



WATER SERVICES
ASSOCIATION OF AUSTRALIA



**WSAA submission to IPART
Draft Water Regulatory
Framework**

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Introduction

IPART's new three C's regulatory framework is a significant reform that is strongly supported across the NSW urban water industry. IPART's openness and approach to engaging with all stakeholders in the design of the framework is also best practice.

The three Cs approach shifts the focus from the regulator representing customer interests to:

- the utility deeply understanding those interests
- reflecting and incorporating them into its operations where possible
- holding themselves to account for delivery.

As part of the framework, IPART has released guidance principles on each of the elements of the three C's framework. It is important that IPART set out such guidance as all parties need to understand what the terms 'standard', 'advanced' and 'leading' mean. Utilities need to understand this if they are to self-assess their engagement, outcomes and expenditure in their submission. IPART needs to be able to be able to credibly hold utilities to account against the criteria.

WSAA considers that draft guidance is a sound start and but that it would benefit from further development.

In the spirit of collaboration that IPART has adopted, WSAA suggests that IPART should continue to work with utilities to refine and calibrate the guidance. This is not to remove all subjectivity as in the first iteration of a new framework this is likely to be inevitable (as it was in the first iteration of the PREMO model in Victoria). Rather, it is to reasonably 'set the bar' in the broadly the right place for each category based on what is reasonable and possible.

For example, improvement can be made in the following areas.

1. Recognise that customers can only influence a small proportion of the bill

It should be explicit in the guidance that customers can not have an impact on the majority of the bill. Currently a number of the criteria – particularly for advanced and leading categories - imply levels of effort or outcomes which are unlikely to be achievable. This could have the perverse effect of lowering utility ambition rather than increasing it, to avoid the financial and reputation costs associated with a downgrade.

IPART has cited a number of examples from Victoria which put flesh to terms advanced and advanced and leading. These case studies are valuable and WSAA agrees that each of these represents examples of excellent performance.

However, there is a mismatch between these examples cited and the language in the draft principles. For example, in one of those examples the utility was very transparent with the customer panel on the boundaries of its consultation. On a bill of around \$1000 it was putting forward a range of options that would decrease the bill by \$20 or increase it by \$130 depending on customer feedback. In the final event customer views may have had a wider influence on the utility, but its initial position illustrates that not all issues are on the table with consultation with customers.

By contrast some of the terminology in the Guidelines for customer principles implies a higher level of customer co-design. The guidance needs to be explicit that as part of the engagement strategy, the utility will need to be clear on what customers are able to influence during the engagement process. For example, the WACC and expenditure required to meet compliance with health regulation are not something that customers can influence though it has a material impact on price.

In addition, to be advanced a strategy needs to demonstrate that customer have a 'high level of influence in how services are delivered'. This is unlikely to be achievable. What we think is really meant is the less exciting but more accurate 'customers have a high level of influence on issues that are of the highest priority to them and where their preference can be taken into account in service delivery'.

2. Recognise the importance of the early stages of the engagement strategy

The guidance is focussed on the latter part of the engagement, that is developing outcomes, whereas we see that there should be more focus of the earlier part of engagement, that is determining what the priorities are to customers.

Under Customers Drive Outcomes, Advanced and leading utilities should as part of their engagement strategy:

- clarify with customers what is 'on the table', that is what the customers can influence, and what proportion of the bill this represents
- identify which of these are of the highest priority to the customer
- understanding and establishing what level of influence the customer would like to have to develop the desired outcomes.
- be guided by customers in regard to their level of involvement in developing the outcomes (according the IAP2 spectrum).

Customers may not necessarily want to co-design and co-develop some (or any) of these outcomes. As such empowering customers to co-develop outcomes may not be appropriate as 'leading' criteria for Engage on what matters to customers or Customers drive outcomes. More appropriate might be demonstrating customers have a high level of influence or empowerment in deciding what the priorities are, and what their level of involvement should be in developing outcomes.

3. Clarity is required to distinguish between standard, advanced and leading criteria

While subjectivity is to be expected, the guidance needs to be clear on the distinction between advanced and leading criteria. There are some aspects of advanced and leading engagement where better guidance could perhaps be given to utilities:

- Feedback loop to customers where leading practice is numerous iterations of the insights due to regular check in throughout the engagement process with customers who been part of the engagement, and also with 'uninformed' customers (Customers drive outcomes).
- Some of the best engagement outcomes have been in transforming the customer culture of the business. This can be demonstrated by the level of involvement in the engagement process by different parts of the business. For example, one of the utilities marked as 'leading' for its engagement under the Victorian PREMO model involved 30% of its employees in the engagement. While this won't be appropriate for most organisations, in the case of this utility it demonstrates a leading example for processes support customer centricity.
- While triangulation is mentioned under the advanced criteria for Choose appropriate engagement methods, WSAA feels that this is a critical part of the engagement process and more detail should be provided in what is expected in regards to ensuring decisions are supported by multiple sources of research and data.

- As discussed above, there needs to be more nuance on which outcomes customers can drive. To imply customers can drive all outcomes is either disingenuous or unobtainable. For example to be 'leading' the requirement, without qualification is that 'outcomes and supporting outcome measures and targets are co-designed with customers'.
- WSAA supports the ODI process of setting outcomes, targets and providing incentives to hold the utility to account. We think further work is necessary to set out the degree to which this is required across the full suite of a utility's operations.

4. Performance is a continuum not a step change

In a number of areas to be Leading the utility needs to achieve a 'step change' in performance. WSAA does not consider that 'step changes' are often possible in practice, nor are they theoretically sound (the exception is customer engagement where we think the framework will genuinely lead to a step change in the level of engagement).

In most areas the requirement for step change does not recognise that utilities have operated under a form of incentive regulation for some time. The new regime is more effective, but unless the previous regimes were ineffective the gains across environment, community or costs, are unlikely to represent a step change.

Theoretically it appears that the requirement for a step change sets up the perverse outcome of penalising the most efficient utility. If a utility is already close to the efficiency frontier then it is least likely to be able to make a step change whereas a utility that is least efficient obviously has greater scope for major improvement.

These comments are illustrative, not exhaustive. Nor are they meant to be overly critical. Much of the guidelines are sound in their current form. Nevertheless, we do think that some recalibration is required in key areas to set the 'bar in the right place'.

Contact

We would welcome the opportunity to discuss these issues further.

Adam Lovell, Executive Director, WSAA

[REDACTED]
[REDACTED]

Stuart Wilson, Deputy Executive Director, WSAA

[REDACTED]
[REDACTED]