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20 December 2012

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

Dear Mr Pierce,

RE: NEM financial market resilience, Options Paper (Reference EMO0024)

Ausgrid welcomes the opportunity to participate in the AEMC's review the financial resilience of the National Electricity Market NEM.

Ausgrid supports the AEMC's decision to focus its review on the effectiveness of current Retail of Last Resort (RoLR) arrangements. Ausgrid recognises that this is an important piece of work as the financial distress of a large retailer could have significant flow-on effects upon other energy market participants, which in turn could flow through to consumers.

If a large retailer in New South Wales (NSW) failed, we do not consider that current RoLR arrangements would be effective in mitigating the flow-on impacts to distribution network service providers (DNSPs). Perversely, the operation of current arrangements may act to exacerbate the risk of financial contagion to market participants and the risk of a cascading retailer failure.

Consequently, Ausgrid considers it appropriate that changes are made to current RoLR arrangements. It is fundamental that these arrangements are strengthened to ensure that they can effectively manage flow-on impacts to other market participants (regardless of whether the failed retailer is large or small) and that they mitigate the risk of cascading retailer failure.

Whilst Ausgrid supports the work being undertaken by the AEMC to address this issue, we have a number of concerns regarding how the AEMC considers this might be achieved. In particular, we are troubled by the:

- understatement of risk and potential consequences to DNSPs from a large retailer failing;
- failure to recognise the inadequacies of existing mechanisms to mitigate these risks; and
- proposed amendments to current arrangements which are aimed at transferring risks away from retailers to DNSPs.

Our submission seeks to highlight these issues by providing analysis on the magnitude of the risks faced by DNSPs from a large retailer under RoLR arrangements in NSW, the National Energy Customer Framework (NECF) and several of the options considered by the AEMC.

With experience obtained during the collapse of energy retail businesses EnergyOne and Jackgreen, Ausgrid has a keen interest in the AEMC's review, particularly any recommendations that the AEMC makes to strengthen the operation of current Retailer of Last Resort (RoLR) arrangements.

If you have any queries or wish to discuss this matter in further detail please contact Keith Yates on (02) 9269 4171.

Yours sincerely,

Joe Pizzinga
General Manager – Finance and Compliance

Submission on AEMC Options Paper – NEM financial market resilience

December 2012

Executive Summary

Ausgrid supports the primary focus of the AEMC's review, which is aimed at mitigating the flow-on impacts from a large retailer failure to other market participants and preventing cascading retailer failure.

Having experienced the collapse of both EnergyOne in 2007 and Jackgreen in 2009, Ausgrid has a keen interest in the AEMC's review, particularly any recommendations that the AEMC makes to strengthen the operation of current Retailer of Last Resort (RoLR) arrangements. Having been impacted by the only RoLR events to occur in the National Electricity Market (NEM), Ausgrid believes that it is well placed to provide the AEMC with its views on the effectiveness of current RoLR arrangements and the options considered to strengthen these arrangements.

Ausgrid has a number of concerns regarding the AEMC's Options Paper: *'NEM financial market resilience'* (Options Paper). In particular, we are concerned by:

- the understatement of risks and consequences to distribution network service providers (DNSPs) following the collapse of a large retailer under current RoLR arrangements; and
- the options discussed in the Options Paper which involves relaxing timelines or lessening requirements and obligations on designated RoLRs that will re-allocate or transfer the risk to other market participants.

Ausgrid is concerned that by understating the magnitude of the risks faced by DNSPs from a large retailer failure, the AEMC may have erroneously reached the conclusion that DNSPs are better placed to bear a greater portion of the risks arising from a large retailer failing than the designated RoLR. Our submission seeks to correct this misunderstanding, whilst also highlighting the operational and customer impacts of options discussed in the Options Paper.

Ausgrid is of the firm view that DNSPs should not assume commercial risks of retailers. In our view, this could have catastrophic affects upon both the NEM and customers, if RoLR arrangements placed DNSPs in a position where they were at risk of financial distress.

A more appropriate approach to strengthening current RoLR arrangements would be to embed a principled framework of risk mitigating strategies in regulation. This could include but is not limited to ensuring that the payment of network charges and provision of credit support are enforceable, that on-going financial assessment of retailers is conducted and that the ultimate cost to the consumer and other stakeholders including government is minimised.

Effectiveness of current RoLR arrangements

This section assesses the effectiveness of current RoLR provisions in mitigating flow-on impacts from a large retailer failure. In particular, this section seeks to:

- demonstrate the risks faced by NSW DNSPs under current arrangements;
- quantify the impacts from a large retailer failure and cascading retailer failure;
- outline potential cost recovery issues;
- draw attention to the customer impacts from a large retailer failing; and
- highlight enforceability issues regarding credit support obligations under the NECF.

Also discussed, are recommendations for strengthening current RoLR arrangements and events which could trigger a retailer failure.

Background

Ausgrid is one of three DNSPs operating in NSW. Ausgrid operates both a distribution and transmission network that supplies electricity to customers in Sydney, Central Coast and Hunter regions.

Currently, Network Use of System charges (NUoS) and service fees account for approximately 88% of Ausgrid's total revenue. There are 31 retailer licences in Ausgrid's distribution network area; however, revenue from these retailers is not spread evenly and is largely concentrated around three large energy retailers[1]. As a result, these retailers pose a significant credit risk[2] to Ausgrid and account for approximately $240 million per month of Ausgrid's billing or 82% of Ausgrid's total revenue.

NSW arrangements allow for weekly billing and 16 business day payment terms to mitigate credit risk from a retailer's failure to pay. Under the *Market Operations Rule (Network Use of Systems Agreements No. 2 of 2001)* ("MOR2") NSW DNSPs are also able to request credit support from retailers. However, a key short coming of this arrangement is that they operate according to a basic risk assessment framework whereby risks associated with small unrated retailers can be mitigated ('high' probability and 'low' impact of default), but those associated with large retailers with an external rating of BBB or higher ('low' probability and 'high' impact of default) cannot.

Risks to DNSPs under NSW RoLR arrangements in the event of a large retailer failure

Current arrangements in NSW have generally proven robust in managing the impacts from a small retailer failure; however, they were not designed to cater for the scenario of a large retailer, nor are they aimed at mitigating the occurrence of a cascading retailer failure. Consequently, NSW DNSPs have no protection if a large retailer failed and no means of mitigating their credit exposure. This is because DNSPs would not be able to draw upon credit support from the failed retailer[3] to minimise its shortfall in its revenue from the retailer's failure to pay network charges; nor would it be likely that a DNSP could recover their direct and indirect costs from the RoLR event.[4]

In addition, current arrangements are also likely to exacerbate the risk of a cascading retailer failure as there is only one designated RoLR[5] for each distribution area. If the failed retailer was any one of the three largest retailers in Ausgrid's distribution area it would be unlikely that any one retailer could absorb all the failed retailer's customers.[6] Therefore, there is an increased chance of the designated RoLR going into financial distress, which further compounds DNSPs' credit exposure.

Quantifying the impact to DNSPs

Scenario 1: large retailer failure

Direct costs

If one of the three largest retailers in Ausgrid's network area failed, the outstanding network charges to Ausgrid would range between $10 million to $35 million per billing week. By the time a RoLR event is declared, the failed retailer could have accrued several weeks of outstanding network charges. This would represent a significant short fall in revenue and will have a corresponding impact on cash flows. For instance, in the case of largest retailer one month of outstanding charges could equate to a shortfall of over $140 million.

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[1] Combined, these three energy retailers hold 12 out of the 31 retail licences in Ausgrid's network.

[2] DNSPs credit risk arises when they are unable to manage the risk of retailers defaulting on payment of network charges, given their obligation to supply distribution services. This means continuing accrual of debt to the DNSP.

[3] Under the *Market Operations Rule (Network Use of Systems Agreements No. 2 of 2001)* a large retailer would not be required to provide credit support, as these retailers typically have an external rating of BBB or higher.

[4] The retailer insolvency cost pass through event does not apply in non-NECF jurisdictions. See note under clause 2 of the National Electricity (National Energy Retail Law) Amendment Rule 2012. Also see cost recovery section.

[5] The Ministerial Determination in relation to Retailer of Last Resort of 19 December 2006, attached a RoLR endorsement to the retail supplier licences of Country Energy, EnergyAustralia and Integral Energy in accordance with s 33(a)(3) of the *Electricity Supply Act 1995 (NSW)*.

[6] For example, the largest retailer in Ausgrid's network holds approximately 1 million NMI's, with the other two having a combined NMI holding of 0.6million.

Indirect costs
In addition to the direct costs to DNSP's from unpaid network charges there are also indirect costs to DNSPs from a RoLR event.[7] From the Jackgreen RoLR event, which was only a relatively small retailer, Ausgrid incurred approximately $78,000 in indirect costs. In the event of a large retailer failure the indirect costs to DNSPs would be significantly higher and may place further strain on DNSP's cash-flows.

<u>Scenario 2: cascading retailer failure</u>

Under the scenario of a cascading retailer failure, the magnitude of Ausgrid's credit risk increases exponentially, particularly if the cascading retailer failure involved one of the three largest energy retailers in Ausgrid network. If the largest of retailers were to fail approximately 50% of Ausgrid's total regulated revenue would be exposed, if the second largest retailer were also to fail a combined 70% of total regulated revenue would be exposed and so on. Under such a scenario, Ausgrid would be left with significant debt and cash flow shortages.[8]

In an extreme case, the short-fall in revenue may place a DNSP in a position where its cash flows are insufficient to meet its obligations. If a DNSP were unable to borrow the necessary funds to cover its increased levels of debt it may go into default. The consequences of a DNSP defaulting would be catastrophic to the NEM and customers, as there are no contingencies in the event of a DNSP failure.

Cost recovery
The AEMC has indicated that a DNSP can recover unpaid network charges through a retail insolvency pass through,[9] however this is only the case in jurisdictions where the NECF has commenced.[10] Even if available, this remedy may be a slow one, due to the likely delays in a DNSP recovering these costs. Depending on when in the period a RoLR event occurs, a DNSP may have to absorb this cost (and the interest that accrues on this debt) for up to 11 months before it can undertake adjustment through its annual pricing proposal to recover the outstanding network charges

Ausgrid also notes that there is some uncertainty regarding whether indirect costs are recoverable under the "retailer insolvency" pass through event. We note that clause 6.6.1(l) refers to "retailer insolvency costs" in calculating the eligible pass through amount.[11] It is not clear under the National Electricity Rules (NER) what is meant by "retailer insolvency costs," particularly whether it encompasses both the unpaid network charges and indirect costs from a RoLR event. In the event that indirect costs fall outside this definition, it is not apparent how these costs would be captured by another pass through event. Consequently, DNSPs may be penalised from absorbing these costs under the Efficiency Benefit Sharing Scheme (EBSS).[12]

Customer impact
In both of the scenarios described above, the DNSP would need to borrow additional funds to meet its cash flow shortage. This in turn, will have a flow-on effect to customers, as borrowing additional funds would change the DNSP's debt to equity ratio and may impact on the DNSP's credit rating. If a DNSP's credit rating deteriorated due to the increase level of its debts, this could increase DNSP's cost of debt[13] and also increase the cost of raising equity from shareholders.[14] This additional cost would eventually be passed through to customers

[7] Indirect costs to DNSPs from a RoLR include: processing costs to update our records, produce estimated reads, re-direct service orders (where required) and produce final sets of charges for the failed retailer.
[8] The debt to Ausgrid would consist of the outstanding debts from the failed retailer and also the network charges equal to the failed retailer (now being accrued by the designated ROLR) in addition to the designated ROLR's usual network charges.
[9] Clause 6.6.1(4) of the National Electricity Rules (NER).
[10] The definition of "retailer insolvency event" and the amended definition of "pass through event" were made by the National Electricity (National Energy Retail Law) Amendment Rule 2012 made by the South Australian Minister for Resources and Energy on 27 June 2012. A note to clause 2 of that Rule states that the Rule does not apply in a participating jurisdiction until the National Energy Retail Law is in application as law of that jurisdiction.
[11] Clause 6.6.1(l) of the NER.
[12] Under the EBSS allowed increases or decreases in actual expenditure associated with recognised pass through events are excluded from the actual and forecast expenditure amounts used to calculate carryover gains or losses.
[13] This is due to the higher interest rate to borrow increased funds.
[14] A higher risk demands a higher required return premium.

through higher regulated network charges, which would be in addition to the costs that would be passed through to customers from a retailer insolvency event.

Consequently, another failing of current RoLR arrangements is the flow-on impacts to customers. Because current arrangements do not provide any means for DNSP's to mitigate their credit exposure from a large retailer failure, customers ultimately bear the risk of the retailer defaulting. If appropriate mechanisms were put in place to enable DNSPs to manage their credit exposure to large retailers, DNSP's would be able to minimise the impact to themselves and customers. This is because the DNSP would be able to recover a portion of the network charges outstanding (if not the whole amount) directly from the failed retailer, reducing the amount outstanding debt that would need to be recovered through customers.

Enforceability issues with credit support under the NECF

If NSW adopts the NECF credit support arrangements[15], NSW DNSPs will have the ability to mitigate substantially more of the credit risk relating to the failure of a large retailer. Based on the current share of Ausgrid's network customers between electricity retailers and retailer's current credit ratings, Ausgrid may be able to mitigate a portion of the credit risk associated with non-payment of network charges by the largest retailer operating in Ausgrid's network area. In this scenario, credit support over $100 million could be required from the retailer, but it is worth nothing that this is less than the average monthly network charge owed by that retailer. There is also uncertainty whether the mechanisms in place to enforce credit support obligations will be effective.

Ausgrid urges the AEMC to look at the effectiveness of current enforcement options as part of its current review. In particular, the AEMC should consider whether the conduct provisions and the RoLR provisions are properly integrated. Ausgrid is concerned that the remedies available to DNSPs to enforce requirements for credit support through the conduct provisions are likely to be frustrated due to the time required for court proceedings to resolve such issues.[16]

Recommendations

In our view, the most efficient way of mitigating the potential credit and cash flow impacts from a retailer failure, is through having credit support obligations which are able to be enforced. We note that in other markets prudent risk management would limit such exposure via credit limits, credit support/collateral, and shortened terms.

Events which can trigger retailer failure

Retailer failure can be caused by a wide range of factors such as funding constraints, inadequate capital, poor financial practices, insufficient hedge cover and exposure to high spot prices.

Each retailer has internal governance and risk management strategies for managing and monitoring market and credit risks. However the risk appetite of each retailer varies in scope and effectiveness and unexpected events like pricing volatility can result in a retailer defaulting on their hedge contracts and breaching its trading limits with AEMO.

Ausgrid considers that it would be a perverse outcome and a significant moral hazard if the retailer's risk appetite, hedging or management shortcomings are transferred to other market participants.

Specific comments on AEMC options

This section of the submission examines the effectiveness of the AEMC's options and seeks to highlight operational and customer impacts which may have been overlooked.

Ausgrid has not provided comments on every option discussed in the AEMC's Options Paper. Our comments are largely focused on the options regarding:

- cost recovery (option 5.1.);
- enhanced preparation (option 5.2);

[15] This is not currently proposed until the beginning of the next regulatory control period.

[16] Refer to Appendix 1: Enforcing credit support obligations

- delayed designation of RoLR (option 5.5),
- amendments to DNSP credit support obligations (option 6.2);
- delaying settlement of network charges (option 7.4); and
- government response (option 8)

Revised cost recovery arrangements

Our understanding of this option is that the AEMC is seeking to expand current RoLR arrangements in non-NECF jurisdictions so that they align with arrangements under the NECF. Ausgrid notes that the perceived benefit of this option is that it would provide the designated RoLR with greater certainty and may assist the RoLR in obtaining additional funds to cover its increased costs.

Ausgrid supports the principle for this proposed amendment. Clarifying the type of costs that can be recovered through RoLR cost recovery schemes and establishing clear timeframes would likely strengthen the efficiency of RoLR cost recovery schemes. The current discretion afforded to the AER to determine the amount recoverable under a distribution payment determination is significant[17] and may create uncertainty regarding whether a designated retailer is able to recover its efficient costs. Ausgrid notes the potential for this uncertainty to undermine confidence in the effectiveness of this cost recovery option.

Whilst Ausgrid supports the principle behind expanding and clarifying cost recovery arrangements, we have concerns regarding the operation of the distributor payment determination as a cost recovery mechanism. It is our understanding that the purpose of such a mechanism is to smear the costs incurred by the designated RoLR across customers in a jurisdiction rather than customers of the RoLR. If DNSPs are required to provide a lump sum upfront payment to the designated RoLR this could place a significant financial burden on DNSPs and may have adverse cash-flow implications, depending on the delay between when a DNSP is required to pay the designated RoLR and when it can recover these costs via the pass through mechanism.

A possible means of alleviating the financial burden to DNSPs caused by the distribution determination could be achieved by creating a mechanism that would allow a DNSP to adjust its prices before the next annual pricing proposal if that proposal was not due for more than six months.

Enhanced preparation

Ausgrid supports the AER's proposal to explore what plans and procedures could be put in place to appoint multiple designated RoLRs. Ausgrid considers that the risk of cascading retailer failure would be reduced by designating multiple RoLRs in certain circumstances, such as where the failed retailer had more than a certain number of customers (for example, greater than 100,000). This would help to mitigate the risk of a cascading retailer failure by reducing the likelihood of the designated RoLR experiencing a liquidity crisis and undergoing financial distress.

Ausgrid notes that the AER is obliged to take into account 'financial resources criterion' as part of a one-off entry test of an applicant retailer and as part of an overall assessment of a RoLR's suitability and capacity. Ausgrid proposes that this assessment of financial viability should be an ongoing assessment as part of the retailer licensing regime and cover the ability of the retailer to repay debt, access to ongoing funding, including the capacity of a ROLR to meet a DNSP's credit support requirements.

Amending RoLR triggers or delayed designation of RoLRs

Ausgrid agrees with the AEMC's assessment of potential benefits from delaying the designation of the RoLR. However, Ausgrid is concerned that there could be significant operational impacts and customer service implications if this delay were to exceed 7 days.

The potential disadvantages highlighted in the AEMC's Options Paper, in terms of impacts to AEMO and generators in delaying the RoLR event, will also impact DSNPs, as it represents a transfer of risk away from the designated RoLR and to the DNSPs.

Each day designation of the RoLR is delayed, introduces further complexities to DNSP's operations. These complexities range from servicing the customer, responding to retailers seeking to win the new site, meter data readings and billing.[18]

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[17] Refer to section 167 (8) of the *National Energy Retail Law (South Australia) Act 2011* ("NERL").

[18] In the case of the largest retailer in Ausgrid's distribution which holds just under one million NMIs, every day 11,000 meters would be read and be expecting to invoice NUoS. By working day 10 Ausgrid would have over

In addition, in deciding to delay the designation of the RoLR consideration would also need to be given to who would act as the customer interface during this interim period. Whilst DNSPs have an enduring relationship with the customer, they are not appropriate to act as a customer interface as they do not have the systems or capabilities to provide such a role.

Amendments to DNSP credit support provisions

The Options Paper proposes to waive or reduce the increased credit support requirements for a short transitionary period. As noted earlier in our submission, if a large ROLR event were to occur, Ausgrid would not hold nor would it be in a position to request credit support which would mean cash flow issues and financial distress.[19]

Under the NECF regime, NSW DNSPs will be able to request credit support from large retailers.[20] If the timeframes for which the designated RoLR is to provide increased credit support to DNSPs were to be relaxed, we consider that this period should only be relaxed for as long as it would reasonably take the designated RoLR to obtain suitable bank guarantees. Ausgrid further considers that this period should be capped as a maximum period in the NER to mitigate DNSPs credit exposure.

Delayed settlement period for designated RoLR to pay increased network charges

Ausgrid is concerned that extending the settlement period would adversely impact the DNSP's cash flow, revenue and provisioning, which would impact the DNSP's credit rating.

As noted previously in our submission, current NSW arrangements allow for weekly billing. Once NSW adopts the NECF, billing will change to monthly. An inherent short-coming of monthly billing is that it leaves DNSPs more exposed to late payments and non-payment by retailers. This is because DNSPs must continue to supply electricity regardless of whether the retailer has paid its network charges. Meaning a retailer can continue to operate in the NEM without paying its network charges until such time that:

- the retailer is unable to meets payments to generators and AEMO suspends it from operation; or
- the DNSP commences civil proceedings[21] or issues a statutory demand for payment.[22]

DNSP's do not typically have large cash flow contingencies. Once outstanding network charges start approaching $170 million, Ausgrid would have insufficient cash flows to meet its commitments and would need to borrow extra funds. In the event of the largest retailer in Ausgrid's network failing, Ausgrid would need to borrow funds once the retailer reached approximately five weeks in arrears.

As the failed retailer can continue operating for some time before being suspended, it is likely that the failed retailer could have accrued close to two months in outstanding network charges before a RoLR event is declared. If the largest retailer in Ausgrid's network area failed, the outstanding network charges could be of the order of $280 million. Given the delay existing delay that exists for DNSPs before a RoLR event is called, Ausgrid is concerned that introducing further delay will increase DNSPs credit exposure and further deteriorate its cash flows, requiring the DNSP to incur higher levels of debt.[23]

110,000 sites waiting to be billed if the RoLR is not assigned. This is based on a 91 day read cycle and the reading of those sites being evenly distributed throughout the 91 days.

[19] Under the *Market Operations Rule (Network Use of Systems Agreements No. 2 of 2001)* a large retailer would not be required to provide credit support, as these retailers typically have an external rating of BBB or higher.

[20] Given the dominance of one retailer in Ausgrid's distribution area, Ausgrid would be able to manage its credit risk by requesting credit support exceeding $100 million under the NECF regime. By holding appropriate levels of credit support, Ausgrid would be able to mitigate its largest risk exposure and reduce costs borne by customers in the event of a retailer default.

[21] Retailer's obligations to pay network charges under the NER are conduct provisions for the purposes of the National Electricity Law. This means that any person (including DNSPs) may institute civil proceedings for breaches of the conduct provisions and may seek to recover amounts for any loss or damaged suffered.

[22] Part 5.4, Division 2 of the *Corporations Act 2001* (Cth). Failure to comply with the statutory demand can form the basis for applying to the Court to have the company involuntarily wound up for insolvency.

[23] As noted earlier in our submission, as DNSP's take on higher levels of debt there will be flow-on impact to customers due to the increased cost of debt causing a higher weighted average cost of capital (WACC).

Whilst acknowledging that delaying payment of increased network settlement charges for a short period of time could assist in mitigating against a cascading retailer failure, we do not consider that this is an effective or efficient option given the significant risks faced by DNSPs.

Government response

Ausgrid strongly supports the proposed amendments to allow for a last resort government response, particularly option 8.3. Given the extremely low probability yet potentially catastrophic effects of a large retailer failure, further consideration of a last resort government response should be explored. As noted by the AEMC, the benefits of a government response, such as an energy supply company administration, would assist in mitigating both the flow-on impacts to other participants from a large retailer failing and also the risk of cascading retailer failure.

Conclusion

Ausgrid's submission has sought to demonstrate the magnitude of the credit risks and cash flow issues faced by DNSP's in the event of a large retailer failure. We have sought to highlight to the AEMC the inadequacies of current RoLR arrangements and have provided suggestions on how these arrangements could be strengthened.

Importantly, Ausgrid has sought to demonstrate the inappropriateness of transferring commercial risks away from retailers to DNSPs. We consider that this would be a perverse outcome and a significant moral hazard if the retailer's risk appetite, hedging or management shortcomings were transferred to other market participants.

Having examined the options discussed in the AEMC's Options Paper, Ausgrid considers that several of these options would be effective in mitigating flow-on impacts from a large retailer failure and the risk of a cascading retailer failure. These include:

- options aimed at clarifying RoLR cost recovery schemes;
- options aimed at enhancing preparation for RoLR events; and
- options aimed at creating a mechanism for a last resort government response.

Appendix 1: Enforcing credit support obligations

The limitations that a DNSP may face in enforcing compliance with credit support provisions will be influenced significantly by the basis for the retailer's failure to comply.

In circumstances where there has not been a RoLR event, the limitations faced by the DNSP include:

- a claim for loss or damage can only be made in circumstances where the DNSP has suffered actual loss or damage – the mere likelihood of loss or damage (e.g. future unpaid network charges) will not be sufficient to justify a claim for loss or damages;
- unless the DNSP has grounds to justify an urgent application, the Supreme Court processes from application to hearing and decision are likely to be lengthy such that seeking an order from the Supreme Court is not likely to result in immediate recovery for the DNSP.

In the event of a retailer failure, the key limitation on the DNSP's ability to take enforcement action for breaches of conduct provisions is the interrelationship between the conduct provisions and RoLR arrangements. These regulatory arrangements while interrelated are not integrated. At best, they enable the DNSP to exhaust all avenues for recovery of unpaid credit support. At worst, the exercise of one option may have the affect of precluding the DNSP from successfully adopting another course of action.

In addition, the dual recovery streams may not prove efficient as DNSP's will not be able to recover all its costs by one application in one forum. Instead, a DNSP may need to submit a cost pass through application to the AER for unpaid network charges and a separate application to the Court to recover any other costs incurred, while also awaiting the results of any insolvency proceedings.

Specifically:

- while the same factual information will be considered by a Court in determining a claim for recovery of actual loss or damages and the AER in determining a pass through application, the amount recoverable by a DNSP under each process may vary substantially given the different means used to calculate the amount recoverable;
- the DNSP can only make a claim for damages and losses for unpaid credit support in circumstances where the DNSP has actually suffered loss or damage;
- in relation to any court claim for damages or loss, the Court may be reluctant to award damages until a bankruptcy/insolvency proceedings in respect to the failed retailer have been finalised;
- any order for damage is likely to be limited by any amount that the DNSP will recover by way of a pass through application;
- the Court may defer consideration of a damages claim until the RoLR mechanisms under the National Energy Retail Law (NERL) have been exhausted.
- if the DNSP is able to recover some of its costs through the cost pass through mechanism it may no longer be worthwhile recovering the remaining amounts by way of a damages claim to the Court;
- where the retailer is in administration, any successful claim for damages will be affected by preference payments due to the retailer's other creditors;
- the ROLR arrangements provide for the DNSP to be given notice where the AER considers there is a risk of the RoLR event. The DNSP has confidentiality obligations in relation to this information and will not be able to rely on this information as a basis to take action for recovery by way of the conduct provisions. Conversely, the AER may withhold giving the DNSP such notice if the notice could lead to a RoLR event (e.g. by the DNSP taking court action); and
- any legal action that a DNSP takes could be superseded by a RoLR event (particularly since the DNSP is likely to be required to notify the AER of non-compliance with credit support obligations).