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Dear Commissioners

Inquiry into reform of South Australia's regulatory framework

The Essential Services Commission welcomes the opportunity to provide background regulatory and contextual information to assist the Productivity Commission in its Inquiry into the reform of South Australia's regulatory framework.

As you are aware, the Commission has already provided responses to the Productivity Commission in response to information requests. This submission will not repeat those responses and instead focusses on the Commission's approach to its economic regulatory and advisory functions.

About the Commission

The Essential Services Commission of South Australia is an independent statutory authority with regulatory functions covering a range of essential services, including water, sewerage, electricity, gas, rail and maritime services, and advisory functions on regulatory and economic matters. Its statutory objective under the *Essential Services Commission Act 2002* is the protection of the long-term interests of South Australian consumers with respect to the price, quality and reliability of essential services.

In meeting that objective, the Commission aims to add long-term value to the South Australian community through providing robust, fit-for-purpose and effective consumer protections in its regulatory regimes and holding entities accountable for their services, while not imposing unnecessary regulatory costs and burdens. Our independent advice to Government informs, and provides an evidence base for, policy making and public consideration of economic and regulatory issues.

In meeting that objective, the Commission seeks to add long-term value to the South Australian community through providing robust, fit-for-purpose and effective consumer protections in its regulatory regimes and holding entities accountable for their services, while not imposing unnecessary regulatory costs and burdens. Our independent advice to Government informs, and provides an evidence base for, policy making and public consideration of economic and regulatory issues.

Our business model involves designing and implementing effective and efficient regulatory frameworks, monitoring and analysing market outcomes under those frameworks and taking action (feedback to businesses, public reports or compliance and enforcement) as needed. Critically, both

that model and our regulatory frameworks are subject to continuous internal and external review, as we look for refinements and improvements over time.

As an independent economic regulator, our role encompasses licensing, consumer protection, service standards, pricing, monitoring, compliance and public reporting in the water, electricity and gas industries, as well as access regulation of essential ports and rail infrastructure.

Through our advisory role, we provide advice and conduct Inquiries to inform the South Australian Government on economic and regulatory policy issues, including but not limited to those industries which fall within our existing regulatory scope.¹

The sectors and businesses that we regulate play a key role in our State's economy. They must operate efficiently and be transparent with and accountable to their customers, particularly in response to customers' changing needs and expectations. Our regulatory approach looks to drive and encourage that accountability, including through requirements for consumers' views and preferences to be genuinely considered by service providers when developing and implementing their long-term business plans.

In that context, we emphasise engagement with our stakeholders - consumers, industry and government. Engagement helps us to understand the context of our work and provides us with a wide range of diverse evidence on which to base our decisions. Critically, by providing opportunities for customers to understand and challenge both their service providers and our decisions, we are better able to deliver robust, independent and well-implemented regulatory and advisory outcomes.

Our business model (explained further below) involves us designing and implementing effective and efficient regulatory frameworks, monitoring and analysing market outcomes under those frameworks and taking action (feedback to businesses, public reports or compliance and enforcement) as needed. Critically, both that system and our regulatory frameworks are subject to continuous internal and external review, as we look for refinements and improvements over time.

Our Strategy guides us in all of these areas, helping us to meet our objective of protecting consumers' long-term interests and to deliver robust, independent advice to the South Australian Government.

We also recognise that we operate in an environment of multiple regulatory agencies and broad policy considerations. The Commission is a regulatory and advisory body within that context, with defined roles and functions, and does not have a policy remit. It is therefore important that we work with other agencies to ensure a consistent and complementary regulatory approach, focussed on the long-term wellbeing of all South Australians.

Our Operating Context

Our regulatory frameworks must be responsive to our operating context and environment. We have identified four factors which may influence those frameworks and the advice that we provide:

- ▶ Changing market and industry structures, including the impacts of new and emerging technologies and events such as COVID-19
- ▶ Changing community expectations on standards of service and access to essential services
- ▶ An increasing focus, nationally and internationally, on ethical business practice and how this translates to ethical business regulation, and
- ▶ South Australian, Australian and global economic climate and trends.

¹ For a list of Inquiries and a copy of Inquiry reports and associated materials, please refer to the Commission's website at <https://www.escosa.sa.gov.au/inquiries>

In responding to these factors, we continually test, review and modify (if appropriate) our approach against the business model to reflect our key functions of regulatory design, market intelligence and analysis, and regulatory action, all underpinned by robust and genuine stakeholder engagement and evaluation of our performance.

Our Areas of Action

Having regard to our operating context, the Commission is currently focussing on five areas to consolidate and strengthen our economic regulatory and advisory functions, contributing to the achievement of our statutory objective.

- ▶ Building stakeholder engagement and providing for consumer inputs and challenge: genuinely engaging with all of our stakeholders to facilitate understanding of consumer and regulatory issues, obtaining the best and widest range of evidence for our work and providing opportunities for consumers to contribute to and challenge service providers' business plans.
- ▶ Design of regulation: delivering fit-for-purpose regulatory design and implementation, using evidence-informed processes and pursuing efficiency and effectiveness in regulatory design, implementation and outcomes.
- ▶ Analytical capability: enhancing our analytical capacity and capability and the use of market intelligence to underpin our regulatory design, monitoring of performance outcomes and the regulatory actions that we take.
- ▶ Regulatory performance: using market monitoring outcomes to provide performance information to consumers, guidance and performance feedback to regulated entities, and reshaping our compliance and enforcement approach to ensure that it is efficient and effective in driving positive consumer outcomes.
- ▶ Evaluation capability: embedding evaluation of our performance – both regulatory and operational – across all of our work, with ex-post and post-implementation reviews being an important element of that evaluation.

In doing so, we take the global learnings of ethical business practice and regulation, ensuring that we continue to focus on independent, robust, evidence and risk-informed decisions and advice, using enhanced market intelligence and analysis to drive efficient and effective compliance and verification.

Each of those areas is expanded on below.

Building stakeholder engagement and providing for consumer inputs and challenge

The information, evidence, knowledge, insights and advice gained from a diverse range of sources through genuine and effective engagement enhances the quality of our work: we are committed to genuine engagement with all of our stakeholders – consumers, industry, government – and acting on the best available data and information. This includes providing readily accessible opportunities for consumers and other stakeholders to understand and challenge our evidence, analysis, findings and conclusions in our regulatory decisions and advisory work.

We particularly acknowledge the importance of providing consumers with the opportunity to test and challenge service providers' price/service/quality proposals through regulatory processes. Consumers can and should have the ability to express to service providers their views on those matters when service providers are starting to develop their business plans. They should also be able to verify that their views have been appropriately considered by service providers once those business plans have been finalised, before regulatory assessment processes commence, as well as during regulatory assessment.

Over the past four years, we have had a focus on establishing principles and practices which will start to entrench those opportunities for consumer input and challenge. This has particularly been the case in relation to our economic regulation of SA Water.² For the 2020 regulatory determination, that included new practices and processes which sought to:

- ▶ 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.
- ▶ Introduce direct customer challenge and negotiation into the preparation of SA Water's draft business plan, in a constructive and non-adversarial approach, including through the use of a negotiation forum.

As explained further below, we are reviewing the effectiveness and efficiency of those practices and principles with a view to adopting them (with appropriate refinement from our evaluation of the 2020 regulatory process) for both the 2024 regulatory determination for SA Water and more widely across the industries we regulate.³

Design of Regulation

We focus on designing efficient and effective long-term regulatory frameworks and processes that deliver the lowest sustainable prices for consumers, reflective of the service levels for which they are willing to pay. This involves examining the need for regulation (regulating only when it delivers benefits to consumers that exceed the costs of regulation), considering the costs (to those who are regulated and to consumers) of the potential different forms that regulation may take and designing our regulatory frameworks using the best available evidence.

To obtain that evidence, we engage with all of our stakeholders to understand their views, and will draw on the market intelligence that we routinely gather, as the information and advice we gain in that way enhances the quality of our regulatory design.

We regularly review our regulatory frameworks, in terms of both outcomes and process, to ensure that they continue to be effective, targeted to the needs of consumers and cost-effective in practice, thereby protecting consumers' long-term interests.

Analytical Capability

Our analytical capacity and capability are critical inputs to our regulatory design and advisory work, as well as our ability to understand and act on regulatory performance outcomes.

² See the Framework and Approach paper which underpinned the 2020 Regulatory Determination for SA Water, available at <https://www.escosa.sa.gov.au/projects-and-publications/projects/water/sa-water-regulatory-determination-2020-framework-and-approach>.

³ Refer the current consultation on the Framework and Approach for the 2024-28 Regulatory Determination for SA water, available at <https://www.escosa.sa.gov.au/projects-and-publications/projects/water/sa-water-regulatory-determination-2024-framework-and-approach/sawrd2024>

Our capacity is our internal skill and ability - in both our people and our systems - to learn and develop our talents, and to obtain, understand, store and analyse data and evidence.

Our capability is the way in which we use data and evidence to generate information which supports our regulatory actions and advisory work, as well as our evaluation of the effectiveness of that work over time and, where needed, in refocussing our approach that must always be robust, effective and flexible.

We continue to enhance and, where needed, reshape our existing capacities and capabilities in data analytics and market intelligence gathering, and continue to invest in our people and our technologies to ensure that we are optimising long-term value from the data and information that we seek and use (acknowledging the costs of data provision by regulated entities). We will also continue to seek working partnerships with regulated entities, other regulators and agencies and consumer groups, in order to improve our information sources, knowledge and abilities.

Regulatory Performance

We use data and information to design and implement regulatory frameworks which reflect consumers' preferences and willingness to pay. This allows us to develop indicators of success, to monitor market outcomes, to question and provide feedback to regulated entities on their performance, to acknowledge positive outcomes and to regularly assess our own performance levels and trends in order to discover whether there is potential to improve consumer outcomes.

We also use data and information to provide consumers with insights and to explain trends in market outcomes – while at the same time encouraging or requiring regulated entities to publish information and advice, in order to demonstrate their own commitment and accountability to their customers.

Where evidence shows that regulated entities have failed to meet regulatory requirements (or are at risk of doing so) and are not being accountable to their customers, we will use our intervention powers - verification, compliance and enforcement.

We constantly look to enhance and refine our approach and practices in all of these areas, understanding that the community expects a strong, targeted and risk-based compliance focus on regulated entities' performance, and we work with regulated entities to assist them in transparently demonstrating their performance to their customers.

Evaluation Capability

We are continuing to build our capability to evaluate, report and act on the outcomes of our regulatory decision-making, as well as our own operational performance. In doing so, we look widely to understand best-practice in evaluation techniques (locally, nationally and internationally) and engage and consult with our stakeholders on those matters.

We also seek information from and collaborate with stakeholders on individual evaluation projects. For example, we recently assessed the effectiveness of the new and enhanced processes that we adopted for the SA Water Regulatory Determination 2020 - and did so in a public and transparent manner (including an independent report on the process and a subsequent Issues Paper seeking views on that report and potential next steps).⁴

⁴ A copy of the independent ex post review conducted by Dr Pat Walsh is available at <https://www.escosa.sa.gov.au/news/water-news/dec20-news-w-sawrd20-furtherinfo2> , and the Commission's Issues Paper for the 2024 SA Water regulatory determination (heavily informed by Dr Walsh's report) is available at <https://www.escosa.sa.gov.au/projects-and-publications/projects/water/sa-water-regulatory-determination-2024-framework-and-approach/sawrd2024>

That focus extends to assessing and understanding the outcomes of our determinations, which has a longer-term horizon and requires analysis of businesses’ regulatory performance and consumer outcomes over time. This informs us of the changes, improvements or enhancements necessary in subsequent determinations that will allow us to better meet our consumer protection objective.

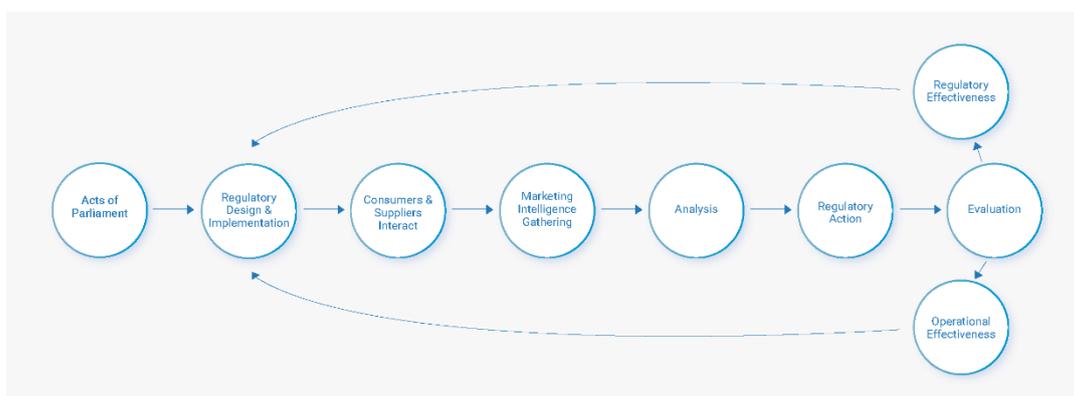
This evaluation capability is also applied to our internal operational practices, making sure that we operate in an efficient and effective manner. We remain committed to publicly reporting our evaluation outcomes and to refining our evaluation techniques over time.

Our Business Model

In meeting our objective of protecting the long-term interests of consumers with respect to price, quality and reliability of essential services, we operate with a carefully developed and tested business model – ensuring that our regulatory design and action is effective and evaluated over time.

The business model provides a framework for both delivering value and adapting to the challenges – including a changing environment and community expectations – that we see in our operating context ahead.

The business model reflects our key functions of regulatory design, market intelligence and analysis, and regulatory action, all underpinned by evaluation of our regulatory performance and operational systems.



Conclusion

The Commission is keen to continue to contribute to the Productivity Commission’s work on this Inquiry and is happy to provide further information as required. In that context, having regard to the Inquiry’s references to the work of the OECD in this area, we note that the Commission’s CEO, Adam Wilson, is a member of the OECD’s Network of Economic Regulators, and may be able to provide further advice and updates on recent thinking in that forum as needed.

Should you wish to discuss these matters further, please contact Adam Wilson, Chief Executive Officer, on 0439 814 257 or via email on adam.wilson@escosa.sa.gov.au.

Yours sincerely

Brett Rowse
Chairperson

Letter will only be sent electronically