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SA Water Regulatory Determination 2024

Final Framework and Approach

September 2021

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Glossary of terms

Term	Description
Commission	Essential Services Commission, established under the <i>Essential Services Commission Act 2002</i>
ESC Act	<i>Essential Services Commission Act 2002</i>
SA Water	South Australian Water Corporation
SAWRD20	SA Water Regulatory Determination 2020
SAWRD24	SA Water Regulatory Determination 2024
WI Act	<i>Water Industry Act 2012</i>

Executive summary

Under the statutory framework governing the economic regulation of SA Water, the Commission makes four-yearly economic regulatory determinations that set the maximum revenues that SA Water may earn from, and the service standards that it must provide to, its customers. The purpose of such determinations for monopoly service providers such as SA Water is to reproduce, in the absence of a competitive market, the incentives for efficient outcomes that benefit customers over the long term.

The Commission will make a new regulatory determination to apply to SA Water for the period 1 July 2024 to 30 June 2028: SA Water Regulatory Determination 2024 (**SAWRD24**).

Capital planning and investment is a continuous and ongoing process. Given the long lives of SA Water's assets, and the lead time on investments, decisions made in one four-year regulatory period will generally have flow-on impacts for future investment plans. The Commission will continue to monitor and evaluate the outcomes of SA Water Regulatory Determination 2020, and SAWRD24 will build on the additional transparency introduced in the current regulatory period to continue strengthening the continuous and consultative approach to the regulation of SA Water's retail services.

Consistent with its primary objective of protecting the long-term interests of consumers with respect to the price, quality and reliability of essential services, and with its past approach, SAWRD24 will challenge SA Water to continue to:

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

An important step in the SAWRD24 process is establishing the Framework and Approach, setting out the timing, process and governance arrangements that will apply. The Framework and Approach looks to add value to the regulatory process for consumers by encouraging greater transparency by SA Water. SA Water must ultimately develop a Regulatory Business Proposal which, under the highest and widest levels of scrutiny, clearly demonstrates how its proposed investments will protect consumers' long-term interests.

The key next steps in the review process are as follows:

- ▶ September 2021 onwards: The Commission will release Guidance Papers to inform the development of SA Water's Regulatory Business Proposal and allow stakeholders to better engage with relevant regulatory issues. The Commission will also convene stakeholder sessions as required, to explain regulatory issues and methodologies, and to provide comment and feedback on regulatory matters as needed.
- ▶ September 2021 onwards: SA Water will formally commence the development of its Regulatory Business Proposal, including:
 - convening a customer challenge group, which will robustly review and question SA Water's proposals before they are finalised and included within the Regulatory Business Proposal
 - undertaking wider customer engagement and research, to inform the projects, plans and deliverables which may be included within the Regulatory Business Proposal, and
 - publishing clear and transparent information about its capital investment and asset planning, management, and delivery proposals and intentions, short-, medium- and long-term, to allow stakeholders and the Commission to understand and test their prudence and efficiency.

Throughout this period, the Commission will work with SA Water and other stakeholders to provide independent guidance and advice on regulatory matters.

- ▶ 3 July 2023: SA Water will submit its Regulatory Business Proposal to the Commission, with stakeholder comment and feedback sought over an eight-week period, to provide input to the draft Regulatory Determination.
- ▶ By November 2023: The Commission will publish a draft Regulatory Determination, with stakeholder comment and feedback sought over an eight-week period, and
- ▶ By May 2024: The Commission will make the Regulatory Determination, to take effect from 1 July 2024.

The Framework and Approach has been informed by stakeholder feedback, including members of the Commission's Consumer Advisory Committee, members of the previous Consumer Negotiation Committee, members of SA Water's Consumer Advisory Groups, and SA Water staff and management. Consultation began in August 2020, with an independent, external ex-post review of the process used in the current regulatory determination, conducted by Dr Pat Walsh. The Commission is grateful for the engagement and contributions from all parties and looks forward to working with them (and others) throughout the SAWRD24 process.

1 Background

The Essential Services Commission (**Commission**) is a statutory authority established as an independent economic regulator and advisory body under the *Essential Services Commission Act 2002* (**ESC Act**).

The Commission has economic regulatory responsibility in the water, sewerage, electricity, gas, rail and maritime services, and a general advisory function on regulatory and economic matters. The ESC Act and various industry Acts together provide the Commission with those regulatory and advisory powers and functions.

Under the ESC Act the Commission has the primary objective of:

'... protection of the long term interests of South Australian consumers with respect to the price, quality and reliability of essential services'

Since 2012, the Commission has been responsible for the independent economic regulation of the water industry, including SA Water and all other South Australian licensed water and sewerage retailers, in accordance with the *Water Industry Act 2012* (**WI Act**) and the ESC Act. A principal element of the Commission's economic regulation of the water and sewerage services provided by the South Australian Water Corporation (**SA Water**), is the making of four-yearly economic regulatory determinations that set the maximum revenues that SA Water may earn and the minimum service standards that it must provide to its customers.

In June 2020, the Commission made the current regulatory determination, which applies for the period from 1 July 2020 until 30 June 2024: SA Water Regulatory Determination 2020 (**SAWRD20**). It will make a new regulatory determination to apply from 1 July 2024 to 30 June 2028: SA Water Regulatory Determination 2024 (**SAWRD24**).

The Commission is committed to continuously improving its approach to the economic regulation of the water and sewerage services provided by SA Water, in line with its statutory objective. In doing so, it recognises the need for regulatory certainty in a long-term industry such as the water sector but also that, as technology, business practices and regulatory practices change for the benefit of consumers, so too should the Commission's economic regulatory regime so that it promotes those consumer benefits.

1.1 Regulatory determinations

Economic regulation of SA Water is fundamentally concerned with protecting the long-term interests of South Australian consumers. Ultimately, the purpose of such determinations for monopoly service providers such as SA Water is to reproduce, in the absence of a competitive market, the incentives for efficient outcomes that benefit customers over the long term.

As such, and consistent with its past approach and its primary objective, the Commission's regulatory determinations challenge SA Water, on an ongoing basis, to:

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

To give context to those desired outcomes, it is important to emphasise that SA Water is a long-term, asset-intensive business and, if the regulatory framework is working effectively, SA Water should be able to provide evidence that it:

- ▶ considers long-term investment needs and planning across regulatory periods, and proposes and delivers solutions with the lowest lifecycle costs to deliver the necessary service outcomes
- ▶ continually assesses its investment needs across its entire portfolio, actively reprioritising its actual investment choices based on the best evidence about the condition and performance of its assets and the risks to service delivery, and
- ▶ provides transparent and timely information to customers and other stakeholders about its current performance, emerging service delivery issues and possible future investment requirements.

The regulatory determination process provides an opportunity for both the Commission and stakeholders to form a view on the prudence and efficiency of SA Water's proposed capital and operating expenditure plans for the upcoming four-year period, and the asset management system used to develop those plans.

Critically, that assessment occurs in the context of SA Water's long-term asset management, financing and service delivery plans: not just in the context of the up-coming four-year regulatory period.

Robust external scrutiny of SA Water's internal business planning, governance and capital delivery systems, processes and controls gives SA Water the opportunity to provide evidence that:

- ▶ the short-term investment package being proposed in a regulatory determination has clear links back to the assumptions being made about long-term investment needs
- ▶ ongoing discussions are occurring across the business to reprioritise investments within a regulatory period, to do everything possible to stay within the maximum revenue caps
- ▶ stakeholders are being involved in discussions about needs identification, investment prioritisation and service delivery approaches, and
- ▶ the benefits delivered from investments are being monitored and evaluated as part of a continuous learning and improvement approach.

During the regulatory determination process, the Commission reviews a sample of projects, programs and initiatives across the business, with a focus on the matters outlined above. It also assesses the scope for efficiencies to be achieved across the business, based on issues identified with the reviewed sample that are likely to apply to the projects, programs and initiatives not reviewed in detail. Having done so, the Commission establishes forward-looking expenditure benchmarks at a level that should allow SA Water, acting as a prudent and efficient business, to meet known and identified obligations and agreed service outcomes.

The expenditure benchmarks are a key input into the calculation of the two separate maximum revenue caps; one for water retail services and one for sewerage retail services. SA Water must then manage its business, using risk-based prioritisation decision-making systems, within those maximum revenue caps over the four-year determination period.

Overall, the regulatory determination process seeks to provide robust external scrutiny of SA Water's investment decision making processes but, crucially, it does not seek to replace SA Water's operational responsibilities. SA Water must own its decisions and explain its choices to the public and its owner.

1.2 Expectations for SAWRD24

Across regulatory determination periods to date, SA Water has evidenced ongoing progress in delivering better outcomes for its customers.

However, there is still more work to be done, such that SA Water can more clearly demonstrate to stakeholders how its immediate investment program aligns with its longer-term investment plans. SA Water also needs to take further steps to demonstrate on an ongoing basis (not merely over the next four-year period), that:

- ▶ stakeholders are consistently and appropriately being involved in discussions about investment needs and planning, investment prioritisation and service delivery approaches—in both a long-term sense and in the context of each four-year regulatory determination period
- ▶ it understands its long-term investment needs and planning across regulatory periods, with activities and projects having the lowest sustainable lifecycle costs, and the four-year investment proposals within its Regulatory Business Proposal having clear links to the assumptions made about those long-term investment needs
- ▶ it continually considers its investment needs over its entire portfolio across time, and reprioritises its actual investment choices based on the best evidence about its asset condition and performance—and, in the context of a four-year regulatory period, does everything possible to stay within the maximum revenue caps, and
- ▶ it monitors, evaluates and is open and transparent with its customers and other stakeholders about its current performance, emerging service delivery issues, and possible future investment requirements.

In doing so, SA Water should focus on three areas which are common in each of those expectations.

1.2.1 Providing transparent and timely information for customers and other stakeholders

The Commission expects to see evidence that SA Water is providing transparent and timely information to its customers and other stakeholders about its current performance, emerging service delivery issues and possible future investment requirements.

SA Water should be able to demonstrate that it is considering the long term and is transparent about upcoming pressures and challenges as early as possible. It is understood that there will be more uncertainty about the specific investments that will be required further into the future and SA Water's long-term plans must be based on assumptions about the future. Nevertheless, the Commission expects SA Water to be open and transparent about its assumptions, and open to challenge and debate from a wide range of stakeholders.

Additional transparency is already being introduced to SA Water's performance during the current regulatory period, so that stakeholders are able to be informed of issues as early as possible.¹ More frequent and regular assessments of performance provide SA Water with valuable opportunities to build and maintain trust with customers, the community and other stakeholders as to how well it is delivering and about the ongoing improvements that it is making.

¹ Refer SA Water Monitoring, Evaluation and Reporting Framework, details available at <https://www.escosa.sa.gov.au/ArticleDocuments/21627/20210122-Water-SAWRD20-24-MonitoringEvaluationFramework-FinalReport.pdf.aspx?Embed=Y>

SAWRD24 will focus on bringing customers, the community and wider stakeholders into SA Water's investment planning and prioritisation processes much earlier, and on an ongoing basis. SA Water will be expected to transparently explain the drivers and assumptions behind the needs for future investments. It should seek to clearly explain how investment choices made in the immediate term will impact on medium- and long-term investment plans. This engagement with stakeholders will allow SA Water to test its assumptions, gain wider perspectives, and then refine its plans, before major investments start. It will also require SA Water to explain how it is continually searching for, and acting on, opportunities to perform its business-as-usual activities in more efficient and effective ways.

1.2.2 Long-term investment planning across regulatory periods

Capital planning and investment is a continuous and ongoing process and SA Water must make decisions on the levels of service, risks and life cycle costs for a diverse portfolio of water and sewerage assets—both within asset systems and across the entire investment portfolio.

Necessarily, SA Water's decisions span multiple regulatory periods. Decisions made in one four-year regulatory period will have flow-on impacts to future investment plans. A life-cycle valuation approach seeks to determine the lowest sustainable cost for managing assets to deliver services over the entire expected life of the assets.

While a regulatory determination focuses on the more immediate horizon, it is not intended to constrain SA Water's expenditure requirements. Inefficient investment occurs where long-term asset management plans do not consider the lowest lifecycle costs for acquiring, managing, replacing or retiring assets. The Commission does not want to see inefficient investment decisions—such as deferring investments and/or inefficient maintenance approaches—as those will ultimately cost SA Water's customers more in the long term.

SA Water's previous Regulatory Business Proposals focused on upfront capital investments, rather than explaining the expected ongoing costs and benefits to stakeholders. More work needs to be done by SA Water to help explain the expected total costs and expected service levels to be delivered through the proposed investments, across the entire lifecycle of the assets. It should also be able to demonstrate its understanding of how it will deliver the upcoming package of proposed investments, and how the immediate investments impact on long-term investment plans.

1.2.3 Ongoing reprioritisation across the business

As regulatory determinations are ex-ante point-in-time assessments, SA Water's actual expenditure during each four-year regulatory period may—and in practice does—vary from the forecasts used in the determination, due to factors such as changing priorities and external factors. SA Water may also need to respond to unexpected events that it cannot directly control, such as extreme weather conditions, an unforeseeable decline in the performance of a group of assets or changes in key input costs.

While some variation is expected over time, it is important to understand the factors driving any material variations. For example, SA Water may be entering a period in the life cycle of its assets where particular classes or systems need replacement, based on age, condition or performance. However, as many of SA Water's assets have long useful lives, the long-term expenditure profile of any such assets should be known or readily identifiable, reducing the likelihood of unexpected or unforeseen expenditure requirements arising in the short term.

Where genuinely new and material issues arise in the short-term after a regulatory determination has assessed the immediate investment program, the Commission expects SA Water to be open with customers and other stakeholders about why it cannot accommodate these new requirements within the overall revenue envelope through reprioritising. SA Water should also seek to explain the impact on medium- and longer-term investment forecasts if these additional new investments are not made immediately, acknowledging that they will come at an additional cost to customers.

There should be less need to make ex-post adjustments to the capital investments included in the Regulatory Asset Base at the start of the next regulatory period if SA Water can demonstrate to stakeholders, on an ongoing basis, that it is doing all it possibly can to undertake risk-based reprioritisations throughout a regulatory period and managing its operations within the maximum revenue caps.

2 Framework and Approach

The first step in a regulatory determination process is to establish a Framework and Approach that will guide the timing, process and governance arrangements. The Framework and Approach is a high-level document, with detail of specific regulatory or related issues being set out in subsequent Guidance Papers.

This Framework and Approach is premised on principles that have been developed in consultation with stakeholders over the past twelve months, which aim to improve the overall outcomes from the regulatory process over the long term.

2.1 Intended outcomes under the Framework and Approach

The intended outcomes under the Framework and Approach are that:

- ▶ Customers' long-term interests and the informed consumer voice are at the centre of the regulatory process.
- ▶ There is a continued focus on stakeholder and consumer engagement throughout the process, utilising existing skills and capabilities (such as the members of the Commission's Consumer Advisory Committee) and providing the necessary supports (resources, access to expert advice and the like) to enable their success. There will also be new opportunities for involvement throughout the process, as new stakeholders are identified and as new and different regulatory issues arise.
- ▶ The customer engagement model further evolves within the regulatory process, with SA Water to convene a customer challenge group, to raise issues, questions and challenges to inform SA Water's Regulatory Business Proposal as it is developed. The Commission will have a close involvement in that group, to identify and discuss potential regulatory issues as they arise.
- ▶ Building on the current monitoring and reporting framework, SA Water provides continuous and early visibility of its long-term asset management, planning and delivery in order to provide stakeholders with better information on its long-term capital investment plans.
- ▶ SA Water can demonstrate through its Regulatory Business Proposal that it considers its long-term investment needs and planning:
 - across regulatory periods, and proposes solutions with the lowest lifecycle costs to deliver the necessary service outcomes, and
 - across its entire portfolio, and actively reprioritises its actual investment choices based on the best evidence about the condition and performance of its assets and the risks to service delivery.
- ▶ SA Water clearly and transparently explains how its proposed investments over the four-year regulatory period are prudent and efficient, as well as how they impact on the assumptions about medium- and long-term investment plans. This will require engagement with customers and other stakeholders (including the customer challenge group) as it refines its plans over time and incorporates those within its Regulatory Business Proposal.

2.2 Principles underpinning the Framework and Approach

Building on experience, stakeholder inputs and the Commission's review and assessment, four principles have guided the development of this Framework and Approach. Those are that the regulatory framework should be:

- ▶ enduring
- ▶ an evolution rather than a revolution
- ▶ not a shadow system, and
- ▶ support ethical business practice through ethical business regulation.

2.2.1 Enduring

Capital planning and investment is a continuous and ongoing process. Over time, existing assets may be upgraded or replaced, and growth of the network requires new assets to be constructed or acquired. SA Water has an existing asset management system to guide both its longer-term and day-to-day investment decisions. Achieving long-term outcomes requires long-term thinking. It also requires regular monitoring of progress towards achieving those long-term goals so that achievements can be built upon and emerging issues can be identified early.

In that context, the economic regulatory system needs to be efficient, with the capacity to provide ongoing oversight of the long-term investment needs for SA Water, while also providing an appropriate level of scrutiny of more immediate investment needs through its four-yearly reviews.

For example, it is inefficient to have a bespoke, three-year review process to scrutinise a four-year expenditure program. There was strong stakeholder feedback on SAWRD20 that the regulatory system needs to move to operate on a more continuous basis, with the four-yearly regulatory determinations being 'check points' rather than stand-alone events. Stakeholders have firmly put their view that the Commission's regulatory oversight needs to be ongoing in the same way as SA Water's planning processes are ongoing, with customer engagement a central feature of both processes.

2.2.2 Evolution rather than revolution

The Commission is committed to continuously improving its approach to the economic regulation of the water and sewerage services provided by SA Water. In doing so, it recognises the need for regulatory certainty in a long-term industry such as the water sector but also that, as technology, business practices and regulatory practices change for the benefit of consumers, so too should the Commission's economic regulatory regime so that it promotes those consumer benefits, and delivers efficient and effective regulation.

The Commission therefore wants to keep what has worked well in previous review processes and adapt or improve those parts of the process that ultimately did not assist.

Discussions with stakeholders have confirmed that many of the mechanisms used in the previous regulatory reviews have been effective:

- ▶ additional transparency around SA Water's investment proposal was introduced through more direct customer challenge
- ▶ consumer advocates were able to discuss, debate and publicly document the issues that were important to them earlier in the process
- ▶ the Guidance Papers allowed stakeholders to understand the Commission's expectations in advance of it receiving SA Water's Regulatory Business Proposal

- ▶ formalisation of the interactions between SA Water’s various regulators through the Regulators’ Working Group achieved greater co-ordination and understanding of the inter-connectedness of decisions being made about future obligations, and
- ▶ implementation of the monitoring and evaluating performance framework for the SAWRD20 period will provide additional transparency around actual outturn performance on an ongoing basis and assist with building the picture for future investment needs as they arise.

While the above mechanisms will be retained for the SAWRD24 review process, the opportunities identified by stakeholders to refine the regulatory determination process further will also be addressed.

The review process has started earlier, so that customers and the community can be involved as SA Water develops its Regulatory Business Proposal, rather than being asked to comment after many key decisions have already been made. Customers and the community will be supported with the appropriate resources from both SA Water and the Commission to properly understand and engage with issues.

2.2.3 Not a shadow system

A key part of the Commission’s regulatory determinations is to review the regulated businesses’ internal governance, systems and processes as they already exist. Where gaps are identified, additional information will be requested and must be prepared by the business.

In practice, this means that regulatory review processes are resource intensive. Regulated entities prepare extensive materials that are highly technical and tailored to the requirements set by their regulators. Often, these materials are in addition to other internal planning processes and documentation. Their audience is limited, and much is considered commercial-in-confidence and thus not able to be shared, discussed and debated with external stakeholders. Stakeholders have expressed frustration that they are often asked to comment on matters without having access to the relevant evidence to inform their decisions.

The Commission wants to continue to focus on understanding SA Water’s existing systems, processes and practices. It wants to enhance the transparency for as wide a group of stakeholders as possible around the investment gateways that already exist in SA Water’s current internal planning and delivery processes. To minimise the overall transaction costs in the wider regulatory system, efforts will be focused on identifying and addressing issues in existing processes, rather than creating ‘shadow’ or additional processes that only exist to formally comply with regulatory requirements.

Stakeholders have expressed a clear desire for there to be opportunities for greater consumer engagement and challenge earlier in the review process, before key decisions have been made. The Commission’s view is that informed consumer input into the drinking water and sewerage retail services provided by SA Water, in the right ways and at the right times, will assist to deliver those services at the lowest sustainable prices for the desired service levels.

Wherever possible, existing stakeholder forums and collective decision-making processes should be built on and adapted to incorporate the external scrutiny expected by stakeholders. Throughout the regulatory review process, stakeholders will be invited to discuss their issues and concerns with SA Water, the Commission, and other regulators (as appropriate) at the same time, rather than having to ask questions or put their submissions multiple times to multiple parties. This will assist with combatting ‘consultation fatigue’ for stakeholders. It will also help to build and maintain trust in the efficiency and effectiveness of the wider regulatory system to identify and resolve issues.

2.2.4 Supports ethical business practice through ethical business regulation

In a system of ethical business practice and ethical business regulation, the relationship between a business and a regulator is characterised by open and transparent interactions in which the business produces evidence of its ongoing commitment to ethical business practice and the regulator recognises and encourages that commitment.²

SA Water has the ongoing relationship with its customers; it needs to understand their needs, expectations and preferences. It must navigate the operational challenges in delivering its services and continually check in with customers to see if they are satisfied with the services they are receiving. SA Water needs to design and adapt its systems, operating procedures, policies and plans to respond to its changing environment. The more open and transparent it is about how it makes such decisions, the more trust it will build and maintain with its customers and the wider community.

To support SA Water to operate in this way, the Commission's involvement in the relationship between the business and its customers needs to be a step removed. The Commission will continue to focus on identifying systemic issues and longer-term trends, deciding when and how to intervene to address those issues. This will apply not only to the regulatory review process but continue throughout the administration of a regulatory determination. The Commission will hold SA Water to account for its actions; it is SA Water that must choose how it responds.

To be an ethical business regulator in respect of its own decision-making processes, the Commission reaffirms its commitment to be clear about its expectations for SA Water, the level of influence stakeholders can have on the final decisions that have to be made, and the evidence ultimately used to inform the final decisions.

2.3 Role of customers and challenge

In exercising its powers to make a regulatory determination, the Commission is informed by and consults widely with its stakeholders, to help shape options and consider alternatives: obtaining and considering a diversity of views is fundamental to a robust decision-making process.

In any form of participatory decision-making process, however, it is important to be clear with stakeholders as to the level of influence they can and will have over the decisions to be made.³ For example, in each regulatory determination, the Commission remains the ultimate decision maker; any consideration of the role of customers, customer advocates and other stakeholders in the SAWRD24 process must clearly take that fact into account.

Similarly, customers and stakeholders also provide a necessary source of external challenge to SA Water's internal decision-making processes—albeit that SA Water is responsible for its Regulatory Business Proposal and delivery of service outcomes.

In the absence of competitive pressures, the Commission's regulatory approach assesses the extent to which the views and priorities of customers and stakeholders inform SA Water's plans, proposals and priorities. It also encourages SA Water to embed these perspectives as a central element of its ongoing service planning and delivery. Consultation and engagement with customers and other stakeholders allows SA Water to test its assumptions, gain wider perspectives and refine its plans, before committing to or commencing major investments. It also requires SA Water to have the capacity to

² Hodges, C and Steinholtz, R, *Ethical business practice and regulation: A behavioural and values-based approach to compliance and enforcement*, Hart Publishing, 2017.

³ The Commission's Charter of Consultation and Regulatory Practice provides guidance for stakeholders on the Commission's processes, available <https://www.escosa.sa.gov.au/consultation/charter-of-consultation-and-regulatory-practice>

clearly explain how it is continually searching for, and acting on, opportunities to deliver services in more efficient and effective ways.

2.3.1 Customer challenge

A key theme arising through consultation during the development of this Framework and Approach, including through the independent ex-post review conducted by Dr Pat Walsh, was the need for the Commission to further consider the role of customers in the regulatory determination process. This was particularly in relation to whether the arrangements in SAWRD20, when a group of three customers was asked to 'negotiate' with SA Water, should be modified such that the role of customer groups (or a dedicated customer group) would be to 'challenge' SA Water throughout the process.

Having regard to stakeholder feedback from SAWRD20 on the purpose, roles, expected outcomes and governance around a 'customer challenge' process, the Commission has formed the view that the most appropriate role for customers, customer advocates and other stakeholders in the SAWRD24 process is to 'challenge' SA Water, rather than to 'negotiate' with it.

'Challenge' may take many forms throughout the review process, ranging from building an understanding of issues through to joint problem solving. The actual methods chosen throughout the review will be determined based on the purpose of the engagement, which will be made clear to stakeholders at the time.⁴

The Commission's position on this matter recognises the power imbalances between the parties and impracticalities of the concept of a 'binding' negotiation in circumstances where the Commission is a statutory decision maker which must have regard to all views and evidence put to it—not just the evidence arising from a negotiation process.

As such, the Customer Negotiation Committee from SAWRD20 will be replaced by a customer challenge group, convened, resourced and managed by SA Water. As a minimum, the customer challenge group is expected to:

- ▶ comprise community members who can engage with SA Water at a strategic, whole of business level, about investment requirements and prioritisation
- ▶ discuss, debate and challenge the assumptions underpinning the needs for investments and the options to be considered to deliver the benefits expected to be achieved, and
- ▶ help SA Water to design, conduct and review the findings from various forms of customer research, with a particular focus on any research that will be used to inform future investment decisions.

The customer challenge group will meet regularly with SA Water as it develops and refines its Regulatory Business Proposal, with Commission staff in attendance to provide support and guidance on regulatory matters. The SAWRD24 process will also allow SA Water to test and experiment with how a customer challenge group of this nature could transition to provide an ongoing advisory role beyond the SAWRD24 regulatory review cycle and become part of its investment planning and prioritisation process.

⁴ The Commission's approach will be consistent with the guidance provided by the International Association for Public Participation, which is the peak body for the community and stakeholder engagement industry. Its quality assurance standard provides a standard process for any engagement process to ensure it meets best practice principles leading to confidence in the outcome for all involved, refer <https://iap2.org.au/resources/quality-assurance-standard/>

2.3.2 Existing stakeholder groups

Other stakeholders will also have ongoing opportunities to be involved throughout the review process. As a minimum, this will include hosting six-monthly stakeholder workshops with SA Water, the customer challenge group, the Consumer Advisory Committee and Regulators' Working Group.⁵ These workshops will allow stakeholders to hear from SA Water about its performance to date and any emerging issues that will need to be addressed in the future. Regular briefings of this kind will allow possible future investment needs to be discussed as they arise.

The Commission will also provide members of the Consumer Advisory Committee with opportunities to request independent expert advice throughout the process, to facilitate their understanding of, and engagement in, relevant regulatory issues. Where consultant (or similar) services are required, the Commission will manage the process. Options for funding advice under the WI Act Consumer Advocacy and Research Fund⁶ will also be explored. To the fullest extent possible, any independent expert advice will be made publicly available.

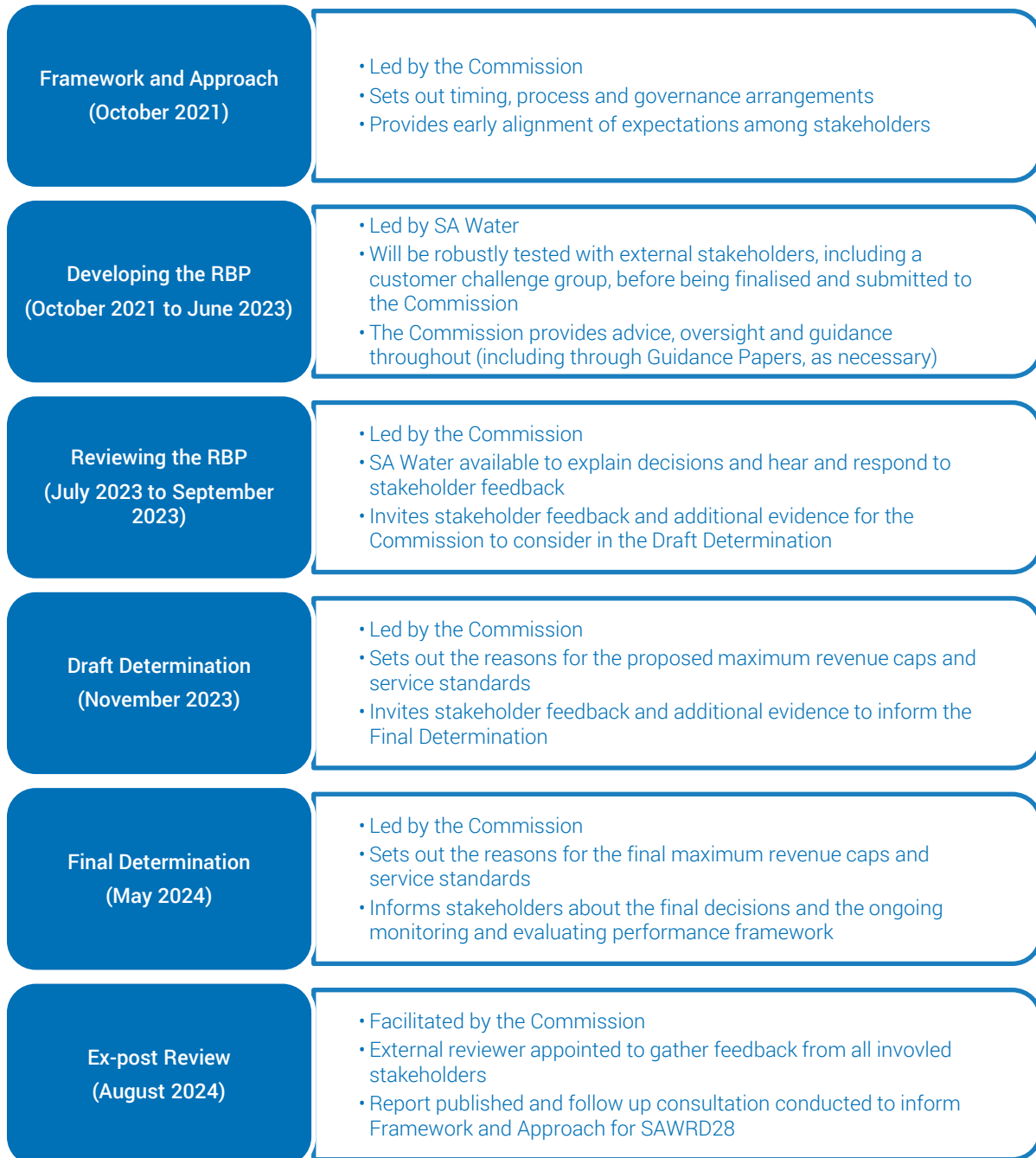
⁵ Further detail on the Regulators' Working Group may be found in Appendix 2.

⁶ The Consumer Advocacy and Research Fund (CARF), established under section 87 of the *Water Industry Act 2012*, provides annual funding of \$250,000 (indexed for inflation each year) to support: research or advocacy that promotes the interests of consumers with a disability, low-income consumers, or consumers who are located within a regional area of the State; projects that advance the interests of consumers from an advocacy perspective; and fund administration. It is administered by the Department for Environment and Water.

3 Timing and Process

There are six key stages in the overall process for SAWRD24, as illustrated in Figure 3.1. Each of those will include significant opportunities for customer and stakeholder consultation and engagement.

Figure 3.1: Regulatory Determination process



3.1 Developing the Regulatory Business Proposal

SA Water is responsible for the process that it uses to develop its Regulatory Business Proposal, for the package of investments it chooses to include in its submission and, critically, for the revenue and service level outcomes it proposes.

However, as explained in the previous Chapter, throughout the process of developing this Framework and Approach, a clear message from stakeholders is that SA Water should establish, resource and utilise a formal customer challenge group—with a long-term and whole-of-business strategic focus—to provide an external perspective which assists and challenges SA Water as it develops the Regulatory Business Proposal (with a view to maintaining that role into the future).

Importantly, that focussed and dedicated customer challenge group should supplement, not replace, the other methods that SA Water is currently using or plans to use when engaging with its customers in developing the Regulatory Business Proposal.

Further, engagement with the customer challenge group should not be limited to testing and understanding things considered simply 'discretionary' or 'customer-led'; instead, it should cover all aspects of proposed investments and actions to test assumptions about need and timing, and extend to challenging and testing issues such as SA Water's proposed research methodologies.

The customer challenge group should also provide to SA Water the opportunity to articulate to customers and the wider community how the next four years of investment impact assumptions as to future investment needs, and align with the investments of previous regulatory determinations.

The Commission does not expect or require that the customer challenge group should negotiate or agree with SA Water on the contents of the Regulatory Business Proposal. But SA Water should be able to clearly explain in that proposal how the customer challenge group has informed and change its thinking and proposals. It should also clearly highlight any areas where the customer challenge group has expressed material concerns or differences of opinion to SA Water's final position, and why SA Water did not agree.

The Commission will be involved in the process, including attending all meetings between SA Water and the customer challenge group. It will provide advice and guidance on regulatory matters, help to identify issues that need to be explored further (including through additional research and analysis or Guidance Papers), or escalated for resolution to a Governance Committee comprising senior representatives from the Commission, SA Water and Department of Treasury and Finance. However, the Commission will not be providing its view on the merits of the proposals discussed; the proper time for that is once it has all of the evidence before it from all stakeholders through consultation on the Regulatory Business Proposal and the draft Regulatory Determination.

SA Water will have the primary responsibility for designing and adapting its internal business processes to embed customer challenge and debate into its ongoing investment planning and delivery processes. The Commission will be involved along the way to identify and address issues as they arise, including giving early direction where needed.

Guidance papers on matters of regulatory policy and practice will be developed and issued, as necessary, throughout the process. Wherever possible, this will include inviting the views of wider stakeholders on draft positions.

The Commission will also convene meetings with the Consumer Advisory Committee, and other stakeholders, as required. This will allow for a wider range of stakeholders to contribute throughout the process.

3.2 Making the Regulatory Determination

Once SA Water has submitted the Regulatory Business Proposal in July 2023, the focus shifts to the Commission. It will assess the Regulatory Business Proposal, in the context of the underpinning statutory framework having regard to the context within which it has been prepared and finalised. It will also, consistent with its *Charter of Consultation and Regulatory Practice*, seek the views of all stakeholders—those who may not have been intimately involved in the detailed discussions to date, as well as those who have.

It is the Commission's current intention to allow for an eight-week consultation period on the Regulatory Business Proposal. This is longer than the six weeks normally provided for under its Charter; however, even with the greater levels of engagement and scrutiny which should sit behind the Regulatory Business Proposal this time, the Commission is cognisant that the issues raised in these processes can be complex and that stakeholders need sufficient time to prepare responses.

Once it has received submissions and comments on the Regulatory Business Proposal, the Commission will prepare a draft Regulatory Determination for release by no later than November 2023. This will include a detailed Statement of Reasons (explaining the proposed outcomes as required under the ESC Act) as well as a draft revenue determination for both drinking water and sewerage services and associated draft regulatory instruments (or draft revisions to existing instruments) necessary to give effect to changes to matters such as service standards.

Again, the Commission will allow for an eight-week consultation period within which stakeholders may make submissions. Once submissions are received, the Commission will then finalise the regulatory determination—including all necessary regulatory instruments—by no later than May 2024.

As is generally the case, and consistent with the overall process for engagement expected under this Framework and Approach, the Commission will not limit this part of the determination process to being conducted 'on the papers'. It will be available to all stakeholders for meetings and discussions throughout the process to share the more detailed thinking, planning and testing, and can host workshops (as needed/requested) throughout the process.

Further, throughout the entire process (not just the elements outlined above), the Commission will hold six-monthly workshops for at least SA Water, the customer challenge group, the Consumer Advisory Committee and Regulators' Working Group. Where necessary and appropriate, invitations will also be extended to wider stakeholders to discuss particular issues in more depth throughout the process. This may include inviting multiple external experts to speak with the group about the issues, discuss options, and undertake additional work. The Commission will co-ordinate that process.

3.3 Detailed timetable

While it is possible to clarify the high-level decision-making process, it is important to acknowledge that the process will evolve over the next couple of years as the process unfolds.

The Commission will be involved throughout the process to identify and address issues as they arise, and the six-monthly progress workshops will allow an avenue for other stakeholders to receive regular updates.

Step	Timing (indicative)
Stakeholder workshops - ongoing	
Six-monthly workshops, commencing December 2021	December and July
Appointing the customer challenge group:	
Customer challenge group terms of appointment finalised, in consultation between SA Water and the Commission	September 2021
Customer challenge group member recruitment	October 2021
Customer challenge group members appointed and induction commences	October 2021
Developing the Regulatory Business Proposal:	
Development of the Regulatory Business Proposal with stakeholders commences	October 2021
The Commission issues Guidance Papers, as required	Entire period
Discussions between customer challenge group, SA Water and the Commission	January 2022 to June 2023
SA Water submits Regulatory Business Proposal	3 July 2023
Commission review of the Regulatory Business Proposal:	
Commission invites feedback on SA Water's Regulatory Business Proposal	July 2023 to September 2023
Draft Determination released	By November 2023
Final Determination released	By May 2024
Implementation of SAWRD24:	
SA Water and SA Government develop prices	May to June 2024
SAWRD24 regulatory period commences	1 July 2024
Ongoing monitoring, reporting and evaluation continues:	
Commencement of Framework and Approach for SAWRD28	August 2024
Ex-post review of SAWRD24 process undertaken with stakeholders	By October 2024

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

Entities involved in the regulation of the water industry

Entity	Overview of role within the water industry	Relevant legislation
Consumer and Business Services	<p>Responsible for administration of the Australian Consumer Law, covering consumer protection and fair trading, in South Australia.</p> <p>Regulates the relationship between landlords and tenants for the payment of rates and charges for water and sewerage services.</p> <p>Regulates the professional conduct of plumbers.</p>	<p><i>Competition and Consumer Act 2012</i></p> <p><i>Residential Tenancies Act 1995</i></p> <p><i>Plumbers, Gasfitters and Electricians Act 1995</i></p>
Department for Environment and Water	<p>Regulates state water resources and other natural resource management matters, including through the establishment of regional landscape boards.</p> <p>Leads the development and review of water policy, including the State Water Demand and Supply Statement, Climate Change Action Plan, Water Industry Act reform, and administration of the Consumer Advocacy and Research Fund.</p>	<p><i>Landscape South Australia Act 2019</i></p> <p><i>Water Industry Act 2012</i></p>
Department of Human Services	<p>Leads the development of social policy and assisting customers experiencing hardship, including setting the Minister's Hardship Policy and administering the concessions scheme.</p>	<p><i>Water Industry Act 2012</i></p>
Department of Treasury and Finance	<p>Administers the Essential Services Commission Act.</p> <p>Manages SA Water as a Government-business enterprise, including establishing SA Water's Charter and performance plan and setting and monitoring the overall annual budget.</p>	<p><i>Essential Services Commission Act 2002</i></p> <p><i>Water Industry Act 2012</i></p> <p><i>Public Corporations Act 1993</i></p>
Energy and Water Ombudsman SA	<p>Investigates and handles complaints from customers of water retailers that have joined the scheme.</p> <p>Assists with the identification of systemic issues arising in the market that may require a business or regulatory response.</p>	<p><i>Water Industry Act 2012</i></p>
Environment Protection Authority	<p>Regulates activities of environmental significance to control and minimise pollution and waste.</p> <p>Leads the development and implementation of best practice environmental management and, where necessary, institute or supervise environmental monitoring and evaluation programmes, including environment improvement programmes and environment performance agreements.</p>	<p><i>Environment Protection Act 1993</i></p>

Entity	Overview of role within the water industry	Relevant legislation
Essential Services Commission	<p>Regulates the retail services provided by water industry entities, including SA Water, to protect the long-term interests of consumers with respect to the price, quality and reliability of those services.</p> <p>Leads the development of consumer protection codes and the form of price regulation to apply to water retail services, and monitoring performance against these standards.</p> <p>Regulator for the third-party access regime.</p>	<p><i>Essential Services Commission Act 2002</i></p> <p><i>Water Industry Act 2012</i></p>
Minister for Environment and Water	<p>Administers the Water Industry Act</p> <p>Jointly with the Treasurer, establishes the Charter for SA Water under the Public Corporations Act 1993</p> <p>Jointly with the Treasurer, issues Ministerial Directions under section 6 of the <i>Public Corporations Act 1993</i></p>	<p><i>Water Industry Act 2012</i></p> <p><i>South Australian Water Corporation Act 1994</i></p> <p><i>Public Corporations Act 1993</i></p>
Ombudsman South Australia	Investigates complaints about South Australian Government and local Government agencies	<i>Ombudsman Act 1972</i>
SA Health	<p>Regulates drinking water providers through a registration scheme, including oversight of the preparation, implementation and review of providers' risk management plans.</p> <p>Leads the management of drinking water quality and the approach to managing water quality improvement programs.</p>	Safe Drinking Water Act 2011
Technical Regulator	<p>Regulates the activities of water industry entities by developing and monitoring the application of technical standards, including through the use of Safety, Reliability, Maintenance and Technical Management Plans (a form of asset plans) and setting and monitoring performance against technical standards.</p> <p>Provides advice in relation to safety or technical standards in the water industry to the Commission (at the Commission's request) and in the plumbing industry.</p>	<i>Water Industry Act 2012</i>
Treasurer	<p>Jointly with the Minister for Environment and Water, establishes the Charter for SA Water under the Public Corporations Act 1993</p> <p>Jointly with the Minister for Environment and Water, issues Ministerial Directions under section 6 of the <i>Public Corporations Act 1993</i></p> <p>Issues Pricing Orders under section 35(4) of the <i>Water Industry Act 2012</i></p>	<p><i>Water Industry Act 2012</i></p> <p><i>South Australian Water Corporation Act 1994</i></p> <p><i>Public Corporations Act 1993</i></p>

Appendix 2: Key decision makers

The Commission's economic regulatory function exists within a broader policy and regulatory system that applies to the water industry. Regulatory determinations are informed by, and then inform, decisions made by the South Australian Government and SA Water. The following section summarises the interconnected decisions made by each of the relevant parties in a regulatory determination.

The Commission

The Commission makes decisions about:

- ▶ the maximum demand-adjusted revenue cap for providing water retail services
- ▶ the maximum revenue cap for providing sewerage retail services
- ▶ the form of price control for other excluded retail services
- ▶ the consumer protections required to regulate the relationship between SA Water and its customers
- ▶ any minimum service standards for the retail services provided to customers, and
- ▶ the ongoing monitoring and evaluation framework to track SA Water's performance against all of the above.

SA Government

SA Water owns assets for and on behalf of the South Australian Government for the benefit of the State. The South Australian Government, represented by the Minister for Environment and Water and the Treasurer, is the owner of SA Water, acting for and on behalf of the people of South Australia.

Of direct relevance to the Commission's regulatory determinations, the South Australian Government makes decisions about:

- ▶ SA Water's Corporate Charter,⁷ which sets out the strategic objectives, operational arrangements and financial requirements for SA Water, including:
 - the commercial activities⁸ and non-commercial activities⁹ that SA Water undertakes on behalf of the SA Government
 - borrowing and investment activities, capital structure and dividend and tax equivalent payments

⁷ The Charter is prepared by the Minister for Environment and Water and the Treasurer, in consultation with SA Water, pursuant to section 12 of the *Public Corporations Act 1993*. The Charter is made publicly available on SA Water's website at https://www.sawater.com.au/_data/assets/pdf_file/0006/508245/SA-Water-Charter-October-2019.pdf

⁸ The nature of the commercial operations are set out in section 8 of the Charter and are defined as 'all operations except for those operations specified as non-commercial activities in section 9 of the Charter.'

⁹ The nature of the non-commercial operations are set out in section 9 of the Charter and include operations that are subject to a community service obligation agreement, a direction under section 6 of the *Public Corporations Act 1993*, operational responsibility for water and sewerage facilities in identified Aboriginal communities or operations otherwise agreed by the Minister for Environment and Water and the Treasurer to be non-commercial. Non-commercial operations are to be costed and funded in line with SA Government policy or as determined by the Minister for Environment and Water and the Treasurer.

- prices, including the provision for community concessions to certain customers, as determined by SA Water, the Minister for Environment and Water or Treasurer, and
 - the annual Performance Statement, setting the performance targets that SA Water is to pursue in the coming financial year.¹⁰
- Pricing Orders that the Commission must have regard to, or adopt and apply, when making a determination.¹¹

In addition to the above, the other regulators and agencies responsible for the environmental, health, social and technical regulation of SA Water are summarised in Appendix 1.

To the fullest extent possible, the Commission works with other regulators and decision-makers to understand how it can best contribute towards the efficient and effective functioning of the wider regulatory system. At an ongoing operational level, this includes, but is not limited to, the work done through the Regulators' Working Group. The Commission will continue to work closely with the other key decision-makers to understand the timing and impact of their respective decisions and, to the fullest extent possible, keep other stakeholders informed as soon as is practicable.

SA Water

As noted above, SA Water owns assets for and on behalf of the South Australian Government for the benefit of the State.

Of direct relevance to the Commission's regulatory determinations, SA Water makes decisions about the Regulatory Business Proposal submitted to the Commission for consideration, containing:

- the proposed investment program, including the operating and capital expenditure required to deliver the relevant retail services within the regulatory period set by the SA Government
- the proposed minimum service standards for the relevant retail services, and
- the proposed rate of return.

The Commission's regulatory determination establishes the maximum demand-adjusted revenue SA Water requires to provide services within a defined period of time.¹² Once the Commission has made its price determination, it is up to SA Water, in consultation with the SA Government as the owner of the business, to develop the prices and price structures for the various retail services. Once the final regulatory determination has been made, the Commission's role is then limited to assessing, at the end of the regulatory period, whether SA Water has recovered revenue within the maximum revenue cap set.

Outside of a regulatory determination process, SA Water is responsible for managing the day-to-day decisions. SA Water must manage its overall investment portfolio within the maximum revenue cap established under the Commission's revenue determination. This includes the need to constantly reprioritise its individual investments as circumstances change.

¹⁰ The annual performance statement is prepared in consultation with the Minister for Environment and Water and the Treasurer, in consultation with SA Water, pursuant to section 13 of the *Public Corporations Act 1993*.

¹¹ The Treasurer can issue Pricing Orders pursuant to section 35 of the *Water Industry Act 2012* which are required to be published on the Department of Treasury and Finance website pursuant to section 35(8)(c) of the *Water Industry Act 2012*. All Pricing Orders that have been issued under the *Water Industry Act 2012* are available at <https://www.treasury.sa.gov.au/economy-taxes-and-rebates/economic-regulation>

¹² The SA Government determines the period of time for which the Commission's regulatory determination will apply and publishes this decision in a Pricing Order. For the SAWRD20 period, this was four-years. The Commission has assumed that the next regulatory period will also be for four years.

Regulators' Working Group

In SAWRD20, the Commission established the Regulators' Working Group to facilitate greater coordination between the technical, safety, environmental and public health regulators.¹³ Members of the group are the Commission, Environment Protection Authority, SA Health, the Office of the Technical Regulator and the Department of Environment and Water. For SAWRD24, the Department for Human Services and Department for Treasury and Finance will be invited to join the Regulators' Working Group. As summarised in Appendix 1, each regulator has an important role to play in the overall regulatory system and has an obligation to perform their respective duties.

The establishment of the Regulators' Working Group evolved over the course of the SAWRD16 and SAWRD20 review processes, as all involved regulators took steps to better coordinate their approach to regulating SA Water.¹⁴ This ongoing process has sought to clarify each regulator's respective role in the regulatory system, to minimise duplication of effort, and to identify joint solutions or efficiencies (where possible).

The Commission also worked to introduce greater transparency around the obligations SA Water was required to meet, by requesting public submissions from these other regulators on the extent to which SA Water's Regulatory Business Proposals reflected their requirements. The Regulators' Working Group continues to meet quarterly to discuss emerging issues.

The enhanced regulatory co-ordination achieved in SAWRD20 was considered valuable by most parties, with suggestions that a body such as the Regulators' Working Group should continue.¹⁵ However, there were also calls for greater clarity around the expectations for the outcomes and governance of the Regulators' Working Group.

In particular, stakeholders thought there might be opportunities for the Regulators' Working Group to be more transparent about existing legally binding 'regulatory obligations' as a source of investment requirements for SA Water. There were also discussions about the opportunities for the Regulators' Working Group to provide guidance around future planned regulatory obligations, as early as possible. Stakeholders have expressed support for even greater coordination between regulators in SAWRD24 to ensure that SA Water can efficiently meet a range of regulatory requirements imposed at least cost to consumers. They also commented on the need to ensure that regulatory costs are transparent.

Throughout SAWRD24, SA Water will be asked to provide joint briefings to the Regulators' Working Group on various aspects of its strategy, performance and future plans. To the extent possible, the members of the Regulators' Working Group will also be invited to provide guidance around any future planned regulatory obligations, as early as possible. This will include invitations to attend the six-monthly progress update workshops, and present on any emerging issues to the wider stakeholder group.

These measures will help to introduce a greater level of transparency around the collective impact of the obligations and expectations each regulator places on SA Water.

¹³ Further background information on the Regulators Working Group is available at <https://www.escosa.sa.gov.au/industry/water/retail-pricing/sa-water-regulatory-determination-2020/regulators-working-group>

¹⁴ The Regulators Working Group developed and agreed to a charter outlining the objectives and commitments members made to the SAWRD20 process, available <https://www.escosa.sa.gov.au/ArticleDocuments/1200/20190225-Water-SAWaterRD20-RWGGGroupCharterSigned.pdf.aspx?Embed=Y>

¹⁵ SA Water Regulatory Determination 2020 External post project review, final report, October 2020, pp. 38-39.



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