

1. Terms of settlement dated the                      day of                      2004 between

“the parties”:

- a. Transpower NZ Limited as System Operator;
- b. Norske Skog Tasman Limited;
- c. Genesis Power Limited;
- d. Vector Limited;
- e. Todd Energy Limited;
- f. TrustPower Limited;
- g. NZ Steel Limited;
- h. Mighty River Power Limited;
- i. Contact Energy Limited; and
- j. Winstone Pulp NZ Limited.

2. In the matter of:

Two alleged breaches of the Electricity Governance Regulations (2003) and Rules (the EGRs) by the System Operator on 10 & 11 March and 29 June 2004, of Rule 5.1.5 Part C Schedule C3, with respect to the reduction of instantaneous reserves requirements to zero in certain trading periods on those dates.

3. The guiding principles of this settlement are agreed between the parties as follows:

- a. The EGRs should facilitate the dispatch of instantaneous reserves when there is a shortfall of energy and instantaneous reserves to cover the largest contingent event, with the purpose of reducing the likelihood and extent of demand shedding, as a consequence of an event less than the largest contingent event; and
- b. The EGRs should provide appropriate pricing signals consistent with a shortfall of energy and instantaneous reserves to cover a contingent event in RTP.

4. It is accepted by all parties to this agreement that:

- a. This informal resolution (settlement) is entered into by all parties pursuant to Regulation 82 of the EGRs.
- b. This settlement does not constitute acknowledgement by any of the parties that the actions of the System Operator do or do not constitute breaches of the rules as alleged.
- c. Norske Skog Tasman Limited shall, as soon as practicable after approval of this settlement by the Electricity Commission, advise the Electricity Commission that it wishes the allegations of breach of the EGRs referred to in paragraph 2 of this agreement to be withdrawn.
- d. The automated partial or non-zero dispatch of instantaneous reserves, when there is a shortfall of energy and instantaneous reserves following a contingent event, is not a feature of the interface software between the Scheduling Pricing and Dispatch software (SPD) and the Reserves Management Tool (RMT).

- e. Dispatch of zero instantaneous reserves in such circumstances is currently achieved by manually reducing the Reserves Adjustment Factor (RAF) to zero in SPD, thereby allowing dispatch of energy, while relying on Automatic Under Frequency Load Shedding (AUFLS), free governor response and HVDC modulation in the event of a second contingent event.
  - f. The same action is taken when there is a shortfall of energy and instantaneous reserves in steady state.
  - g. Where the instantaneous reserve requirement is reduced to zero at the beginning of a trading period, but increased to the full requirement during a trading period, reserves are dispatched during that period but final prices will be based on initial conditions, resulting in a zero price. This means that reserve providers will not be paid for reserves delivered within part of a trading period.
  - h. Dispatch of partial or non-zero dispatch of instantaneous reserves in such circumstances could reduce the likelihood and extent of demand shedding, as a consequence for a subsequent event, being an event less than the largest contingent event.
  - i. Such partial or non-zero dispatch of instantaneous reserves could, enhance the consistency of pricing signals both in RTP and final prices.
  - j. Ideal partial or non-zero dispatch of instantaneous reserves with existing software appears to require both software and rule changes so that the process is transparent and provides all parties with greater certainty about pricing outcomes.
  - k. To achieve broad acceptance, any such changes require industry consultation and involvement and Electricity Commission oversight. The rule change process, under the auspices of the Commission's Advisory Group process, seems most appropriate to deliver this consultation and oversight.
5. Accordingly, and subject to paragraph 6 of this agreement only in so far as it might additionally produce an alternative suggested means acceptable to the System Operator to achieving the object as set out in paragraph 3 of this agreement, it is agreed that the System Operator propose rule changes to the Electricity Commission within 40 working days of this settlement being signed (a copy of which shall at the same time be distributed to the parties to this agreement), seeking an Advisory Group-led review of the rules pertaining to the dispatch and pricing of instantaneous reserves during grid emergencies, based on the following principles and those in paragraph 3 of this agreement:
- a. That the System Operator's ability to meet its PPOs is not compromised:
  - b. The EGRs should facilitate the dispatch of instantaneous reserves when there is a shortfall of energy and instantaneous reserves to cover the largest contingent event, with the purpose of reducing the likelihood and extent of demand shedding, as a consequence of an event less than the largest contingent event:
  - c. The EGRs should provide transparency and greater certainty to the market as to how instantaneous reserves dispatch will occur in such circumstances:

- d. Final reserve prices will reflect the dispatch of a variable reserve requirement within a single trading period:
- e. The market members should pay for the level of security it receives.
- 6. In preparing its rule change proposal to the Electricity Commission (referred in paragraph 5 of this agreement) the System Operator will also investigate, consider, and respond (including with reasoning) to the suggestions proposed by Norske Skog Tasman Limited in Mr Graeme Everett's letter to the Electricity Commission dated 16 April 2004. The System Operator will consider whether it is appropriate and able to implement the mechanisms suggested by Mr Everett on an interim or permanent basis, either in lieu of or in conjunction with the proposed rule change. The System Operator's response will be provided to the Electricity Commission in the System Operator's rule change proposal. The parties note that any mechanisms adopted under this paragraph are to be transparent to Market Participants.
- 7. The parties urge the Electricity Commission to accept this settlement and to endorse it further by recommending that the process for reviewing the rule change proposal, so far as it is able, be accorded the highest priority.
- 8. The parties to this agreement acknowledge the execution of this agreement constitutes full and final settlement between all the parties in respect of the alleged breaches of the EGRs set out in paragraph 2 of this agreement and all matters giving rise to the alleged breaches.
- 9. This Agreement may be signed in any number of counterparts all of which, when taken together, will constitute one and the same instrument. Any of the parties may enter into this Agreement by executing any counterparts.
- 10. The settlement recorded in this Agreement will take effect on the date on which it is approved by the Electricity Commission under Regulation 84 of the EGRs.

Signed as an agreement.

Signed by and on behalf of  
**TRANSPower NEW ZEALAND  
LIMITED**

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Signed by and on behalf of  
**NORSKE SKOG TASMAN  
LIMITED**

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Signed by and on behalf of  
**GENESIS POWER LIMITED**

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Signed by and on behalf of  
**VECTOR LIMITED**

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Signed by and on behalf of **TODD  
ENERGY LIMITED**

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Signed by and on behalf of  
**TRUSTPOWER LIMITED**

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Signed by and on behalf of **NZ  
STEEL LIMITED**

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Signed by and on behalf of **MIGHTY  
RIVER POWER LIMITED**

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Signed by and on behalf of  
**CONTACT ENERGY LIMITED**

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Signed by and on behalf of  
**WINSTONE PULP NZ LIMITED**

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