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Submissions
Electricity Authority
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ERGANZ SUBMISSION ON IMPROVING PRUDENTIAL SECURITY ARRANGEMENTS

The Electricity Retailers' and Generators' Association of New Zealand ('ERGANZ') welcomes the opportunity to provide feedback on the Electricity Authority's issues and options paper, 'Improving prudential security arrangements' from October 2025.

ERGANZ is the industry association representing companies that sell electricity to Kiwi households and businesses. Collectively, our members supply almost 90 per cent of New Zealand's electricity. We work for a competitive, fair, and sustainable electricity market that benefits consumers.

Executive summary

Overall, ERGANZ retailers support the Authority's proposals to improve prudential security arrangements for the New Zealand electricity system.

ERGANZ's members already deliver the overwhelming majority of prudential security and risk management under current settings. The Authority's proposals will shift even more responsibility onto the large participants. Despite this, ERGANZ supports policy options 1, 2 and 4.

However, ERGANZ does not support option 3 which reallocates a significant portion of residual funds to smaller retailers to reduce their prudential burden. The Authority frames this reallocation as supporting competition, but it arbitrarily shifts credit risk without any supporting principle or ability for larger retailers to more efficiently manage their risk.

Submission points

Option 1 – More frequent calibration of the adder (Support)

We support the Authority's proposal to move away from a single annual adder toward more frequent calibration. This approach better reflects conditions in the wholesale market, particularly seasonal or structural shifts in volatility.

A dynamic adder reduces the risk of over-collateralisation in benign periods while ensuring the clearing manager maintains sufficient coverage in high-risk states of the world. It enhances efficiency without compromising generator credit protection.

This is consistent with the Authority's long-standing principle that prudential settings should be risk-aligned and cost-reflective.

Option 2 – Shorter default exit period for small retailers (Support)

ERGANZ supports the limited, targeted reduction of the post-default exit period for retailers with 1,000 ICPs or fewer. This recognises that the consequences of default from a small retailer are more contained, and that reducing barriers to entry remains an important policy objective.

However, we emphasise two points. The justification must be based on objective risk and scale, not business model. ERGANZ is concerned by the suggestion in paragraphs 5.23–5.25 of the consultation paper, that a shorter exit period could be extended to independent retailers only, while excluding gentailers.

A business model has no intrinsic relationship to the risk of non-payment, speed of customer transfer, or the operational burden placed on the clearing manager. Discrimination between "independent retailers" and "generator-retailers" is therefore not objectively justifiable.

Consistency and predictability are central to any effective prudential regime. The regime should be neutral and not tilt risk allocation based on structural or political preferences. Any future modifications should be grounded in quantifiable prudential risk, not participant category.

Option 3 – Reallocation of residual funds (Do not support)

ERGANZ acknowledges the Authority's comments in the paper that residual funds arise from interest earned on retailers' payments and that, in principle, a case can be made for allocating these funds to purchasers rather than generators. We also note the current approach is justified because residuals compensate generators for ongoing credit risk and the possibility of default-related shortfalls. ERGANZ considers a good-faith argument can be made for either of these approaches.

However, we strongly oppose the proposal to carve out a portion of residual funds to allocate solely to independent retailers based on their chosen business model. This is not risk-based, nor proportional to exposures, nor supported by any principled rationale.

ERGANZ is concerned the proposal is a transfer from one set of participants to another, carving out a portion of funds solely for independents represents an arbitrary transfer from one business model to another. Market risk, prudential exposure, and credit-risk contribution are not correlated with business model.

The paper provides no objective justification and risks setting a regulatory precedent. Embedding business-model-based discrimination into the prudential regime sets a concerning precedent for future Code processes undertaken by the Authority.

In this example, the size of the funds at stake may not be significantly large, but the change undermines competitive neutrality and reduces the mechanism that covers shortfalls when defaults occur.

ERGANZ strongly recommends that residual funds should either continue to be allocated to generators, reflecting their exposure to default risk; or be allocated to all spot purchasers pro rata to purchase volumes, reflecting the fact that purchasers provide the funds from which residuals arise.

Option 4 – Allowing ASX futures to offset spot prudentials (Qualified support)

ERGANZ supports further work on this option. ASX-linked offsets may improve the alignment of prudentials with net risk exposure. However, careful design will be essential to avoid any correlation risk between spot stress and futures margin stress. In addition, the Authority should seek to avoid any timing mismatches between the clearing manager processes and ASX settlement cycles, as well as any risk of under-collateralisation if hedge effectiveness is over-estimated.

If designed conservatively, Option 4 could improve efficiency without materially increasing credit risk.

Consultation questions

Questions	Comments
Q1. Do you agree that the current risk profile of the prudential framework is appropriate? If not, why/how should risk be redistributed?	ERGANZ considers the current overall risk profile to be broadly appropriate. The existing prudential framework provides generators with adequate protection against retailer default, while imposing costs on retailers that are proportional to the risks they pose. We support refinements that improve efficiency without materially increasing credit risk. Any redistribution of risk should be grounded in objective measures of exposure rather than the chosen business model.
Q2. Do you agree that the issues identified by the Authority are worth addressing?	Yes. But in the context of large, complex change projects the Authority is already requiring from market participants, the priority for this set of proposals is low.

Q3. Are there other issues with the current prudential security settings that we have not identified but are worth addressing?	ERGANZ encourages the Authority to ensure that any changes preserve business-model neutrality. Where the consultation proposes different treatment for gentailers versus independent retailers, this raises fairness and precedent concerns. Differentiation should be based on risk or retailer size, not business model.
Q4. Do you consider that there are other adjustments that the Authority could make that would better reduce cost and enhance efficiency in prudential requirements for small retailers without significantly increasing credit risk for generators.	A more streamlined and automated switching process would help reduce exit-period length in a risk-controlled way. The Authority could also explore whether more frequent or real-time prudential updates (beyond the adder changes) would further align security with actual exposure.
Q5. Do you support the transition to a more dynamic adder? If not, what are your concerns?	Yes. A more dynamic adder would better align prudential requirements with market conditions, reducing over-procurement in stable periods while maintaining or increasing protection in high-risk periods. We encourage careful calibration and clear transparency around how changes will be triggered.
Q6. Do you support the proposal to allow reductions in the post-default exit period? Why/why not?	Yes. Shortening the exit period for small retailers (through removing unused tender steps and minor switching efficiencies) reduces prudential costs without materially increasing credit risk. A shorter exit period for small retailers is appropriate because the default of a small retailer carries lower system-wide impact.
Q7. Do you agree that the threshold for qualifying for a reduced post-default exit period should be 1,000 ICPs?	Yes, ERGANZ supports 1,000 ICPs as a pragmatic threshold. It targets small retailers for whom prudential costs can be a significant barrier to entry.
Q8. If broader changes to the trader default process make it feasible to reduce the post-default exit period for all independent retailers, should the Authority pursue this? Why/why not?	No, not on the basis of “independence” alone. There is no principled or risk-based justification for treating gentailers and independent retailers differently. If further reductions are feasible, they should apply based on retailer size or other objective criteria, not business model.

Q9. Do you agree with the proposal to reallocate residual funds to retailers on a scaled basis?	No. While a reasonable case can be made for allocating residual funds either to generators (current approach) or to all spot purchasers (because the funds originate from purchaser payments), ERGANZ does not support allocating a carved-out portion solely to "independent" retailers. This proposal represents an arbitrary transfer of value from one business model to another, is not grounded in credit-risk exposure, and sets a concerning regulatory precedent. Any reallocation must apply neutrally.
Q10. Is there an alternative model by which residual funds could be reallocated to retailers in a fair manner that still achieves the policy objectives?	Yes. ERGANZ recommends either retaining the current allocation to generators (which compensates for residual credit risk) or reallocating residual funds across all spot purchasers pro rata based on purchase volumes. Both options are principled and neutral. ERGANZ does not support any change that provides preferential treatment or discriminates based on business model.
Q11. Do you support a possible physical and futures offsetting arrangement? Why/why not?	ERGANZ supports further development of an offsetting arrangement, provided it is designed conservatively. Allowing ASX futures positions to offset prudentials can improve efficiency and better reflect net exposure. However, safeguards are needed to manage correlation risk, timing mismatches, and hedge effectiveness.
Q12. Are existing market-based work arounds to physical and futures offsetting arrangements sufficient for managing the issue?	Existing workarounds (such as adjusting hedge portfolios or using OTC products) are functional but imperfect.
Q13. If ASX futures positions could offset spot market prudential requirements, would you be more likely to trade in the futures market?	N/A

Conclusion

ERGANZ would like to thank the Authority for considering our submission.

If there are any outstanding questions or a need for further comments, please let me know.

Yours sincerely,

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