Unification:
beyond the residual

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Introductory Notes

1. The model described in this presentation does not necessarily represent the view or position of any particular person or company. It is an idea or concept for the ICD group to consider as a possible solution.

2. The model's design is premised on the following assumptions/observations:

    - There will be costs associated with balancing intraday, daily and seasonal demand
    - The cost allocation mechanism ultimately adopted by users will allocate these costs to the causers of imbalance
    - The causers will be users (i.e., Shippers, Welded Parties and pipeline operations)
    - The causers of imbalance (i.e., users) would prefer to have control over the design and management of the system that a) controls and manages primary balancing and transportation and b) incurs and allocates (residual) balancing costs
    - It will need to build on existing systems, operators and contractual terms in a transparent, simple and coherent way
    - Like all other solutions, it will require some form of change to contracts and probably the establishment of a new entity
    - Like all other solutions (other than perhaps a regulatory solution), it will require the agreement of the TSOs before it can be adopted and implemented

Scope

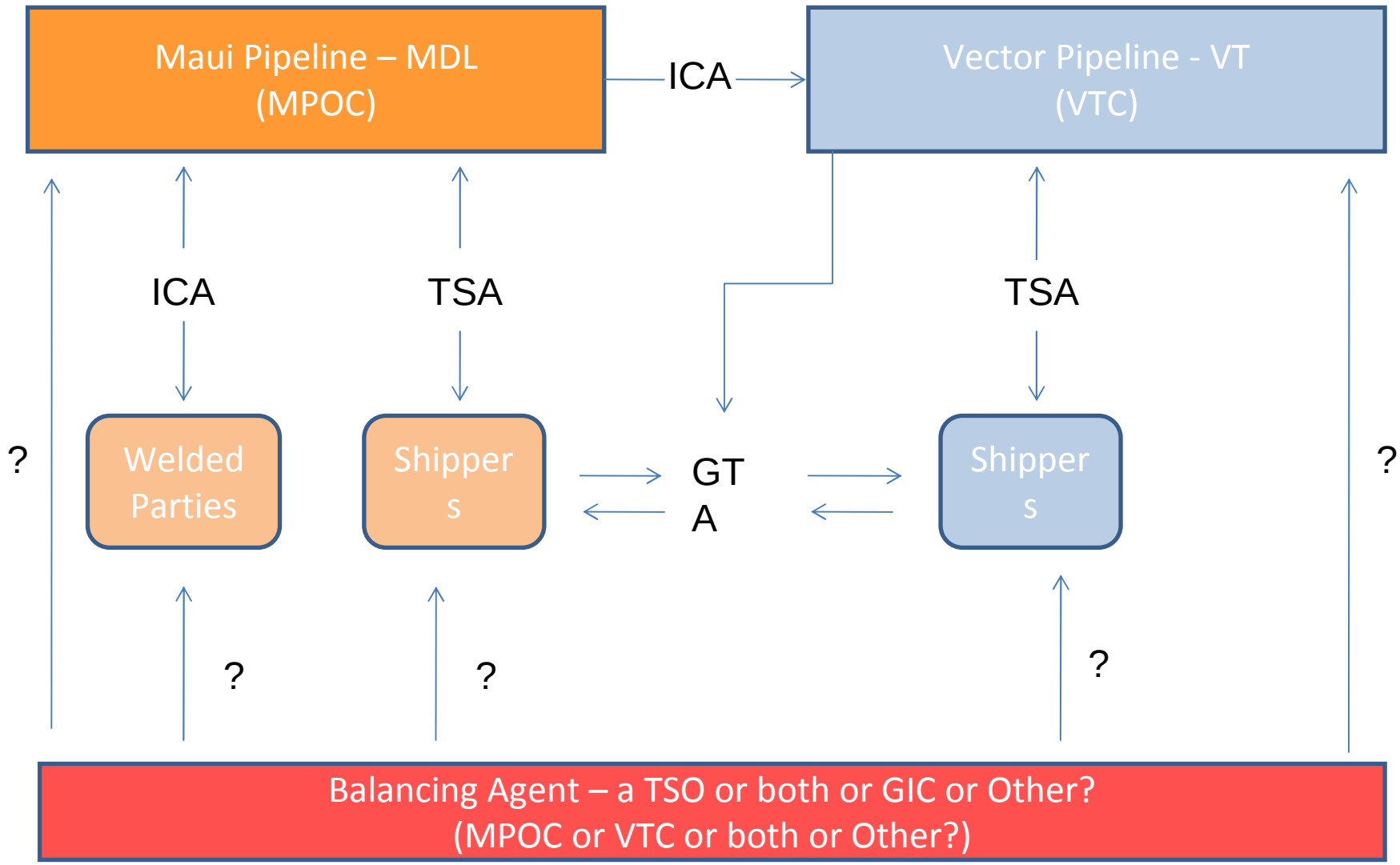
1. Model Objectives
2. Orientation – Model Overview
3. Contractual Structure:
    a. Industry and Contractual Participants
    b. Broad Elements
    c. Concession Agreement
    d. Interconnection and Use of Asset Agreement
    e. Gas Management Agreement
    f. Gas Transmission and Management Operating Code
    g. Fees and Charges
4. Industry Gas Management Company (GasCo)
5. Gas Industry Company
6. Benefits
7. Next Steps

Objective

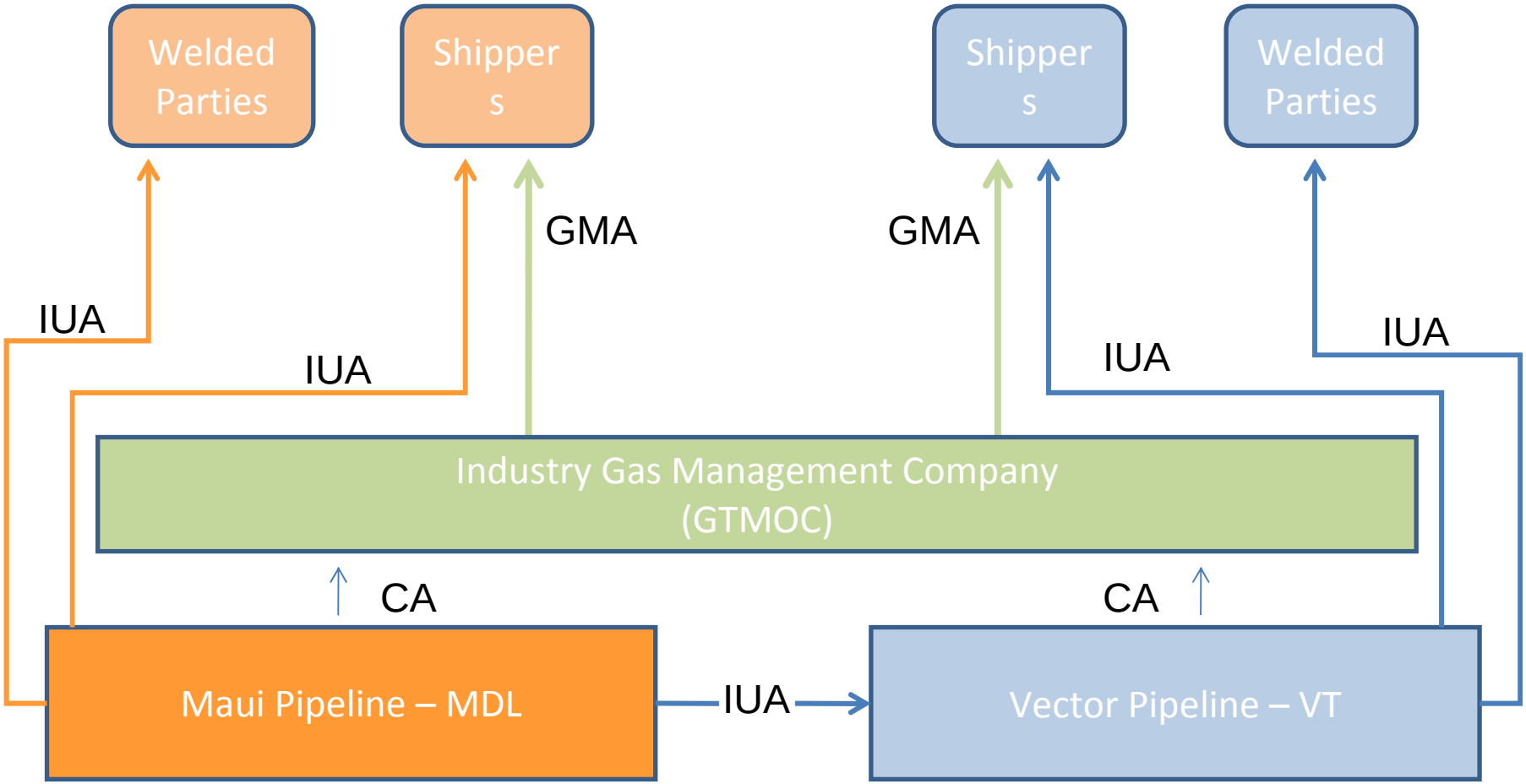
To design a model for the unification of transmission pipeline balancing that meets the following objectives:

- Achieves GPS and Gas Act objectives
- Builds on and extends what is working well now
- Is for the Industry and by the Industry
- Provides certainty and long-term stability for users, owners, energy industry investors, regulators and Officials
- Has operational and commercial integrity
- Is flexible to amend and therefore easier to evolve
- Provides good governance
- Efficiently and fairly allocates risk and rewards (and therefore places incentives in the right place at the right time)
- Is sustainable and lower cost relative to other solutions

Current Contractual Structure (plus proposed residual balancing unification)



Model Contractual Structure - Overview



Orientation – Model Overview

1. Gas transmission and management on both transmission pipelines covered by one operating code (GTMOC)

2. GTMOC predominantly based on MPOC operational design (with minor modifications, such as to accommodate small stations and downstream users)

3. A new user owned company (GasCo) established to own /lease and manage line pack and provide gas transmission and balancing services

4. TSOs continue to contract with Welded Parties and Shippers for access and use rights: charging Shippers for return on capital and cost recovery (although latter partially offset when GasCo commences)

5. Continued use of current IT systems (OATIS and BGX) and existing operators

6. Virtual welded point concept not required as all large stations across the transmission system operate on a single regime – with unified primary and secondary balancing

Contractual Structure

Industry and Contractual Participants

The unification model has five participants:

1. Industry Gas Management Company (GasCo)
2. Transmission System Owners (TSOs)
3. Shippers
4. Welded Parties
5. Regulators (GIC and CC)

Contractual Structure

Broad Elements

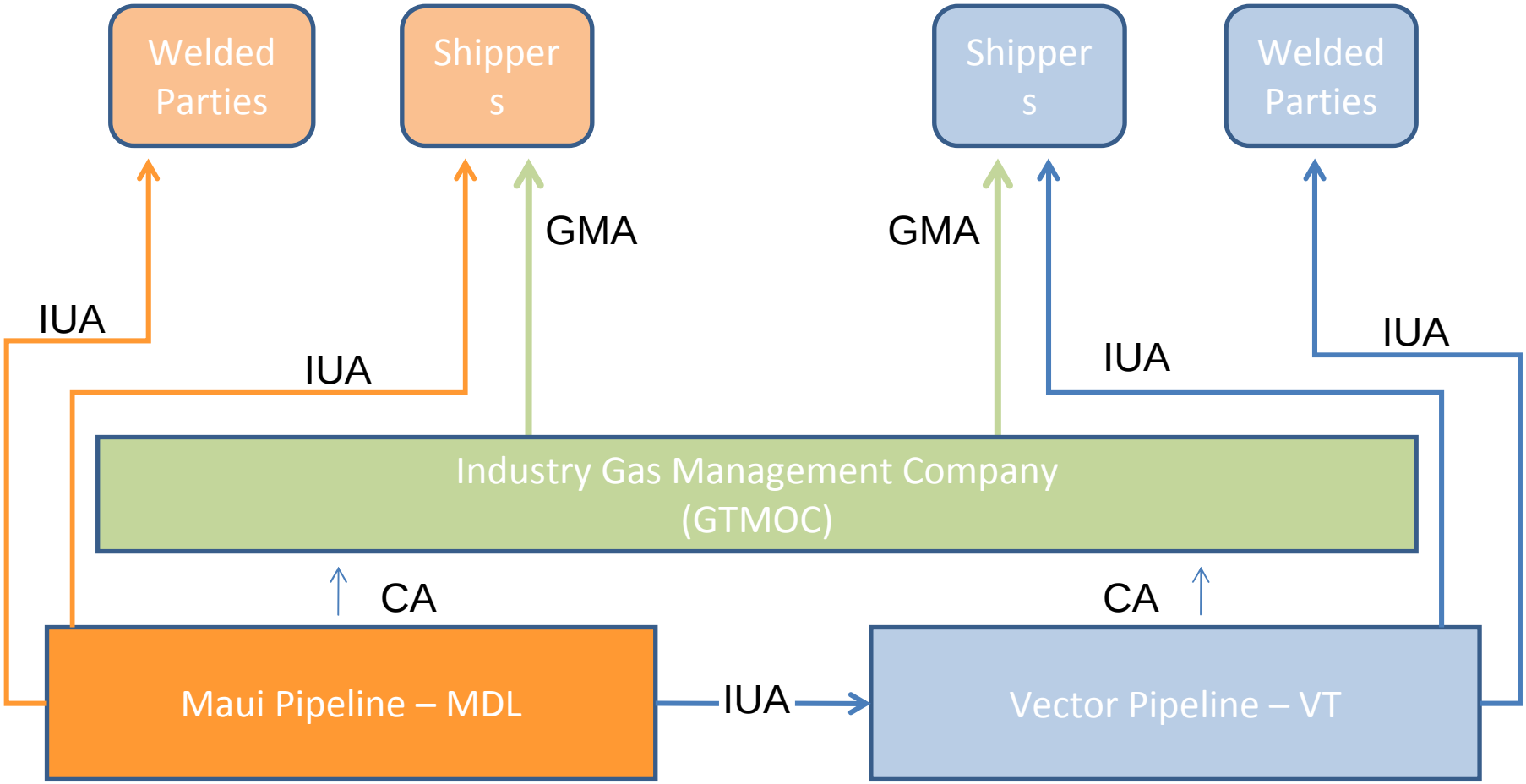
The unification model will need:

1. At a primary level, contracts between the TSO, Welded Parties, Shippers and GasCo

2. At a secondary level*, contracts between TSOs and their respective service providers and GasCo and its service providers

* This presentation only addresses the secondary level in passing

Model Contractual Structure – Primary Level



Contractual Structure

Primary Level

At the primary level, the contractual structure for the unified operational proposal envisages:

1. A Concession Agreement between a TSO and GasCo

2. An Interconnection and Use of Asset Agreement (IUA) between a TSO and a Welded Party or Shipper

3. A Gas Management Agreement (GMA), which incorporates GasCo's Gas Transmission and Management Operating Code (GTMOC), between GasCo and a Welded Party or Shipper

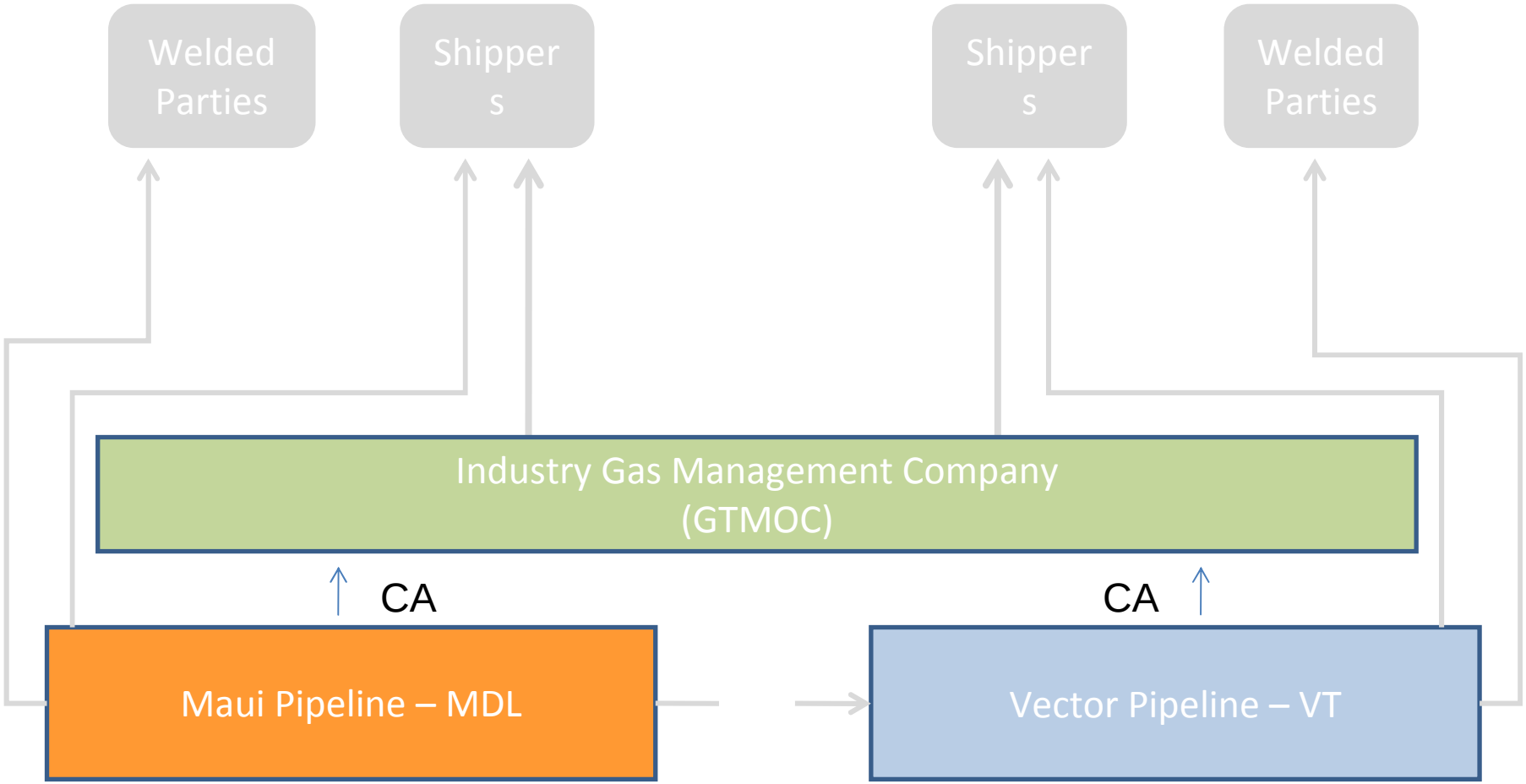
The requirements are as follows:

- To connect, a Welded Party must be a party to an operational and effective IUA and GMA

- To transport, a Shipper must be a party to an operational and effective IUA and GMA

- In each case there must, at the same time, be an operational and effective Concession Agreement in respect of the relevant pipeline

Concession Agreement (CA)



Contractual Structure

Concession Agreement

The Concession Agreement would provide:

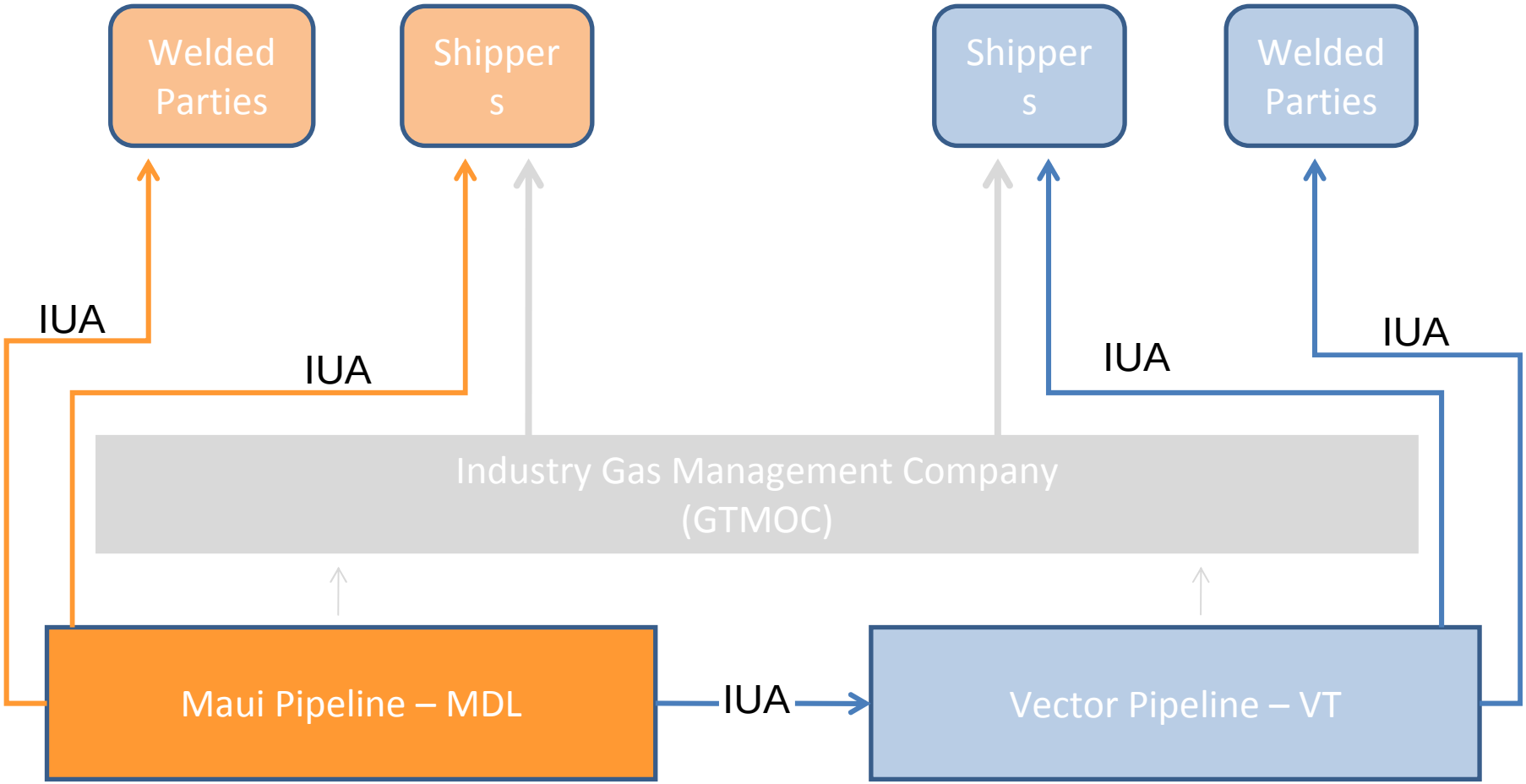
1. GasCo with the right and authority to offer transmission services on the relevant transmission system subject to the terms of the GMA

2. The TSOs grant GasCo the concession for nominal pecuniary consideration (or, if flowing line pack not sold to GasCo, for a user fee in respect of such flowing line pack)

3. For the charging of any TSO imbalances under the GTMOC

- The TSO will recover its return on capital and operational costs directly from users under the IUAs

Interconnection and Use of Asset Agreement (IUA)



Contractual Structure

Interconnection and Use of Asset Agreement (IUA)

The IUA would provide:

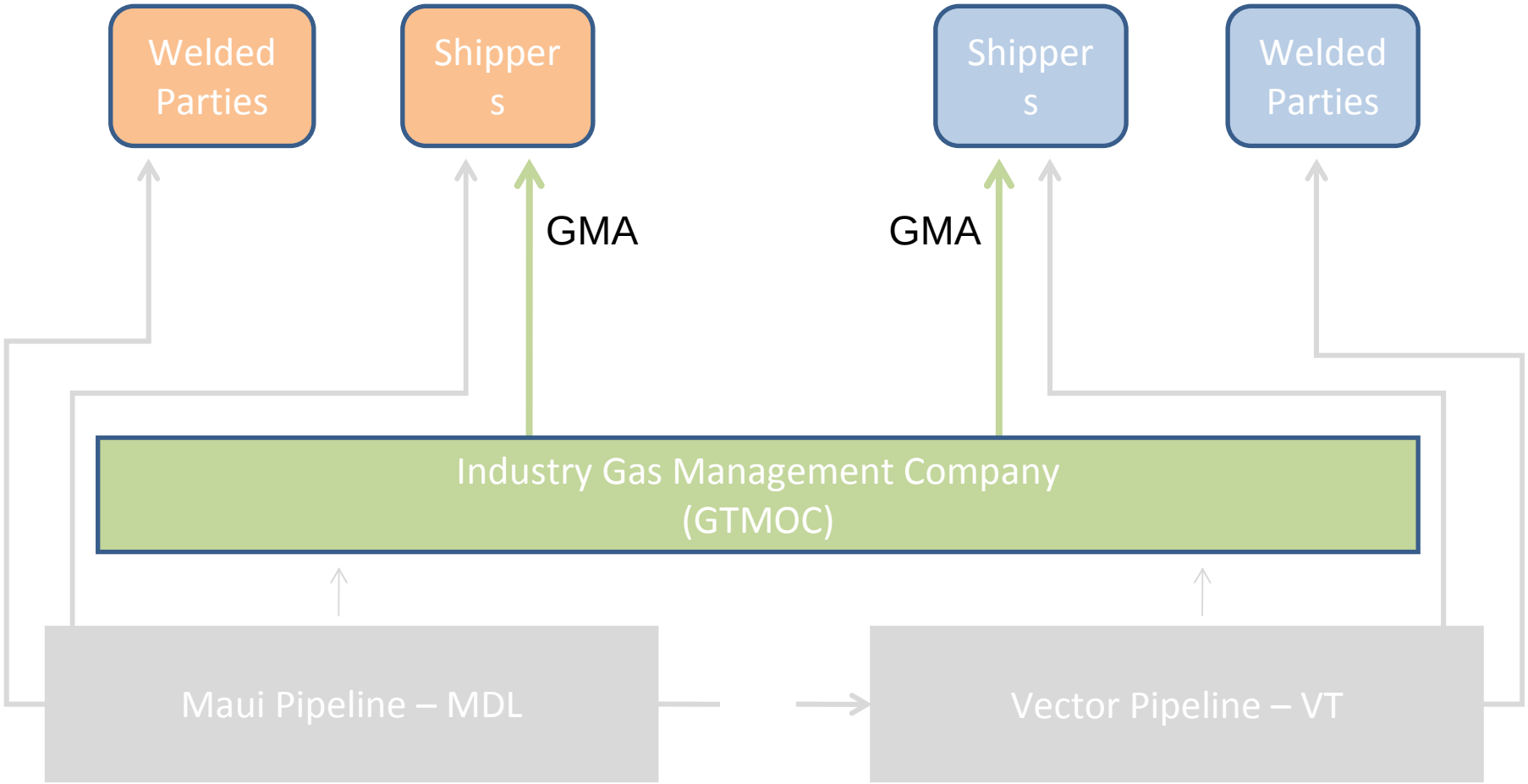
1. On open access terms, for a Welded Party to connect to the TSOs transmission system and/or for a Shipper to use that system (i.e., convey energy in the form of gas) in accordance with a IUA and GMA

2. For the TSO to recover its return on capital in the manner it chooses, provided that that does not conflict with or override the GTMOC, or render the GTMOC wholly or partly inoperable

3. For the TSO to receive from the relevant Welded Party, Shipper and from GasCo all the information that it needs to calculate and recover its return on capital

- For clarity, a TSO will not promise to provide a gas transmission service to a Shipper, as against allow the Shipper to use the transmission system for that purpose upon and subject to the terms of its GMA

Gas Management Agreement (GMA)



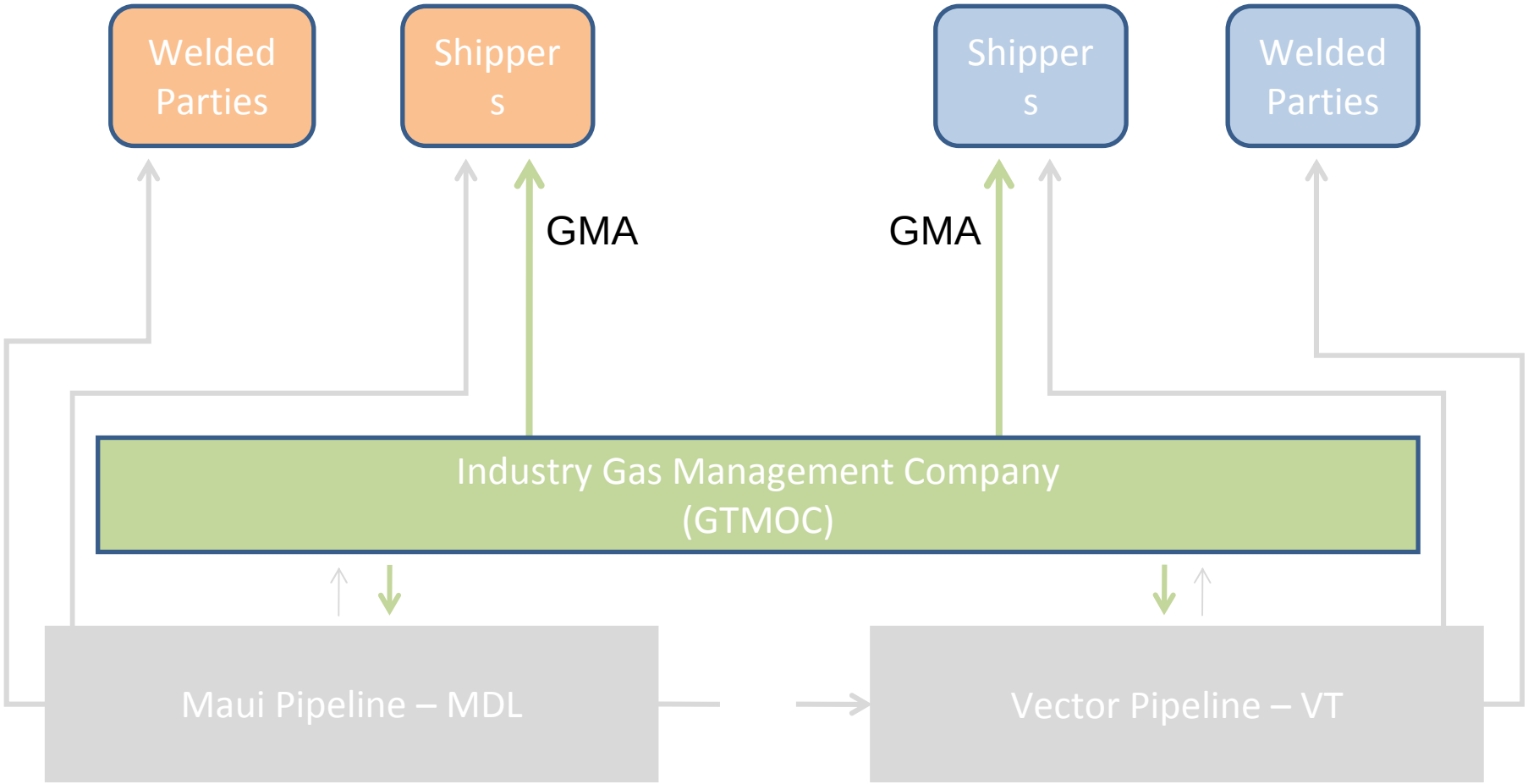
Contractual Structure

Gas Management Agreement (GMA)

The GMA will incorporate the Gas Transmission and Management Operating Code (GTMOC) and will provide for:

1. Gas transmission services
2. Nominations
3. Welded Party confirmations of scheduled quantities
4. Title
5. Operational imbalances
6. Balancing, including balancing policy and balancing charges (including daily and peaking)
7. Possibly tolerances (if so, then use-of-tolerances charges)
8. Curtailment
9. Trading

Gas Transmission and Management Operating Code (GTMOC)



Contractual Structure

Gas Transmission and Management Operating Code (GTMOC)

The GTMOC would adopt the following principles:

1. Gas allocation and title by nomination and OBA
2. Shippers (and VT, if it continues contract carriage) obliged to be in balance every day
3. Daily charges for use of tolerances, for peaking and (back-to-back) for imbalance
4. Balancing actions governed by a policy adopted by GasCo's Board and published: this policy is expected to include thresholds to action, use of balancing markets, transfers of imbalances, accounting for UFG, and publication of information
5. Certain users – identified by maximum flow quantity – not required to nominate or install compliant metering: their share of balancing costs, plus additional administration and other costs, allocated by algorithm
6. If VT continues contract carriage, its share of balancing costs determined by algorithm by reference to zones and a standard pressure calculation (the latter as agreed between GasCo and VT)
7. Curtailment and OFOs based on MPOC concepts
8. Tariff for recovery of all operational and some associated capital costs using T1 and T2 concepts from the MPOC

Contractual Structure

Fees and Charges

Under the revised regime the following fees and charges would apply:

- GasCo:
  - Tariff 1 – return on capital
  - Tariff 2 – recovery of operational expenditure
  - Causer pays balancing charges – back-to-back OI, and peaking and tolerance charges
- VT:
  - Return on capital
  - Recovery of operational expenditure
  - Concession Fee
- MDL:
  - Return on capital
  - Recovery of operational expenditure
  - Concession Fee

Note: it is expected VT and MDL cost recovery tariffs will decrease when GasCo commences delivering transportation and balancing services – may not be a complete offset

Industry Gas Management Company Limited (GasCo)

GasCo could have the following legal structure:

1. A company under the Companies Act 1993
2. Owned by Welded Parties and Shippers (as a condition of interconnection and use)
3. Shareholder capital related to pipeline use and interconnection
4. Board of Directors consisting of five independent Directors (with at least two having relevant industry experience)
5. Decisions made by Board (subject to shareholder approval in some cases e.g, changes to the GTMOC)
6. Management and operational services initially provided by existing MDL and balancing services providers until longer-term arrangements are decided and established by the Board

Gas Industry Company

No change to GIC's current role as a regulator of the gas industry with respect to transmission pipelines (except for access to the Rulings Panel for Disputes)

GIC may continue to have a change request role in relation to IUAs

GasCo's Board of Directors would assume responsibility for changes to GTMOC subject to shareholders special resolution

Conclusion

How does this model benefit the industry?

1. 1 Code + 1 gas management system = simple and workable unification (i.e., coherent)
2. It builds on and extends what is workable with the current (and soon to be enhanced) MPOC system (i.e., familiar)
3. It uses existing operators (i.e., continuity)
4. It places industry at the helm of gas management and transmission (i.e., partially separate ownership and control)
5. It will be less expensive than a regulatory solution
6. It will be more flexible than a regulatory solution
7. It will provide full transparency around gas management and transmission
8. It will provide longer-term certainty and stability
9. It will be easy and quick to implement relative to other solutions (other than sticking with the status quo)

Next Steps

- User survey: (to be carried out next week)

  - Do you support the design premise/observations/objectives?
  - Is there anything you do not understand about the model and require further information/explanation?
  - Are there any aspects of the model you do not support? If yes, please specify and provide reasons
  - Are there aspects of the model that you especially support? If yes, please specify and provide reasons?
  - Assuming there is sufficient industry support for this model, what level of progress towards adopting and implementing it do you think is achievable by the end of November? Do you think this level of progress should satisfy the GIC?

- User survey results (to be presented at the next meeting)

- Compare and contrast the model with other (clear) solutions

- If sufficient support, then take the conversation to the next level