

Our ref: DOC22/262276

Ms Donnelly, IPART Chair  
PO Box K35, Haymarket Post Shop NSW 1240

By email: [REDACTED]

20 September 2022

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## Subject: IPART Review of Regulatory Framework

Dear Ms Donnelly,

I am writing to you regarding the Independent Pricing and Regulatory Tribunal's (IPART's) Draft Report *Delivering Customer Value: Draft Water Regulatory Framework*.

As the Chief Executive Officer, NSW Water Sector, I support the intent of IPART's proposed new regulatory framework, incentivising regulated water businesses to deliver long term value for customers. I acknowledge that the framework introduces useful improvements, and I commend the focus on:

- establishing clear objectives that aim to deliver long-term value for customers and the community
- increasing the transparency of the regulatory process
- encouraging innovation and holistic planning
- improving performance monitoring and accountability for delivery of outcomes
- extending regulatory periods to 5 years.

I support the broad direction of IPART's proposed updates to the regulatory pricing framework for the sector. However, I wish to raise some potential challenges for applying it to the regulation of the Water Administration Ministerial Corporation's (WAMC's) water management services.

### Limitations of cost benchmarking and comparative expenditure reviews

The proposed 3Cs framework notes that benchmarking will play a key role in assessing the performance of businesses and the quality of its proposal, in particular to compare proposed expenditure with industry benchmarks. IPART's report suggests that benchmarking will indicate whether current expenditure is efficient, reducing the need for additional scrutiny of proposed costs.

Benchmarking expenditures across WAMC water management activities will be challenging as there are no comparable entities with the same legal context, regulatory framework or breadth of functions. In most states, government departments carry out their water management functions with no separate accounting and charging, or transparency for these services. For example, in Victoria, water management is shared between regional water corporations and catchment authorities that are partly funded through environmental levies. These significant differences in

functions and funding sources, including the absence of independent pricing regulation, will make it difficult to do a comparative assessment of WAMC across jurisdictions. Given these issues, it is likely that effective benchmarking of WAMC costs would take the same, if not more, regulatory effort to implement than the current framework. Providing regulatory confidence will be very difficult and any benchmarking is likely to be unreliable and require heavy qualification.

### Engagement challenges for WAMC water management services

IPART's draft regulatory framework proposes a greater focus on customer engagement to inform outcomes and services to be delivered by water businesses. I support the focus on delivering value to customers over the long-term, however I am concerned that some of the customer engagement principles cannot be applied to the WAMC context.

The customer principles outlined in IPART's draft framework are heavily focussed on utilities delivering urban water and wastewater services to customers who directly benefit from these services. However, WAMC delivers a much wider mix of functions with a strong focus on broad community and environmental outcomes for a much wider community of interest. Most WAMC functions are required to meet legislative water planning and management obligations, including compliance and enforcement activities undertaken by the Natural Resources Access Regulator (NRAR). Further effective implementation of many WAMC activities can have consequences that limit customers' access to water and the value they derive from it, at least in the short term. This will create risks for perverse outcomes if pricing regulation is too reliant on customers' preferences about the service levels of future WAMC activities.

IPART's report notes that the framework will be flexible and move away from a one-size-fits-all approach. It would be useful if IPART could provide guidance on incorporating feedback from the broader community and the role of customers as impactors in the context of WAMC activities. This would assist WAMC to tailor its engagement to its core business of managing water resources to balance the needs of the environment, water users and communities.

### The complexity of the regulatory framework and the role of incentives

IPART's 3Cs framework and the upfront financial incentives linked to proposals seek to provide a strong focus on innovation and provision of additional or higher quality services beyond the standard level.

In recent years WAMC has placed greater importance on planning for the future and delivering on our core objectives. We have implemented reforms that improve coordination in the sector, strengthened compliance and enforcement, made responsibilities clear and have released a Greater Sydney Water Strategy and regional water strategies across the State.

The proposed incentive mechanisms in IPART's draft regulatory framework appear too complex. These mechanisms are likely to see the regulatory effort shift from ensuring robust planning, efficient delivery, and accountability consistent with Government policy direction to a focus on uncertain benchmarking and cost modelling beyond the current horizon for detailed long-term capital plans.

## Department of Planning and Environment

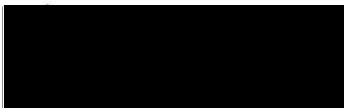
In the case of the proposed Capital Expenditure Sharing Scheme (CESS), the incentive mechanism seems weak compared to the benefit of obtaining a return on capital expenditure over the lifetime of the asset that is inherent in the regulatory framework.

Review of proposed capital expenditure, particularly for utilities with high levels of capital remains essential. Further detail on the workings of the incentive schemes within a regulatory review scheme is needed. Detailed worked examples should be based on IPART's assessment of how to tailor incentives for businesses to maximise efficient capital expenditure through the price determination period in a range of scenarios.

For WAMC, the focus of incentives should be on the core challenges of providing sustainable, efficient and affordable services across the water sector.

I would welcome ongoing dialogue with the Tribunal to ensure the regulatory regime remains clear and credible and contributes to delivering outcomes in the long-term interest of customers and the community.

Yours sincerely,

A solid black rectangular box redacting the signature of Jim Bentley.

Jim Bentley

Chief Executive Officer, NSW Water Sector