

SETTLEMENT AGREEMENT

(Regulation 83(1) Electricity Governance Regulations 2003)

DATED:

BETWEEN:

- (1) **Carter Holt Harvey Limited**, of State Highway 1, Tokoroa (**CHH**)
- (2) **Transpower New Zealand Limited**, of Level 7, 96 The Terrace, Wellington, in its capacity as System Operator (the **System Operator**);
- (3) **TrustPower Limited**, of Truman Road, Te Maunga, Mt Maunganui, (**TrustPower**);
- (4) **Meridian Energy Limited**, of 33 Customhouse Quay, Wellington, (**Meridian**)

collectively the **parties**.

BACKGROUND:

- (A) On 30 August 2007 the System Operator alleged that CHH had breached rule 4.11 of section III of part G of the Electricity Governance Rules 2003 (Rules) by failing to comply with dispatch instructions for Kinleith for trading period 2 on 4 July 2007 (the Alleged Breach).
- (B) In accordance with regulation 69 of the Regulations, the Board of the Electricity Commission (**Board**) appointed an investigator to investigate the Alleged Breach.
- (C) The System Operator, TrustPower and Meridian joined the investigation as interested participants.
- (D) The parties have agreed to settle the Alleged Breach on the terms contained in this Agreement.

IT IS AGREED:

1. Interpretation

1.1 In this Agreement, unless the context requires otherwise:

- (a) **Agreement** means this Settlement Agreement;
- (b) **Approval Date** means the date the Board approves this Agreement under regulation 84(2) of the Regulations;

- (c) **Alleged Breach** means the alleged breach of the Rules arising from the Circumstances and set out in clause 2.2;
- (d) **Circumstances** means the circumstances set out in clause 2.1;
- (e) **Regulations** means the Electricity Governance Regulations 2003;
- (f) **Rules** means the Electricity Governance Rules 2003;
- (g) all capitalised terms not defined in this Agreement have the same meanings as in the Regulations or Rules, as the case may be; and
- (h) all references to clauses are to clauses of this Agreement.

2. Circumstances and Alleged Breach

2.1 The parties agree on the following circumstances of the Alleged Breach:

- (a) On 3 July 2007 the Kinleith mill was in a significant scheduled maintenance shut down of No.1 Fibreline. This included PM6, No.1 Batch Mill, No.5 Recovery Boiler, No.8 Primary Boiler, and the steam turbine. During the day, one of the plants suffered a significant failure leading to the shutdown of practically the entire mill. No.1 Fibreline began start up throughout the afternoon. As a result the steam demand increased throughout this time until No.8 Primary Boiler was online and controlling the header pressure just after 23:00. CHH was then able to attempt to bring the turbine back online – it began a cold run-up of the turbine at 23:34. During that time most of the plant was running with the exception of No.1 Batch Mill. However, the operational plant was either still ramping up or just reaching stability.
- (b) Once Turbine run-up started, TrustPower was notified at 23:35. The run-up proceeded smoothly and the turbine synchronised at 00:14 but the automatic loading of the turbine took longer than normal to run up.
- (c) Normally the Kinleith turbine, starting up after a trip, will load up to between 10 and 20 MW over a short period of time (depending on site steam demand since the generator output is directly coupled to mill steam demand). More steam users can then be brought online and the offer can be revised appropriately as steam demand increases. This was the status at 23:35 when the initial offer on the turbine was put in. It was done when run-up of the turbine was to begin, with the sole purpose to give as much advance information as possible to TrustPower and the System Operator. Such an approach reduces the likelihood of situations where CHH begins generating significant quantities of power prior to being dispatched. CHH believes it was a reasonable estimate of the steam demand given the uncertainty around the major start up of a complicated integrated mill.
- (d) However, once the turbine started loading, significantly more steam production was coming online than planned when the original offer was made. The turbine reached 11.5 MW by 00:30, and at this stage CHH realised that with the steam usage continuing to ramp up, generation was also going to continue to ramp up.

- (e) After re-evaluating the generation profile with current and expected future steam demand CHH attempted to contact TrustPower sometime between 00:35-00:37. The generation exceeded the ± 5 MW band of dispatch by 00:36. However, CHH was unable to get through to TrustPower as the line was busy. TrustPower called CHH at 00:40 after apparently having been called by the System Operator. CHH updated the TrustPower trader about the current situation and advised a bona fide change in generation to 22 MW. At 00:40, TrustPower submitted revised offers to the System Operator, for 22 MW, for trading periods 3 to 6 on 4 July 2007. Shortly after, TrustPower called the System Operator to advise that revised offers had been submitted and that Kinleith would generate 22 MW for the remainder of trading period 2. This was 12 MW above the dispatched quantity of 10 MW.
- (f) Due to the nature of its industrial plant and the non-condensing turbine, CHH cannot quickly shed steam demand.
- 2.2 On 30 August 2007 the System Operator alleged that CHH had breached rule 4.11 of section III of part G of the Rules. In this case CHH failed to comply with dispatch instructions for Kinleith for trading period 2 on 4 July 2007.
- 2.3 The parties also agree that the Rules do not permit offer revisions within a trading period. Situations can arise where a fault or process interruption results in CHH generation being revised downwards (including to zero) for bona fide reasons but which is then resolved sooner than could have been reasonably foreseen. In such cases the Rules do not allow CHH to submit a revised offer that takes effect prior to the following trading period. Without a revised offer in place for the remainder of the trading period, CHH cannot be dispatched back to where they were prior to the fault or process interruption occurring. After the fault or process interruption is located and resolved, the generator ramps up according to recovering plant steam demand. The profile of the recovering plant steam demand is often difficult to predict accurately (non-linear and asymmetric). Consequently, compliance with the existing dispatch instruction after the fault is resolved (before the next trading period commences) would delay testing and restoration of the generator or delay the resumption of the downstream steam demand. This would continue and exacerbate the disruption to the tightly coupled co-located factory process and require either part of the site or the entire site to remain out of service for the remainder of the trading period. The parties acknowledge CHH's concerns that this situation (created by the Rules) is financially and operationally undesirable.
- 2.4 The parties agree there should be a review of the Rules to establish if the Rules should be changed to facilitate the offer and dispatch of a generator in the situation described in paragraph 2.3. The most appropriate means of undertaking the review is through the Electricity Commission rule change process so as to ensure appropriate industry consultation occurs.

3. Guiding Principle

The parties agree the following guiding principle in relation to this Agreement: that any actions the parties may be required to undertake in order to achieve a settlement should

not require the parties to invest in significant additional resources to comply with the Agreement.

4. Settlement

The parties agree to the following settlement terms:

- 4.1 CHH will seek an Electricity Commission-led review of the rules, as described below:
 - 4.1.1 It is agreed that CHH will seek an Electricity Commission-led review of the relevant rules by proposing rule changes to the Commission. Such a proposal is to be lodged within 2 months of this settlement being approved, to address the issue of offer revisions within a trading period. The proposal will describe the reasons why a review of the relevant rules is being sought and describe rule changes (at a conceptual level) to address those issues.
 - 4.1.2 TrustPower and the System Operator will, if requested, assist CHH with the preparation of the rule change proposal. In any event, CHH will consult with TrustPower and the System Operator to ensure the proposal takes account of their respective operational requirements.
- 4.2 Within 3 months of the date of approval of this settlement, CHH and TrustPower will review whether their offer practices facilitate compliance with dispatch within +/-5MW as far as possible. As requested by the System Operator, this review is to focus on past examples of when generation has increased to levels well above dispatch and whether the offer could have been set differently to allow for this possibility. The System Operator will provide assistance with this review. For the 6 months after the review is completed, CHH and TrustPower will monitor the effectiveness of any changes made to offer practices as a result of the review, and implement any further identified improvements having first notified the System Operator of any improvements to be implemented.
- 4.3 CHH will use the offer revision processes set out in rules 3.15 and 3.17 of section II of part G of the Rules when dispatch instructions are not able to be met. The parties note their acknowledgement that even if CHH has used the offer revision processes set out in these rules, generation outside +/-5MW of the dispatched quantity is prima facie a potential breach of rule 4.11 of section III of part G. CHH is to investigate such incidents and self-report a breach as soon as possible, and within 20 business days, where there are reasonable grounds to conclude a breach has occurred.
- 4.4 CHH will inform the System Operator as soon as it becomes aware of conditions that are likely to affect its ability to meet dispatch instructions, particularly where such conditions are likely to result in generation that is higher than the quantity offered.
- 4.5 Within 3 months of the date the Commission approves the settlement, CHH and TrustPower will review the communications protocols both between themselves

and with the System Operator. The objective of the review is the minimisation of delays in communication and ensuring revisions to offers are made in a timely manner. The System Operator will provide assistance with the review.

5. Agreement Subject to Approval

5.1 This Agreement takes effect on the date it is approved by the Board under regulation 84(2) of the Regulations.

6. Settled Breaches

6.1 Subject to the approval of the Commission under regulation 84(2)(a):

(a) The terms of this Agreement are a full and final settlement between the parties to this Agreement of all claims and liabilities under the Regulations and Rules of:

- (i) the Alleged Breach; and
- (ii) any other breaches of the Regulations and Rules, involved in or arising from the Circumstances

(together the "Settled Breach")

(b) In accordance with regulation 84, but subject to regulation 87, this Agreement is also binding on the Electricity Commission and all other Participants to the effect that:

- (i) the Electricity Commission may not on its own initiative instigate a further rule breach investigation, or take any enforcement action, in respect of the Settled Breach; but
- (ii) a Participant who is not a party to this Agreement may, in accordance with regulation 87, make a further notification under regulation 62 or 63 in relation to a Settled Breach and the Electricity Commission may then take all or any of the steps provided for by Part 4 of the Electricity Governance Regulations notwithstanding this Agreement.

7. General

7.1 Each party will execute all documents and do, or refrain from doing, all other things necessary or desirable to give full effect to the provisions of this Agreement, including to secure the Board's approval of this Agreement under regulation 84(2) of the Regulations.

EXECUTED AS AN AGREEMENT:

For **Carter Holt Harvey Limited** by:

Name:
Position:

For **Transpower New Zealand Limited** by:

Name:
Position:

For **TrustPower Limited** by:

Name:
Position:

For **Meridian Energy Limited** by:

Name:
Position: