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Delivering Customer Value

# Draft Water Regulatory Framework

Summary slide pack

# Key changes since Discussion Paper 3

Element of the framework	Preliminary position as at 3 <sup>rd</sup> Discussion Paper	Revised position for Draft Report
<b>Determination length</b>	6-year determination periods as a default, with mid-point check-in	5-year periods as a default, and offering 'Early Engagement' between the business and IPART
<b>Board sign-off of proposals</b>	Not discussed. Pre-reform position is CEO sign-off of proposals	Board endorsement that the proposal promotes the long-term interests of customers
<b>3Cs grading rubric</b>	11 principles underpinning the 3Cs framework	12 principles – splitting out the 'community' principle into two separate 'community' and 'environment' principles  Other improvements to provide clearer guidance
<b>Business self-assessment of its pricing proposal</b>	Grading based on customers and costs	Each business can identify focus principles – appropriate for its customer base – to help inform its self-assessment
<b>Within and inter-period revenue flexibility</b>	Minor updates to our cost pass-through principles	Our framework provides suite of revenue adjustment mechanisms that provide appropriate tools for the business to manage costs that arise during a regulatory period, and guiding principles where IPART will consider proposals for smoothing costs between periods.
<b>Review period</b>	Not discussed. Pre-reform position is 12-month review periods as a default	9-month review process (September-June) as a default.
<b>Modelling simplifications</b>	Not included	Various proposed simplifications in Technical Paper.

# IPART's commitments under the proposed framework



1. **Act fairly** – assess proposals on the quality of what is presented, not on historical experience



2. **Openness** – maintain an open-door policy and proactively engage with boards, executive leadership and regulatory teams



3. **Tailored approach** – focus on matters that materially impact customer value, reward businesses for efforts rather than penalise small errors



4. **Earned autonomy** – high quality proposals will be rewarded with lower regulatory burden



5. **Customer-centric** – hold business accountable for genuinely engaging with customers to identify what is in their long-term interest



6. **Continuous improvement** – continuously listen to feedback and improve the regulatory model

## Next steps

- Draft report release 17 May
- Submissions due 9 August (12 weeks)
- Collaborate with the sector to develop a 'water regulation handbook' through stakeholder-led workshops
- Public hearing
- Implement new framework for 2024-25 water reviews



Summary of our new approach

## Why are we reviewing our approach?

- People continue to need **safe, reliable water** services
- Water businesses provide **essential services**, and customer expectations are changing
- Water sector also facing **numerous challenges** like climate change, population growth and economic volatility
- NSW Government is developing long term water strategies to improve **sustainability and resilience** in water sector
- Regulatory framework needs to evolve to enable businesses to **deliver customer value**

## IPART's key proposals

- **Broaden the focus of pricing reviews** to promote customer value
- Enable businesses to deliver customer outcomes over the short and long term through a more **flexible and tailored regime**
- Financial, procedural and reputational **incentives** that reward businesses for delivering customer value, and penalise those that do not meet their commitments
- Retain elements of the existing framework that work well (building block model, propose-respond etc.)
- No change to the role of IPART, only how we approach regulating water businesses to better promote the long-term interests of customers

# A framework that focuses on customer value

- The business uses the 3Cs principles (customers, costs and credibility) to demonstrate that its pricing proposal promotes customer value
- Business can select 'focus principles' from each 'C' that are most important to customers
- IPART uses the same 3Cs principles to assess proposals

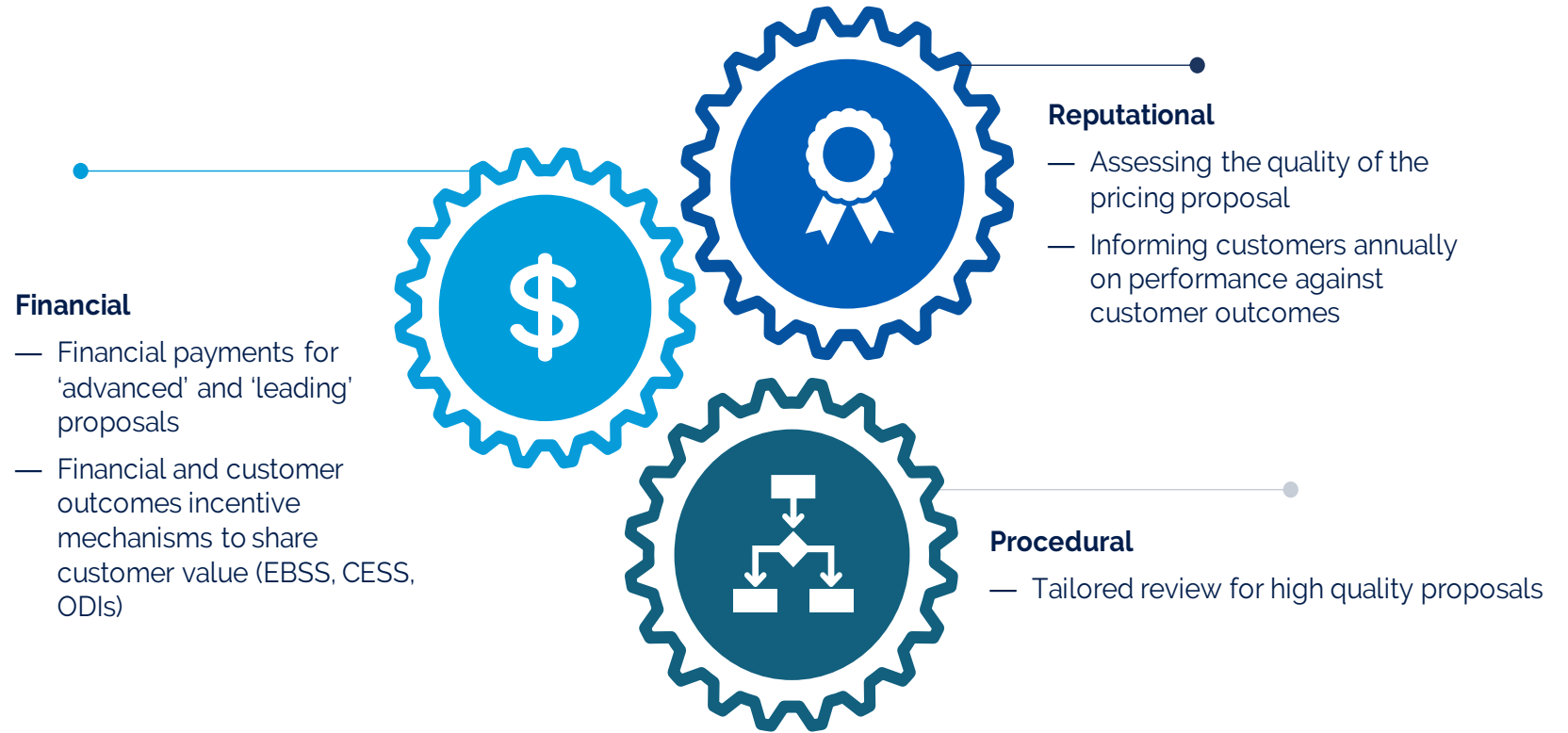




## A flexible, proposal driven approach

- Customers are at the core of the new regulatory model
- The 3Cs framework encourages businesses to engage directly with customers, and develop pricing proposals that meet the long term needs of customers
- The quality of a business's proposal – whether it is promoting customer value at a 'standard', 'advanced' or 'leading' level - determines the way IPART conducts a pricing review
- Businesses that deliver better customer outcomes and cost efficiency are rewarded with streamlined regulatory processes and financial incentives

# Enhanced incentives to promote customer value



# Financial incentives that align business and customer interests

- Provide reputational and financial rewards for high-quality pricing proposals assessed as 'advanced' or 'leading'
- This supports innovation and better customer outcomes

## Annual revenue adjustments based on quality of pricing proposal

		Business self-assessment		
		Leading	Advanced	Standard
IPART assessment	Leading	2.5%	1.75%	n/a
	Advanced	1%	1.25%	0.5%
	Standard	-1%	-0.5%	0%
	Sub-standard	Business to review proposal and resubmit		

- Additional financial and service performance mechanisms for advanced and leading businesses
- Balanced incentives to improve service levels and reduce costs
- Support businesses to make longer-term trade-offs that benefit customers

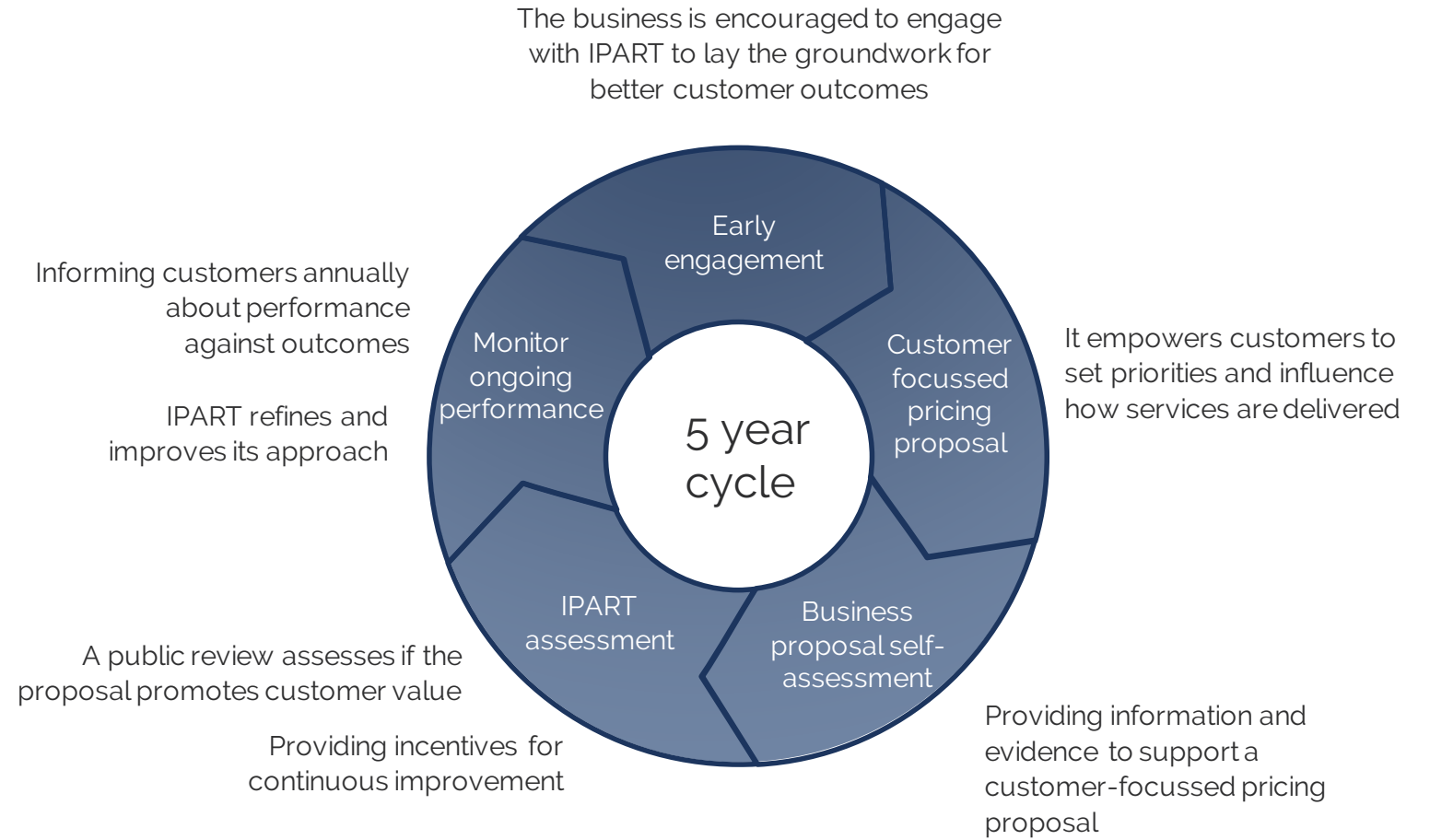
Ongoing  
monitoring of  
performance to  
promote long term  
thinking

- Additional focus on performance throughout the regulatory period
- The framework is designed to encourage all businesses to improve on its performance year-on-year, from its own starting point
- IPART focuses on matters that materially impact customer value
- Incentive mechanisms reduce regulatory burden over time. By providing balanced incentives, IPART can rely on these to be confident business decisions are efficient, and place less reliance on periodic expenditure reviews by consultants

## Additional improvements to support water businesses

- Clear principles and guidance about regulatory tools to manage cost uncertainty, and inter-generational price smoothing
- Develop a 'water regulation handbook' to support customer-centric proposals
- Improvements to the expenditure review process including:
  - 9-month pricing review (instead of current 12-months)
  - A base-step-trend approach for operating expenditure
  - Ex-post capex reviews by exception only
  - Simplify building block model and information returns
- Establish a Regulators Advisory Panel (RAP) to promote collaboration among the NSW water sector regulators
- Built-in commitment to review and update the framework

# Pricing proposals drive how we employ regulatory tools



# A tailored approach to price regulation

Standard proposals:	Advanced/leading proposals:
<ul style="list-style-type: none"> <li>• Pre-set <b>maximum prices</b> to meet customer outcomes</li> </ul>	<ul style="list-style-type: none"> <li>• Options for <b>different price structures</b></li> <li>• Scope for <b>differentiated pricing</b> for specific customers</li> <li>• Financial flexibility to deliver customer value through <b>incentive schemes</b></li> </ul>
<ul style="list-style-type: none"> <li>• <b>Reviews of proposed expenditure</b></li> </ul>	<ul style="list-style-type: none"> <li>• A <b>focus on outcomes</b> rather than internal processes</li> </ul>
<ul style="list-style-type: none"> <li>• An expectation for <b>pre-review engagement</b> with IPART</li> </ul>	<ul style="list-style-type: none"> <li>• Optional pre-review engagement with IPART</li> </ul>

- Changes to the regime for all businesses:
- A stronger focus on **customer outcomes**
  - **Self-assessment** of proposals against IPART's 3Cs criteria
  - **IPART assessment** of proposals as either standard, advanced or leading
  - Better **collaboration** between water sector regulators by establishing the Regulator's Advisory Panel
  - **5-year regulatory periods** to promote better long-term planning