

SETTLEMENT AGREEMENT

(Regulation 24(1) Electricity Industry (Enforcement) Regulations 2010)

DATED:

BETWEEN:

- (1) Winstone Pulp International Limited of State Highway 49, Ohakune (WPI); and
- (2) Transpower New Zealand Limited as System Operator of 96 The Terrace, Wellington (System Operator); and
- (3) Meridian Energy Limited of 33 Customhouse Quay, Wellington (Meridian).

(Collectively the **parties**).

BACKGROUND:

- (A) On 21 January 2011, WPI self-reported to the Authority that on 11 January 2011 it had breached clauses 13.18(1)(a) and 13.46(3)(a) of the Code.
- (B) In accordance with regulation 12 of the Regulations, the Authority appointed an Investigator to investigate the Alleged Breaches
- (C) The System Operator and Meridian joined the investigation as affected participants.
- (D) The parties have agreed to settle the Alleged Breaches 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) **Alleged Breaches** means the alleged breaches of the Code arising from the Circumstances and described in clause 2;
- (c) **Approval Date** means the date the parties to this Agreement are notified that the Board of the Electricity Authority has approved this Agreement under regulation 24(4) of the Regulations;
- (d) **Board** means the Board of the Electricity Authority;
- (e) **Circumstances** means the circumstances set out in clause 3;
- (f) **Regulations** means the Electricity Industry (Enforcement) Regulations 2010;

- (g) **Code** means the Electricity Industry Participation Code 2010;
- (h) all capitalised terms not defined in this Agreement have the same meanings as in the Regulations or Code, as the case may be; and
- (i) all references to clauses are to clauses of this Agreement.

2. Alleged Breaches

2.1 Clause 13.18(1)(a) provides:

13.18 When revised bids or offers must be submitted

- (1) Before the beginning of the **trading period** to which the **bid** or **offer** applies, despite subclause (2) and clause 13.19, a **purchaser** or a **generator** (other than an **intermittent generator** submitting an **offer** under clause 13.17) must immediately submit revised **bid** or **offer** quantities to the **system operator** if—
 - (a) the ability of a **purchaser** to purchase the quantity bid for a **trading period** at a **grid exit point** is expected by that **purchaser** to change by more than 20 **MW** or 10% of the quantity bid by that **purchaser** (whichever is smaller); or ...

2.2 WPI breached clause 13.18(1)(a) by failing to immediately submit a revised bids for energy purchases when the ability to purchase the quantity bid changed by more than 10%. This clause was breached just prior to the commencement of the scheduled outage and again when the outage continued beyond the original scheduled outage period.

2.3 Clause 13.46(3)(a) provides:

13.46 Reserve offers may be revised or cancelled

...

- (3) Before the beginning of the **trading period** to which the **reserve offer** applies, and despite subclause (4) and clauses 13.47 and 13.97 to 13.101, an **ancillary service agent** must immediately submit revised **reserve offer** quantities to the **system operator** if—
 - (a) the quantities specified in the **reserve offer** no longer represent a reasonable estimate of the quantity of **instantaneous reserve** available from the **ancillary service agent** at the **grid injection point, grid exit point** or **interruptible load group GXP**; or

2.4 WPI breached clause 13.46(3)(a) by failing to immediately submit to the System Operator, revised offers for interruptible load instantaneous reserves (IL) when the offer no longer represented a reasonable estimate of the quantity of IL available. This clause was breached when the outage continued beyond the original scheduled outage period.

3. Circumstances of the Breaches

- 3.1 WPI bids for electricity for the total usage at its Karioi pulp mill and offers IL from its pulp refiners.
- 3.2 WPI prepares in advance the next week's production schedule including bids and offers for each 8 hour production shift. The schedule notes offers to apply for planned maintenance within a production shift. The schedule is sent to WPI's trading agent who submits the bids and offers into the information system.
- 3.3 WPI has an automated alarm system to identify when the refiner load is insufficient to provide the offered IL. The alarm can only be preset to one level for each production shift. Production shifts are from 06:00-14:00, 14:00-22:00 and 22:00-06:00. The alarm is reset as required during production shifts to match changes to IL offers.
- 3.4 On 11 January 2011 from 06:30 to 12:00, a plate change was scheduled for one of the refiners for which WPI submitted reduced offers for the outage. WPI did not submit revised bids for the outage. For the entire production shift from 06:00 to 14:00 on 11 January 2011, WPI had preset the alarm to the level of IL available during the scheduled outage.
- 3.5 The refiner plate change commenced from 06:30 and coincided with the scheduled reduction in reserve offers. At 12:00, WPI's offers reverted to the level available from full refiner load, however, the actual refiner load was still at the level of the outage. The alarm remained set at the level of the refiner outage, therefore the alarm did not activate to indicate load was below the offered level. WPI mistakenly took the outage level as the scheduled offer and therefore did not inform its trading agent of the required change to its offer.
- 3.6 At 14:00, the commencement of the next shift, WPI's alarm was activated to show that WPI was below the level required to meet its scheduled IL offers. The WPI operator acknowledged the alarm and reduced the offered values on the WPI control screen to what the operator thought the IL offers were. The change was made by the WPI operator without communication with WPI's trading agent. This was because the WPI operator at the shift change at 14:00 had mistakenly interpreted comments on the WPI control screen that WPI's trading agent was already aware of the lower bids and offers that applied from 14:00.
- 3.7 At 17:45, WPI's load increased and WPI advised its trading agent to increase WPI's bids and offers. At this point WPI was informed by its trading agent that it should have already been at the level of the revised bids and reserve offers. This is when WPI became aware of the breaches.
- 3.8 From 0630 hours to 1800 hours revised bids should have been submitted by WPI as the bids for this period were on average 14.5MW (+37%) greater than its actual load. WPI attributes the failure to update bids for the period 0630 to 1200 hours to a

misunderstanding between WPI and its trading agent on the process for updating bids for planned outages. WPI attributes the failure to update bids for the period 1200 to 1800 hours due to human error by its operator's.

- 3.9 From 1200 hours to 1800 hours and WPI's fast IL and sustained IL offers were respectively 4.9MW (+43%) and 13.5MW (+55%) greater than its actual capability to provide. Revised offers should have been submitted for the period 12:00 to 18:00. WPI attributes the failure to revise its offers to human error by its operator's.

4. Impact of the Breaches

- 4.1 The parties agreed that the actual market impact as assessed by the Investigator should be recorded as negligible.
- 4.2 The impact of not revising bids is that the System Operator used inaccurate demand information in its schedules. The amount in this instance would have caused negligible market impact.
- 4.3 The market impact of not revising IR offers was that WPI was dispatched and paid \$616 for instantaneous reserves that it would not have been able to provide had an under frequency event occurred.
- 4.4 The security impact was potentially serious on the power system had an under frequency event occurred. In the worst case scenario the System Operator may have been forced to rely on automatic under-frequency load shedding to arrest the fall in frequency.

5. Steps taken to prevent recurrence

- 5.1 WPI has reviewed its processes and produced an updated procedure for planned maintenance concerning bids and offers.
- 5.2 WPI operators have been trained on the process and Code requirements.
- 5.3 WPI operators will now only change the alarm levels after communicating the change with its trading agent, this applies to planned maintenance, changes prior to two hours of the relevant trading period and for bona fide revisions.
- 5.4 WPI will be discussing with its trading agent the demand bidding process for scheduled maintenance.

6. Settlement

- 6.1 The parties agree that:
- (a) WPI acknowledges the potentially significant implications on the security of the power system from a failure to ensure offers for reserves are reasonable estimates of the quantity of reserve available; and has invited the System

Operator to visit in October 2011 to discuss the wider security implications of instantaneous reserves and processes with WPI personnel; and

- (b) WPI acknowledges that its process for planned maintenance interruptible load management involves a number of manual steps that increase the risk of human error incidents occurring. To mitigate this risk WPI will:
- ensure it operators are trained on an ongoing basis on the process and the implications of failing to follow the process; and
 - self review its process performance for planned maintenance outages; and
 - will discuss with its trading agent the demand bidding process for scheduled maintenance.

7. Confidentiality

7.1 If the Board decides under regulation 25(2) of the Regulations not to publicise any part of this Agreement, each party will treat that part of the Agreement as confidential information and will not disclose it other than:

- (a) to the party's employees or contractors who need to know the confidential information to implement or monitor the implementation of this Agreement;
- (b) to the party's professional advisers, auditors and bankers;
- (c) as required by law or for the purposes of judicial proceedings;
- (d) as required by any securities exchange or regulatory or governmental body to which the party is subject or submits; or
- (e) as authorised in writing by the other parties.

7.2 A party must not disclose confidential information under clause 7.1(a) or (b) unless the party obtains a confidentiality undertaking from the person to whom the confidential information is to be disclosed on terms no less onerous than those set out in this clause 7 before disclosing the confidential information. Any confidential information to be disclosed in the circumstances set out in clause 7.1(c) or (d) may only be disclosed after written notice to the other parties (unless the disclosing party is prevented from notifying the other parties by law).

8. Agreement Subject to Approval

8.1 Subject to clause 8.2, this Agreement will come into effect on the Approval Date.

8.2 Clause 7 is binding on the parties as from the date of this Agreement. Pending the Board's approval of this Agreement under regulation 24(4) of the Regulations, clause 7 will apply as if the Board has decided under regulation 25(2) of the Regulations not to publicise any part of this Agreement or the existence of this Agreement.

9. Settled Breaches

9.1 This Agreement is in full and final settlement of all claims, actions and demands against any party (under the Regulations, the Code or otherwise) in relation to:

- (a) the Alleged Breaches; and
- (b) any other breaches of the Regulations or Code involved in or arising from the Circumstances that the claiming party ought reasonably to have known about at the date of this Agreement,

(the Alleged Breaches and such other breaches together the **Settled Breaches**).

9.2 Pursuant to regulation 24, but subject to regulation 26 of the Regulations, this Agreement is also binding on the Board and all Participants who are not a party to this Agreement to the effect that:

- (a) the Board may not on its own initiative instigate a further breach investigation, or take any enforcement action in respect of, the Settled Breaches; and
- (b) a Participant who is not a party to this Agreement may, subject to and in accordance with regulation 26 of the Regulations, make a further notification under regulation 7 or 8 of the Regulations in relation to a Settled Breach, and the Board may then take all or any of the steps provided for in the Regulations despite this Agreement.

10. General

10.1 Each party will execute all documents and do, or refrain from doing, all other reasonable 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 24(4)(a) of the Regulations.

10.2 This Agreement is the whole and only agreement between the parties relating to the settlement of claims, actions and demands arising from the Circumstances. Each party acknowledges that it has not been induced to enter into this Agreement by any representation made by or on behalf of the other party that is not repeated in this Agreement.

10.3 This Agreement may be signed in any number of counterparts.

SIGNED:

For Winstone Pulp International Limited

Name:

Position:

SIGNED:

For Transpower New Zealand Limited

Name:

Position:

SIGNED:

For Meridian Energy Limited

Name:

Position: