered good outcomes for customers (discussed further in the section below); however, reflecting on submissions to the Commission's draft Framework and Approach paper,⁸ the Commission recognised that its current approach did not maximise the opportunities to draw on the feedback and expertise from a wide range of parties. A key focus for SAW RD20 is to provide a more inclusive process of stakeholder engagement.

In addition, the Commission recognised that there are opportunities to involve stakeholders in the review process much earlier than in SAW RD16. Stakeholders will be provided with more opportunities to provide feedback to SA Water as it develops its regulatory business plan to apply from 1 July 2020 (**business plan**), rather than waiting to comment on a fully developed draft plan as was the case in previous determinations.

The manner in which SAW RD20 will address those opportunities for improvement is discussed later in this paper.

How has SA Water performed to date?

Since the Commission's first SA Water Regulatory Determination in 2013, SA Water has reduced its prices to customers, in real terms (removing the impacts of inflation), while maintaining overall service levels.

The annual drinking water bill for a typical residential customer has decreased, in real terms (using 2018-19 prices), from \$972 in 2013-14 to \$851 in 2016-17 (a 12 per cent reduction), with the corresponding annual residential sewerage bill reducing from \$560 in 2013-14 to \$453 in 2016-17 (a 19 per cent reduction).⁹

SA Water has generally achieved cost savings since 2013-14, relative to the expenditure amounts included in the Commission's Regulatory Determinations. Figure 1 and Figure 2 below show the trends in SA Water's drinking water and sewerage capital and operating expenditure since 2013-14 in real terms.¹⁰ SA Water is forecasting an increase in capital expenditure in 2018-19 and 2019-20, mainly driven by investments in renewable generation (to reduce its overall electricity costs) and the Northern Adelaide Irrigation Scheme.

⁸ Those submissions are available on the Commission's website at <https://www.escosa.sa.gov.au/projects-and-publications/projects/water/sa-water-regulatory-determination-2020-framework-and-approach>.

⁹ Bureau of Meteorology, National Performance Report 2016-17: Urban Water Utilities, Part B (available at <http://www.bom.gov.au/water/npr/>).

¹⁰ The Figures combine drinking water and sewerage expenditure and do not include expenditure for excluded and unregulated services.

A significant proportion of this capital expenditure increase will be funded by savings generated by the projects or revenue from sources other than SA Water’s drinking water and sewerage customers.

Forecasts of SA Water’s operating expenditure for drinking water and sewerage services in 2018-19 and 2019-20 are not available. However, information from the South Australian Government’s 2018-19 State Budget indicates that SA Water is forecasting operating expenditure savings (across all areas of its business, not just drinking water and sewerage services) of approximately \$18.5 million in that year (relative to 2017-18 estimated operating expenditure), which is expected to be maintained in 2019-20. Those expenditure savings are expected to be passed through to customers from 1 July 2020 through lower revenues under SAW RD20.

Further analysis of SA Water’s expenditure, including a comparison to expenditure incurred by major water utilities interstate, is contained in Guidance Paper 4 - Prudent and efficient expenditure.

Figure 1: Trends in SA Water’s capital expenditure (\$m, in Dec18 prices)

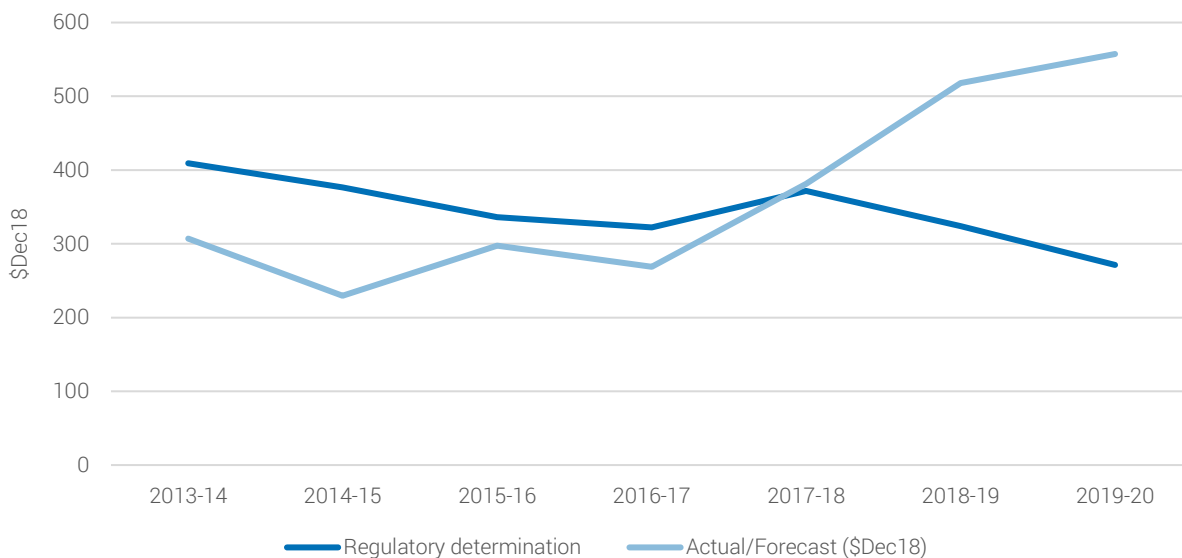
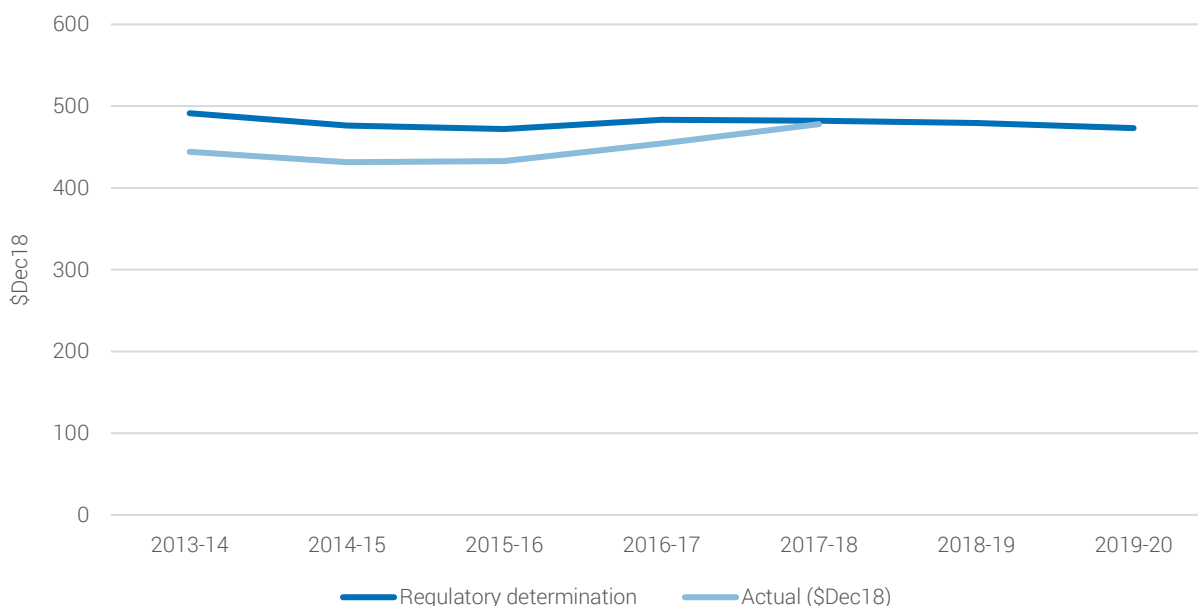


Figure 2: Trends in SA Water’s operating expenditure (\$m, in Dec18 prices)



Customers benefit from SA Water's cost savings as the lower actual expenditure outcomes in a regulatory period are used as the basis for establishing the starting revenues and prices for the subsequent regulatory period.

To ensure that cost reductions are not achieved at the expense of service levels, the Commission's regulatory framework requires SA Water to maintain service levels over time. Since 2013, SA Water has maintained its service levels to customers while also delivering consistently on the broader consumer protections provided for under the Water Retail Code – Major Retailers.

SA Water has also been working to implement an asset management system that aligns with the Institute of Asset Management (IAM) Framework.¹¹ The IAM Framework draws on ISO55000¹², which is an international standard covering the management of assets of any kind.

Those achievements suggest that SA Water has responded well to the Commission's regulatory approach. Nevertheless, the Commission's approach under SAW RD20 challenges SA Water to find ways to put further downward pressure on prices, while continuing to maintain service levels and improving its asset management practices.

What needs to be considered for SAW RD20?

The Commission has designed a governance and stakeholder engagement process that is designed to obtain the best available evidence to inform SAW RD20.

The SAW RD20 review process will raise issues for consideration earlier and introduce a greater level of direct customer testing and negotiation into the preparation of SA Water's draft business plan.

While the Commission remains responsible for making the final regulatory determination, which will require SA Water to provide the water and sewerage retail services valued by customers for the lowest sustainable cost, the review process will involve multiple opportunities for stakeholders to be involved prior to that final determination. Input from a diverse range of stakeholders is important, as it helps the Commission to make better informed and more inclusive decisions. The Commission will therefore draw on the full range of evidence provided by all stakeholders in making the final determination.

The Commission's determination will respond to the business plan submitted by SA Water in October 2019, which should be informed by and address issues raised through the various engagement stages. If the Commission identifies areas where SA Water should change its business plan, based on the Commission's analysis of evidence, it will identify those changes in its draft Regulatory Determination, to be released in February 2020. It will also identify areas where the Commission accepts SA Water's proposals.

The Commission will consider comments received on the draft Regulatory Determination and will release a final Regulatory Determination in May 2020 that either accepts SA Water's business plan or directs SA Water to modify specified parts of the plan. The final business plan (which will accord with that final determination) will represent SA Water's commitment to customers during the 2020 – 2024 regulatory period.

Once the determination is made, SA Water will be accountable for delivering water and sewerage services that meet its customers' needs, while meeting all relevant regulatory obligations. It will be responsible for delivering its business plan and transparently reporting progress and outcomes to customers on an ongoing basis.

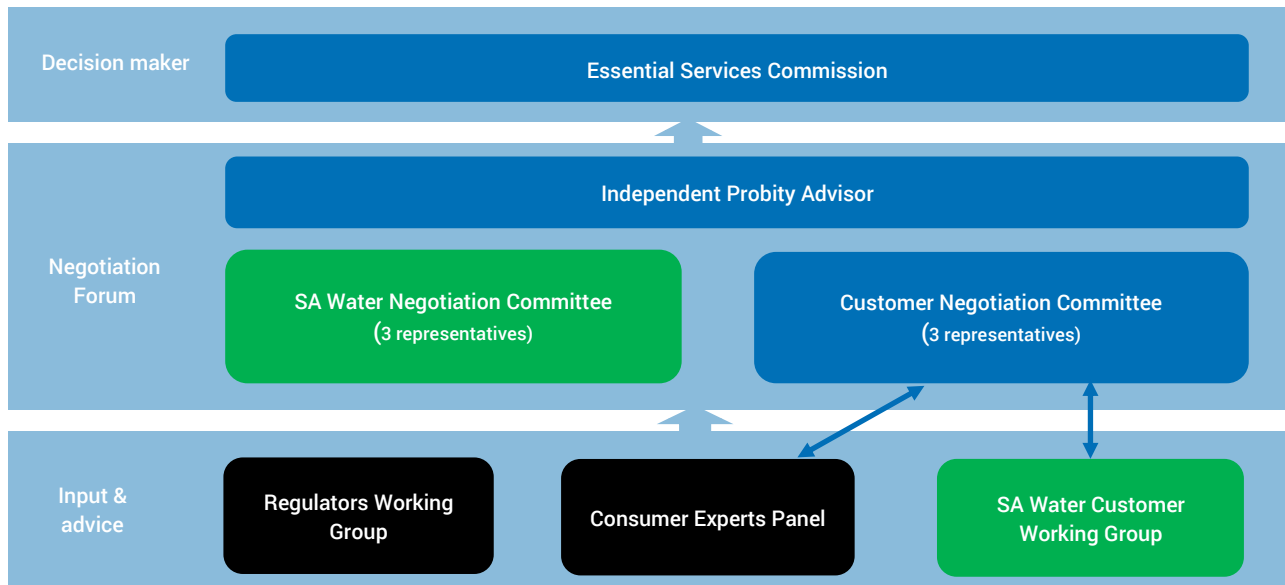
¹¹ The Institute of Asset Management is an international professional body for asset management professionals. The IAM develops asset management knowledge and best practice and generates awareness of the benefits of the asset management discipline for the individual, organisations and wider society. The IAM has over 22,000 members in 158 different countries. <https://theiam.org/>

¹² International Organisation for Standardisation, ISO55000, available <https://www.iso.org/standard/55088.html>

Process governance

The governance arrangements outlining the roles for the various groups in the Commission's decision-making process are illustrated in Figure 3 and discussed briefly below. Further detail about the arrangements is set out in the Framework and Approach paper.¹³

Figure 3: SAW RD20 governance structure



The Commission is providing and supporting additional forums for customers, and customer representatives, to debate, discuss and understand the needs, preferences and priorities of SA Water's diverse customer base.

Negotiation Forum

The Negotiation Forum will ensure that the business plan submitted to the Commission has been thoroughly tested by a wide range of stakeholders. The Negotiation Forum is comprised of the Customer Negotiation Committee, the SA Water Negotiation Team and an Independent Probity Advisor (appointed by the Commission).

The Customer Negotiation Committee has been established by the Commission to elicit and represent the perspectives, preferences and priorities of SA Water's diverse customer base in the Negotiation Forum to test SA Water as it prepares its proposed business plan for the next regulatory period.¹⁴ The Customer Negotiation Committee is expected to:

- ▶ understand and operate within the regulatory and legislative framework that applies to the decisions the Commission will make in SAW RD20 about SA Water's retail services and provide its advice consistent with these requirements
- ▶ understand SA Water's strategic direction and priorities, the broader regulatory and legislative requirements around the retail services it provides, past performance outcomes, future service delivery challenges, opportunities and investment needs

¹³ Essential Services Commission, *SA Water Regulatory Determination – Framework and Approach*, July 2018, available at <https://www.escosa.sa.gov.au/ArticleDocuments/1172/20180702-Water-SAWaterRegulatoryDetermination2020-FrameworkandApproach-Final.pdf.aspx?Embed=Y>

¹⁴ Further details on the Customer Negotiation Committee and Negotiation Forum are available at <https://www.escosa.sa.gov.au/industry/water/retail-pricing/sa-water-regulatory-determination-2020/negotiation-forum>

- ▶ understand current customer and regulatory priorities, as evidenced through the Consumer Experts Panel Priorities Report and representations made by or available from other regulators, including but not limited to the members of the Regulators Working Group
- ▶ elicit, understand and represent the perspectives, preferences and priorities of SA Water’s diverse customer base on the matters subject to the negotiations, and
- ▶ constructively test and negotiate with the SA Water Negotiation Team with a view to agreeing on the matters to be included in SA Water’s proposed business plan that will provide water and sewerage services at the lowest sustainable price for the quality and reliability levels valued by customers.

The Customer Negotiation Committee is responsible for negotiating SA Water’s proposed business plan. There will be some aspects of SA Water’s plan that are non-negotiable, such as whether or not it should undertake activities to comply with the requirements of its regulators. It may, however, test SA Water on whether or not it has proposed the lowest sustainable cost of delivering the activities to meet regulatory requirements. The matters that are subject to negotiation are summarised in Table 2 below. Further discussion about the methods for determining each of these matters is contained in the accompanying Guidance Papers.

Table 2: Matters to be considered through the Negotiation Forum

Matter to be considered	Subject to negotiation?	Comments
Form of price regulation	No	Drinking water and sewerage services will be subject to revenue caps and excluded services will be subject to pricing principles
Cost allocation method	Yes	SA Water must demonstrate that its proposed method is consistent with the National Water Initiative Pricing Principles
Service standards (including possible guaranteed service level scheme)	Yes	SA Water to propose draft service standards and performance targets for drinking water, sewerage and excluded services. This may include a possible guaranteed service level scheme that provide financial penalties for providing service levels below certain standards
Other consumer protections in the Code	Yes	Subject to any legal requirements for consumer protections
Regulated asset values	Limited	Although efficient capital expenditure to be included in asset values is subject to negotiation
Determination of efficient actual and forecast capital expenditure	Yes	The Negotiation Forum may consider the efficiency of capital expenditure incurred by SA Water during the SAW RD16 regulatory period and the forecast capital expenditure for the SAW RD20 regulatory period. Where capital expenditure is driven by a regulatory requirement, it cannot negotiate whether or not the expenditure is prudent, but may consider the efficiency of the expenditure
Determination of efficient forecast operating expenditure	Yes	Where operating expenditure is driven by a regulatory requirement, the Negotiation Forum cannot negotiate whether or not the operating expenditure is prudent, but it may consider the efficiency of the expenditure
Regulatory depreciation	Limited	Although efficient capital expenditure to be depreciated is subject to negotiation
Regulatory rate of return	Yes	The Negotiation Forum should focus on an appropriate rate of return at an aggregate level, having regard to risks faced by SA Water, relevant benchmarks and analysis of SA Water’s profitability and financial position. The Commission will use that input to determine the regulatory rate of return, estimated through the weighted average cost of capital approach

Matter to be considered	Subject to negotiation?	Comments
Tax expense	No	Tax is a small component of total revenue (<1%) and should not be the focus of negotiation
Return on working capital	No	The return on working capital is a small component of total revenue (<1%) and should not be the focus of negotiation
Forecasts of water demand and customer numbers	Yes	Forecasts of water demand and customers are inputs into the expenditure forecasts and are important for determining prices (noting that prices are outside the scope of the determination)

Guidance Paper 2 – Revenue regulation and pricing principles contains further discussion of how the negotiation process supports the Commission’s drinking water and sewerage revenue determinations.

Consumer Experts Panel

A Consumer Experts Panel has been established to provide for joint sittings of the Commission’s and SA Water’s consumer advisory groups.¹⁵ The involvement of the Consumer Experts Panel is likely to continue to evolve over the course of SAW RD20. At this stage, members of the Consumer Experts Panel:

- ▶ have contributed towards the development of a Priorities Report for SA Water’s Board and the Negotiation Forum to consider
- ▶ will provide further information to the Negotiation Forum, as it conducts its detailed discussions on SA Water’s draft regulatory business proposal from February 2019 to June 2019
- ▶ will provide ongoing feedback, advice and evidence for the Commission as it develops its final decisions by May 2020, and
- ▶ will participate in an evaluation process at the end of the SAW RD20 review.

Regulators Working Group

A Regulators Working Group has been established to provide a forum for the various regulators to coordinate their efforts for achieving positive outcomes for the South Australian community through their combined regulation of SA Water.¹⁶ Those regulators include the Commission, the Environment Protection Authority, SA Health, the Office of the Technical Regulator, the Department of Environment and Water and Consumer and Business Services.

The Regulators Working Group will work together to develop a statement of the outcomes that SA Water is expected to achieve over the four-year period 1 July 2020 to 30 June 2024. The Regulators Working Group will continue to work together throughout the 2020-2024 regulatory period to jointly monitor, evaluate and publicly report on SA Water’s performance in meeting regulatory requirements.

¹⁵ Further details on the SA Consumer Experts Panel are available at

¹⁶ Further details on the Regulators Working Group are available at <https://www.escosa.sa.gov.au/industry/water/retail-pricing/sa-water-regulatory-determination-2020/regulators-working-group>

Opportunities for stakeholder input into SAW RD20

There are multiples opportunities for stakeholders to provide input into SAW RD20.

Those opportunities include commenting on these Guidance Papers and making submissions to SA Water's proposed business plan and the Commission's draft Regulatory Determination. The timetable for those consultation processes are set out in Appendix 2 of this paper.

The Commission will ensure that its engagement processes are flexible and allow all stakeholders the opportunity to provide input into the determination process. There will be regular opportunities for stakeholders to meet with Commission staff and, where appropriate, the Commission may hold stakeholder forums.

The Guidance Papers

The Commission is seeking feedback on various issues discussed in this initial suite of Guidance Papers, which will help inform the determination. The Guidance Papers provide up-front guidance to stakeholders on the proposed principles and methodologies that the Commission intends to apply, including the matters that it intends to subject to the negotiation process and those that are non-negotiable.

The Guidance Papers are a critical part of the Commission's assessment of SA Water's regulatory business plan. Through the formal determination process, the Commission will look to ascertain the extent to which that plan falls within the framework established by these papers. Where it does not, the Commission will seek to understand whether the reasons for departure are reasonable and have been supported, or even proposed, by customers through SA Water's consultation and engagement process.

The initial Guidance Papers address the matters summarised in Table 3, and will include technical appendices as required. Any comments provided by stakeholders on the Guidance Papers will be taken into account by the Commission as it prepares for and undertakes the determination. The Commission may release further guidance papers to inform and to assist the negotiation process as required.

Table 3: Content of initial Guidance Papers for SAW RD20

Guidance paper	Purpose
1. Overview of economic regulation of SA Water	This paper confirms the process for SAW RD20. It will enable stakeholders to understand future opportunities to provide input into the determination.
2. Revenue regulation and pricing principles	This paper explains how SA Water's drinking water and sewerage revenues will be determined, using a cost-based (building blocks) approach and informed by a negotiation process. It also explains how the Commission will regulate the prices of SA Water's excluded services.
3. Service standards	This paper explains the Commission's process for reviewing its principal consumer protection industry code: the Water Retail Code–Major Retailers, which includes customer service standards.

Guidance paper	Purpose
4. Prudent and efficient expenditure	<p>This paper explains the Commission’s approach to reviewing SA Water’s proposed expenditure to assess whether it is prudent and efficient, to feed into the calculation of the maximum revenue allowance. It provides context on the ‘negotiable’ and ‘non-negotiable’ elements of SA Water’s costs, and provides an indication of some of the potential future cost drivers.</p> <p>It also provides guidance to SA Water on the minimum information that it should provide to the Negotiation Forum to allow it to assess whether proposed initiatives, programs and projects are prudent and efficient.</p>
5. The cost of funding and using assets	<p>This paper explains the Commission’s methodology for determining the efficient cost of funding and using assets to provide drinking water and sewerage services, in particular the return on, and of, regulated assets.</p>

Determining the effectiveness of SAW RD20

There are two aspects of SAW RD20’s success that the Commission will evaluate.

First, the Commission will review the process for the determination in the second half of 2020. It will seek stakeholder feedback on key process matters, such as the effectiveness of the Commission’s consultation processes and the negotiation process. The Commission will use stakeholder feedback to inform its thinking about possible process improvements that could be made for the following determination (SAW RD24).

Second, the Commission will evaluate whether or not SAW RD20 has delivered the intended outcomes for customers, on an ongoing basis during the 2020-2024 regulatory period. Reporting by SA Water of its performance in providing regulated services will be a critical input into that evaluation. The Commission will monitor SA Water’s costs of providing drinking water and sewerage services and assess its performance against the regulated service standards.

The Commission will also evaluate the extent to which SA Water has been able to meet the requirements of other regulators, within the maximum revenue caps.

This will require a longer-term program of monitoring and reporting of outcomes by SA Water and its regulators. The Commission will work closely with other regulators to ensure that our monitoring and reporting frameworks are capturing and measuring relevant aspects of SA Water’s performance, while also minimising regulatory costs.

The Commission will also make SA Water accountable for reporting its performance to customers. That program will help the Commission understand the effectiveness of its regulatory approach and guide the design of future SA Water regulatory determinations.

Appendix 1: About SA Water

The South Australian Water Corporation Act 1994 establishes the South Australian Water Corporation (**SA Water**) as a statutory corporation, wholly owned by the Government of South Australia. It is a public corporation subject to the Public Corporations Act 1993. SA Water's primary functions are to provide services for the:

- ▶ supply of water by means of reticulated systems
- ▶ storage, treatment and supply of bulk water, and
- ▶ removal and treatment of sewage by means of sewerage systems.

It also has other functions, including:

- ▶ carrying out research and works to improve water quality and sewage disposal and treatment methods
- ▶ commercial development and marketing of its products, processes and intellectual property produced or created in the course of the SA Water's operations, and
- ▶ encourage and facilitate private or public sector investment and participation, whether from within or outside the State, in the provision of water and sewerage services and facilities.

In addition, SA Water is also responsible for acting as the agent of the Minister for Environment and Water:

- ▶ in the Minister's capacity as Constructing Authority under the Murray-Darling Basin Act 2008, and
- ▶ for the purpose of purchasing water entitlements under the River Murray Act 2003, for and on behalf of and as instructed by the Minister from time to time.

As a statutory corporation, wholly owned by the Government of South Australian, SA Water must comply with various State Government requirements. As a result, SA Water:

- ▶ has a Board that is accountable to the Minister for Environment and Water and the Treasurer for the sound management and stewardship of SA Water and its assets for and on behalf of its owners
- ▶ must undertake its commercial operations in accordance with prudent commercial principles and use its best endeavours to achieve a level of profit consistent with its functions
- ▶ must undertake its non-commercial operations in an efficient and effective manner, consistent with the requirements of its charter, which are:
 - subject to a community service obligation agreement between SA Water and a purchasing Minister
 - subject to a direction under section 6 of the Public Corporations Act¹⁷
 - related to the operational responsibility of water and wastewater facilities for identified Aboriginal communities, or
 - agreed by the Minister and the Treasurer to be non-commercial
- ▶ must comply with state government policies and relevant Treasurer's Instructions on dividend and tax equivalent payments; including paying all rates, duties and taxes that would apply if SA Water were not a government-owned entity.¹⁸

¹⁷ Pursuant to section 6 of the Public Corporations Act 1993 and sections 6 and 7(2)(f) of the South Australian Water Corporation Act 1994.

¹⁸ Refer section 29 and section 30 of the Public Corporations Act 1993.

Appendix 2: Key milestones in the SAW RD20 review

There will be various stages during the SAW RD20 process where stakeholders can provide input.

The Commission welcomes any comments on this initial set of Guidance Papers and may release further Guidance Papers during the determination process.

The Commission will release the Priorities Report from the Consumer Experts Panel, outlining panel's views on the priorities that should be taken into account by SA Water as it develops its regulatory business plan.

SA Water has commenced its planning process for the next regulatory determination and, by February 2019, will be prepared to discuss and negotiate draft business plan proposals with the Customer Negotiation Committee over a four-month period from February 2019 to May 2019.

Following those negotiations, the Commission expects SA Water to submit its business plan in October 2019. The Commission will assess that business plan in the context of:

- ▶ statutory objectives and factors under the Commission's legislative framework
- ▶ reports from the Chairperson of the Customer Negotiation Committee, the Independent Probity Advisor, the Consumer Experts Panel and regulators of SA Water, and
- ▶ stakeholder submissions.

The Commission will release a Draft Regulatory Determination in February 2020 for further public consultation. It will consider submissions received during that consultation period and will issue a Final Regulatory Determination in May 2020. The key output of the determination is an approved SA Water business plan. SA Water will be accountable for delivering the outcomes of that plan.

SAW RD20 process timeline

Date	SAW RD20 Milestone
Sep 2018	Commission appoints Customer Negotiation Committee, Independent Probity Advisor and establishes Consumer Experts Panel
Sep - Oct 2018	Meetings of the Consumer Experts Panel to discuss priorities
End-Oct 2018	Release of initial Guidance Papers
Nov 2018	Consumer Experts Panel produces Priorities Report
Dec 2018	Release of further Guidance Papers (if appropriate)
Feb 2019	SA Water prepares draft regulatory business plan for negotiation with Customer Negotiating Committee
Feb - Jun 2019	Negotiation Forum
Oct 2019	SA Water submits proposed business plan for 2020-2024
Oct 2019	Independent Chair of the Customer Negotiation Committee submits report on negotiation process and outcomes

Date	SAW RD20 Milestone
Oct 2019	Independent Probity Advisor submits report on integrity of negotiation process
Oct – Dec 2019	Consultation on SA Water's proposed business plan and reports of the Independent Chair and Independent Probity Advisor
Feb 2020	Commission issues draft regulatory determination
Feb – Mar 2020	Consultation on draft regulatory determination
May 2020	Commission issues final regulatory determination
July 2020	Approved SA Water business plan takes effect