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Our Ref: 12,238,153
Contact Officer: Karen Krist

Dear Mr Gaetjens

Re: Regulator Performance Guide, April 2021

Thank you for the opportunity to comment on the consultation draft of the *Regulator Performance Guide* released April 2021.

The AER supports the overarching direction of the Guide - that is, that Australian regulators should commit to providing an outcomes-focussed, principles-based service that emphasises a proportional approach to risk and genuine engagement with regulated entities and the broader community. This aligns with our vision to be a high performing regulator that is independent, open and accountable; builds trust in Australia's energy system; takes considered risks; ensures the regulatory regime is fit for purpose; and engages actively with stakeholders.

In December 2020, the AER finalised and launched its five year Strategic Plan 2020-2025. In addition to our four strategic objectives, the Plan articulates our enablers – the way we need to work. Our objectives and enablers are well aligned with the three principles articulated in the draft Guide.

Principle 1: Continuous improvement and building trust

The Guide's Principle 1 asks regulators to adopt a whole-of-system perspective, continuously improving their performance, capability and culture, to build trust and confidence in Australia's regulatory settings. In practical terms this includes having well defined and communicated organisational values and culture; considering best practice examples from other jurisdictions; and minimising duplication with other regulators.

Our Strategic Plan clearly signals our intention to grow an organisational culture that supports our strategic direction, though a focus on 'Achievement' and 'Innovation'. Our innovative response during the COVID-19 pandemic through the publication of a series of Statements of Expectations designed to protect consumers experiencing hardship exemplifies our commitment to an agile, adaptive and flexible approach. We are currently developing a Culture Plan which will guide our behaviours and ways of working, as well as how we support and develop our people.

Additionally, several of the priorities in our Strategic Plan demonstrate our commitment to evolving our regulatory services so that they remain fit-for-purpose, including by:

- being more efficient in our regulation by focussing on high-impact actions that matter most to consumers;
- making sure that our regulatory regime and our network performance reporting evolves to support the energy transition;

- advocating for simplification of the retail market regulatory framework to encourage effective competition and reduce the cost to serve; and
- implementing regulatory sandboxing, informed by (international) best practice models.

Principle 2: Risk-based and data driven

Principle 2 will require regulators to maintain essential safeguards, using data and digital technology to manage risks proportionately to minimise regulatory burden and to support those they regulate to comply and grow. Adopting a risk-based and data-driven approach can mean regulators: use intelligence and data to inform a risk-based approach to compliance and enforcement; publish and maintain a compliance and enforcement strategy; and build capability to maximise the use of data and digital technology.

The AER takes a risk-based approach, informed by data, evidence and intelligence. Our Compliance and Enforcement Policy outlines how we ensure accountability, confidentiality, timeliness, proportionality and fairness in our approach to compliance and enforcement. We do this by fostering compliance, applying a risk-based approach, working with other agencies and working in a transparent manner. Recently we have enhanced our underpinning of this approach by improving the granularity in assessment of both static (obligation-based) compliance risk and introducing new dynamic (entity-specific) risk measures.

Also, our Strategic Plan provides that we will:

- enhance sources and use of market intelligence in compliance and enforcement activities;
- improve market surveillance capability to interrogate information more effectively; and
- develop an information management framework for compliance intelligence.

Principle 3: Collaboration and engagement

The Guide's Principle 3 provides that regulators should be transparent and responsive, implementing regulation in a modern and collaborative way. This means that regulators will engage genuinely with stakeholders and listen to feedback; provide guidance and information to help regulated entities understand their obligations; and be transparent in their decision making.

In accordance with our own *Stakeholder Engagement Framework*, the AER's work is informed by regular dialogue with a range of stakeholders including other market bodies, industry bodies, consumer groups and governments. The AER recognises that we must: proactively engage with stakeholders and seek to listen to and understand diverse perspectives; embrace creative ways of engaging that work for stakeholders, not just us; and clearly communicate decisions and make it easy to engage with us.

AER recommendations for the draft Guide

While the three principles articulated in the draft Guide are well aligned with our own direction and therefore broadly supported, we would note the following reservations:

- Draft Principle 2 elaborates that adopting a risk based and data driven approach can mean that regulators "modify their regulatory approach to encourage voluntary compliance where possible...". We recommend that 'where possible' is replaced with 'where appropriate'.

- Draft Principle 3 is titled “Collaboration and Engagement”. As a regulatory body, we find the use of the term ‘collaboration’ problematic and suggest replacement with ‘consultation’.

The AER believes that best practice regulators engage actively with all stakeholders, as reflected in the description of our own practice above. However, we do not ‘co-design’ or ‘collaborate’ with regulated entities (for example, regulated monopoly electricity and gas network businesses) on the design and implementation of our regulatory systems and processes. To do so would risk undermining our independence (either real or perceived) and may lead to outcomes that do not align with our statutory duties to promote the interests of consumers. Rather, we take a cooperative approach by consulting genuinely and then make decisions that are in the best interests of Australian energy consumers.

We work closely with our consumer stakeholders, to whom we are ultimately responsible for our decisions. Where appropriate we collaborate; for example in our current work on developing a Vulnerability Strategy. We are currently collaborating with key (consumer) stakeholder groups on the design of actions that the AER can take or contribute to, which will improve outcomes for consumers in vulnerable circumstances over the next three years.

- The explanatory text under draft Principle 3 emphasises the importance of ‘clearly setting out the obligations imposed on regulated entities’. We suggest that this language be softened to better accommodate principles-based regulatory approaches.

We agree that best practice regulators should communicate their expectations of regulated entities clearly. However, where risk and the regulatory context allows, we prefer a principles-based approach to regulation which provides flexibility for businesses to determine the means by which they will comply.

Principles-based regulation is by its nature, less clear than prescriptive obligations. However, well designed principles-based regulation seeks the appropriate and necessary level of protection with the minimum level of regulatory burden. Principles-based regulation can also help to drive innovation and efficiencies from an economic regulation perspective. It does this by effectively allocating risk and incentives to regulated businesses in a manner that promotes responses that are aligned with the interests of consumers. One way that we manage the ambiguity that is inherent in principles-based regulation is through the issue of guidelines.

We recommend that care be taken to ensure that an emphasis in the Guide does not lead to the unintended outcome of regulators favouring prescription over principles in circumstances where principles-based regulation is likely to be more effective.

- Although the Guide promotes outcome-focussed performance frameworks, a number of the example measures reflect outputs rather than outcomes. Ideally the Guide would provide more useful examples that we could learn from. This should be a goal for future iterations of the Guide.

Measuring outcomes and impact is an important but difficult area for regulators. The AER has recently undertaken an organisation-wide review of our Key Performance Indicators with a view to making them less about outputs and more about outcomes and impact. Our initial review of performance measurement by different regulators, in Australia and overseas, suggests that there are few outstanding examples of performance measurement and reporting focused on impact and outcomes, and considerable scope for improvement.

We also note that quite often regulators are contributors to outcomes, but do not solely own them. In transitioning to an outcome-focussed performance framework it

needs to be recognised that achievement of performance targets will not be entirely within regulators' control.

In regard to the relationship between regulators' performance frameworks and Ministerial Statements of Expectations, we note that the Government's most recent Statement for the AER expired in 2017. In the absence of a current Statement we have used the former Council of Australian Governments' *Strategic Energy Plan* as the foundation for the direction articulated in our *Strategic Plan 2020-2025*. This Strategic Plan will underpin our annual Corporate Plans until 2025, with each Corporate Plan focussing on what we will achieve in that financial year. Further, and consistent with the recommendations of a recent ANAO audit, the AER has recently developed a performance measurement and reporting framework, aligned to our new Strategic Plan, which contains improved performance measures. We look forward to working with Energy Ministers on the next iteration of the Statement of Expectations to ensure it complements our new performance framework.

The proposal for performance monitoring and reporting to be via the existing Corporate Plan and Annual Report processes is welcome.

Thank you again for the opportunity to comment. Should you require any further information, please contact Karen Krist at karen.krist@aer.gov.au.

Yours sincerely

Dr Liz Develin
Chief Executive Officer, Australian Energy Regulator

Sent by email on: 20.05.2021