



John Pierce
Chairman
Australian Energy Market Commission
PO Box A2449
Sydney South NSW 1235

16 October 2014

Dear Mr Pierce

Cotton Australia welcomes the opportunity to comment on the AEMC's draft rules for distribution network pricing. Cotton Australia is the key representative body for Australia's cotton growing industry. The cotton industry is an integral part of the Australian economy, worth over \$2.5 billion in export earnings and employing 10,000 people.

The overarching objective of the draft network pricing rules is to ensure network prices are set to reflect the costs of providing network services, allowing consumers to make better decisions about energy use. The draft pricing determination will require networks to apply the following pricing principles:

- Network pricing objective: prices reflect the efficient cost of providing network services to consumers
- Long run marginal costs: prices are based on the network's long run marginal costs
- Total efficient cost recovery: networks recover revenues without distorting price signals to consumers
- Consumer impact principles: prices can be understood by consumers and impacts on consumers are managed
- Jurisdictional obligations: networks adhere to any jurisdictional obligations.

Cotton Australia is concerned that without flexibility and equity embedded into the principles, cost reflective network tariffs have the potential to unfairly disadvantage electricity consumers in regional Australia, despite the jurisdictional obligations and consumer impact principles.

There is already a clear imbalance in network charges between the regions and urban areas. The network charge for regional Queensland and NSW is around 30% more than the network charge for urban areas of those states (Figure 1).

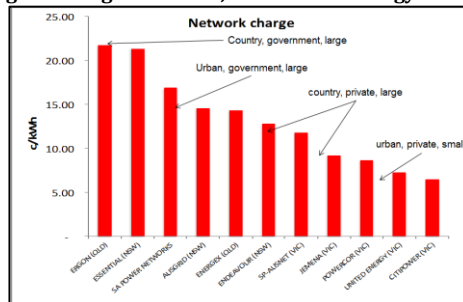
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In NSW, Essential Energy maintains 1.4 million poles, 400 substations and 200,000 kilometers of power lines for 800,000 consumers. By way of comparison, Ausgrid maintains 500,000 power poles, 200 substations and 50,000 kilometers of power cable for 1.6 million consumers in the Sydney, Hunter and Central Coast area.

Figure 1: Network charges are higher in regional areas, Carbon and Energy Markets 2013



The objective of the National Energy Law is to promote efficient investment in, and efficient operation and use of, electricity services for the long term interests of consumers of electricity with respect to – price, quality, safety, reliability, and security of supply of electricity; and the reliability, safety and security of the national electricity system.

Cotton Australia considers that the objective of the rule change should ensure that the market delivers a fair and equitable price for electricity, particularly for regional Australia. We recognise the importance of efficient pricing and cost-reflectivity in tariff setting, however we ask that the AEMC consider the need for the principles of flexibility and fairness in the draft network pricing rules.

As highlighted in our previous submission to the AEMC on network pricing rules, the Australian cotton industry has made structural on-farm irrigation adjustments, which have seen significant improvements in water efficiency. However these new irrigation systems are also more energy intensive. The timing of cotton farm irrigation is driven by water license conditions, the need of the crop and weather patterns. The impact on irrigators of moving to cost-reflective tariffs has been acknowledged by the Commonwealth Government in its Energy Green Paper:

Some consumers are not in a position to change their electricity consumption patterns in response to price signals...agricultural businesses such as irrigators where the time of electricity use is not flexible. Both the pattern of daily use and overall use will affect the cost implications of cost-reflective tariffs on such consumers.



Already, we have seen businesses replace water efficient irrigation systems and return to flood irrigation methods to minimise exposure to electricity network price rises. We are concerned that further price rises will force many irrigators to go off grid or leave the industry altogether. As most of the Australian cotton crop is irrigated, if 10% of the irrigated cotton industry elected to leave the industry this represents a fall in Australia export earning of up to \$350 million per year. Importantly for networks, if irrigators switch off or leave the grid the networks risk a lower revenue base and higher number of stranded assets.

As such, we ask that the draft rules be expanded so that networks are required to set tariffs that are efficient, subject to a cost consideration for regional Australia and are flexible enough to recognize that some consumers are constrained by factors outside their control.

Current network tariffs, particularly those offered to irrigators in NSW, do not encourage efficient use of the system. By incorporating flexibility and equity into the draft rules, we would expect networks to design tariffs that provide real incentives to switch usage patterns (critical peak/off-peak) and recognise and reward users for accessing network in off-peak periods. Flexibility would allow a tariff structure that delivers a positive correlation between the network tariff charges and the electricity usage pattern of irrigators. For example, a decrease in use or shift in use to shoulder and off-peak time would trigger a decrease in prices for network charges. The use of demand or capacity charges perversely penalises growers for using the network when it is actually required. There are cases where the demand charge is so significant that growers have placed locks over their irrigation pump switches to prevent accidental usage. We are aware of a grower who was charged \$2,000 in a month for using 20kWh, the equivalent of an average daily household consumption.

Cotton Australia supports the NSW Irrigators' recommendation (in its previous submission to the AEMC on network pricing principles) that food and fibre irrigation tariffs should adhere to the following design principles:

- There should be a positive correlation between the network tariff charges and the electricity usage pattern of irrigators.
- Tariffs should not discourage irrigators from participating in national and state water efficiency and land care programs
- Tariffs should not discourage irrigators from utilising technologies and infrastructure that contribute to the national goal of increased food and fibre production:



- Tariffs must allow for an efficient use of electricity related equipment on farms.
- The tariffs must allow for optimal water application that best assists plant growth.
- The tariffs must avoid the perverse pricing outcomes associated with demand/capacity charges, where irrigators are penalised for using network to irrigate based on the need of the crop, weather and license conditions, rather than when irrigation is not required.

While Cotton Australia is concerned about the potential price impacts for regional consumers transitioning to cost reflective tariffs, we support the inclusion of consumer impact and jurisdictional obligation principles in the draft rules. Nevertheless these principles do not of themselves inject equity and flexibility into the rules. Especially as there are currently no jurisdictional obligations applying to agricultural businesses in regional NSW. While in Queensland there are plans to phase out transitional tariffs over the next 10 years.

Through the Energy and Agricultural Competitiveness White Paper processes, Cotton Australia is seeking the introduction of a Regional Australia Food and Fibre Community Service Obligation (F&F CSO). The Regional Australia F&F CSO will address the inequitable costs of providing electricity to regional Australia, compared to urban and semi-urban Australia. A Regional Australia F&F CSO would have the multiple benefits of providing support for regional Australian communities, as well as preventing the crippling of food and fibre irrigators and the mitigating the 'death spiral' in regional areas. Ideally, the Regional Australia F&F CSO would be paid for by governments. Such an approach would shift what is currently an opaque subsidisation between regions and consumer classes to a transparent budget expense that could be reviewed annually by Parliament. Alternatively and less optimally, the Regional Australia F&F CSO could be transparently levied on electricity bills of non-regional Australian electricity consumers. Again, the total levy collected could be reviewed annually.

Cotton Australia recognises the Regional Australia F&F CSO is a cross-subsidy, however we are deeply concerned that electricity network price increases (of around 300% in the past five years) are diminishing profitability and jeopardizing the ongoing sustainability of irrigated food and fibre production in Australia (worth over \$13.5 billion per year).

Furthermore, investment and production decisions have been made by cotton producers (and other food and fibre irrigators) based on existing, albeit,



inefficient and inappropriate tariff structures. A significant change to the tariff structure and price of electricity without appropriate transition mechanisms (such as a Regional Australia F&F CSO) would undermine those business decisions.

Acknowledging that while there is limited scope for adjusting energy use patterns and the resultant low load profiles of most irrigators, Cotton Australia, in collaboration with NSW Irrigators' Council and the NSW Office of the Environment and Heritage has embarked on a program of on-farm energy audits. The purpose of the audits is to identify opportunities to improve electricity productivity in irrigation and initial estimates suggest savings of over \$1 million per year are achievable from the 11 pilot participants alone. We are seeking Government support for a wider ranging irrigation audit program through the Energy and Agricultural Competitiveness White Paper processes.

The irrigation energy audits will consider demand management with a view to improving the load variability, where possible. However, we note that as network revenues are set for a five year period consumers are may not realise any significant benefit from decreasing or modifying the pattern of energy consumption as networks will continue to recover the same revenue over the period. Cotton Australia considers that the Australian Energy Regulator's Efficiency Benefit Sharing Scheme should be reviewed to ensure that the benefits of consumers responding to efficient tariffs are shared and are not eroded by the networks revenue recovery process.

In summary, Cotton Australia recognises the value of cost-reflective and transparent tariff setting, where price signals encourage consumers to make informed decisions about their electricity use and any investments to manage that use. Nevertheless we ask that the AEMC consider the need for the principles of flexibility and fairness to be reflected in the draft network pricing rules to recognize that some consumers are constrained by factors outside their control. We also seek support for the Regional Australia F&F CSO.

We also ask the AEMC to work with the AER to:

- develop a develop a methodology or framework for networks to determine their long run marginal costs to promote transparency.
- ensure that consultation on the new tariff structures, including tariff setting statements (TSS) is meaningful, understandable and useful to all consumers

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- ensure that the benefits of consumers responding to efficient prices by modifying or decreasing energy consumption are shared and not eroded by the networks revenue recovery.

Thank you again for the opportunity to comment on the proposed rule change. Please do not hesitate to contact me on 07 4639 4908 or michaelm@cotton.org.au if you wish to discuss this submission in more detail.

Yours sincerely

Michael Murray
Policy Manager