

The Ministry of Petroleum and Energy
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Oslo, March 15, 2013

Proposed reduction of the tariffs for transportation and processing of gas on the Norwegian continental shelf

1 Introduction

We refer to the Green Paper of January 15, 2013 (the "Consultation Paper") issued by the Ministry of Petroleum and Energy (the "Ministry"), requesting comments on proposed amendments to the Regulations of 20 December 2002 No 1724 relating to the stipulation of tariffs etc. for certain facilities (the "Tariff Regulation"). The Consultation Paper broadly proposes a 90 % reduction in the capital tariff (k-element) for all future capacity bookings in Gassled, the Norwegian gas export infrastructure.

We hereby submit our comments to the proposed Gassled tariff reductions, including comments on what we believe are substantial omissions and misleading arguments in the Consultation Paper. Further, we are proposing an alternative approach which better targets identified resource management objectives.

We have asked independent analysts in Pöyry Management Consulting ("Pöyry") and Thema Consulting Group ("Thema") to present their views of critical facts and assumptions presented in the Consultation Paper and a summary of some of their findings are documented by way of attachments hereto.

2 Infragas – a long term contributor of capital and competence

Infragas Norge AS ("Infragas") is a single purpose company established in 2011 for the purpose of acquiring a 5.006 % interest in Gassled from A/S Norske Shell. Infragas' ultimate parent is Canadian pension fund manager Public Sector Pension Investment Board ("PSP Investments"), one of Canada's largest pension investment managers with \$68 billion of assets under management as at September 30, 2012. PSP Investments is a Crown Corporation established to manage employer and employee net contributions to various pension funds of the federal Public Service, the Canadian Forces and the Royal Canadian Mounted Police, and since March 1, 2007, of the Reserve Force.

PSP Investments holds substantial infrastructure investments around the world, focusing on direct investments in the transportation, utilities, power and energy sectors. PSP Investments has a long-standing experience from infrastructure investments and are used to cooperating closely with regulators in this

respect. Infragas and PSP Investments' objective in acquiring a Gassled interest was to become a long term committed owner of gas infrastructure as well as a long term reliable contributor of capital and competence, an ambition that can only be fulfilled under a stable and predictable regulatory regime.

3 Summary of our consultation response

As an owner in Gassled and recent contributor of a substantial investment in the Norwegian gas infrastructure, we are surprised and disturbed by the proposal made by the Ministry in the Consultation Paper and the stated reasons for such proposal. Our reaction is driven, inter alia, by the fact that important considerations generally applicable to regulated assets, and more specifically to the organization and operation of Gassled, are overlooked or disregarded in the Consultation Paper. In essence, the Ministry's proposal clearly departs from what can be regarded as a predictable and transparent regulation of a natural monopoly and from the perceived risks taken by investors contributing capital to Gassled.

The proposed tariff reductions clearly cannot be justified on the basis of resource optimization reasons or reasonable return arguments as presented in the Consultation Paper. While recognizing that resource optimization is an important consideration and that the recovery of additional petroleum resources from the NCS will be in the interest of both the Gassled owners and the Norwegian State, we find that the measures proposed by the Ministry are premature and too widely formulated. In addition, the omission of key decision parameters in the Consultation Paper adds to our concern with respect to the adequacy of the proposed measures.

As evident from the current regulations and previous administrative practice, any proposal for changes in previously stipulated tariffs is subject to strict legal limitations. The proposed tariff reductions in Gassled have no legal basis in the Petroleum Act or otherwise.

Our key comments on the Consultation Paper are the following:

Positive resource optimization effects on the NCS have not been substantiated from the proposed tariff reductions

- The Ministry does not substantiate the stated argument that the proposed tariff reductions will have any positive impacts from a socio-economic perspective on specific petroleum projects. This is a surprising omission given the scope and magnitude of the proposed changes in the tariff regime.
- The Ministry's proposal is too widely formulated and not targeted to address specific resource optimization considerations on the NCS. As proposed, the tariff reductions will mostly benefit existing and developed fields or fields which will be developed regardless of the proposed tariff reductions.
- In the Consultation Paper, the Ministry has not addressed the reasonableness of the current tariff level in Gassled. On the basis of statements in the White Paper Meld.St. 28 (2010-2011), the Ministry seems to be of the opinion that the Gassled tariffs are "*relatively low*" and that the current tariff level in itself is not a problem.

- The unpredictable reduction in tariffs for Gassled owners will affect the overall perception of regulatory risks on the NCS and Norway in general, which could be detrimental to resource optimization as a result of increased cost of capital and associated negative socio-economic effects in the future.

The proposed tariff reductions curtail reasonable and expected returns for the Gassled owners

- The Gassled tariffs were stipulated in 2003 and no explicit or implicit reservations were made by the Ministry regarding future changes. The Gassled owners have since taken the risks associated with the underlying assumptions (gas throughput, operational risk, credit risk etc).
- Considering the cash flows from 1975 onwards to assess the return in Gassled is misleading, and constitutes a new and completely unpredicted development which has never previously been applied in the Gassled history. We note that:
 - The pre-Gassled returns were not publicly available.
 - The pre-Gassled returns were not evenly realized by the current Gassled owners making it impossible to appropriately allocate the historic return arguments to the unitized ownership regime created by Gassled.
 - The Ministry states that a 10 % pre-tax real return has been achieved in Gassled since 1975, a substantial part of which was earned by the owners of Statpipe during the 1980s and 1990s, without its operations being subject to any return regulation as now being proposed.
 - Gassco states that a 7.2% return was already achieved when Gassled was established in 2003, implying that tariffs were reset at that time.
- The introduction of tariff reductions on the basis of the value of existing bookings exceeding assumptions made upon the establishment of Gassled is in breach of basic principles regarding transparency in administrative processes. These assumptions are not publicly available and we are not aware of any basis for claiming that deviations from such assumptions should lead to tariff reductions.
- If adopted, the proposed tariff reductions will, in an unprecedented manner, negatively impact the investment case for investors who have relied on the existing regulatory regime and an expectation of reasonable profits. The result will be a massive transfer of value between infrastructure owners and resource owners, representing tens of billions of NOK.

The process leading up to the Consultation Paper has not been satisfactory and clearly departs from administrative practises historically applied for the Norwegian petroleum sector

- The Ministry's approach in this process clearly departs from decades of industry-focused and dialogue-based public resource management on the NCS, and disregards numerous attempts by us and other key stakeholders to establish dialogue on the tariff matter upon becoming aware of the work undertaken by the Ministry. Instead, the Ministry has unilaterally proposed dramatic changes in the regulation of Gassled, based on considerations that are not transparent and which are not appropriately substantiated in the Consultation Paper.
- We are also concerned by the sequence of events immediately after our investment in Gassled, which, at least from the outside, could be seen to imply that the potential for tariff reductions was under review by the Ministry at such time when we made our investment, without any indication thereof being communicated to us by the Ministry during our various contacts in the context of our acquisition.

- When assessed against publicly known facts and the principles historically applied to the Gassled tariffs, the proposed reductions were highly unpredictable for investors in Gassled. Pursuant to its due diligence, Infragas has based its investment in Gassled on the expectation of a reasonable return within the stated public policy, a stable and consistent regulation regime, and that any tariff adjustments would be consistent with past practice and on the basis of a consultative and balanced process.
- Alternatives to the proposed tariff reductions exist and will provide for a more targeted and efficient approach to applicable resource optimization considerations. More targeted measures include; an extension of the license period for Gassled, prolonging the pay-back time for new investments, and targeted tariff relieves for marginal petroleum resources.

4 Positive resource optimization effects on the NCS have not been substantiated from the proposed tariff reductions

4.1 The proposed tariff reductions will mostly benefit existing and developed fields or fields which will be developed regardless of the tariff reductions

The stated reason for the Ministry's proposal to reduce the Gassled tariffs is the need to promote resource optimization on the NCS to ensure that as much NCS petroleum resources as possible will be produced and brought to market. However, the resource optimization argument made is not relevant for substantial parts of the volumes which will benefit from the proposed tariff reductions, either because the investment decisions have already been made for such projects or because the project economics dictate that the resources will be developed regardless of the tariff reduction.

We have asked Pöyry to prepare an analysis of the future volumes in Gassled which will be affected by the proposed tariff reductions, see [Appendix 1](#) hereto. As substantiated by their analysis, the net present value of the tariff reductions discounted at 7 % is NOK 40.3 billion. Of this amount, 42.8 % will be for the benefit of resources that are already producing or approved for development, while another 20.4 % for the benefit of contingent resources in existing fields. Discoveries represent 26.7 % of the expected volumes, of which approximately one half relates to resources currently being planned for development. Only 10.1 % will be for the benefit of prospective resources.

In view of the above, the proposal set forth in the Consultation Paper results in a substantial transfer of value from the Gassled owners (specifically those not owning gas resources) to the owners of developed or otherwise economically viable gas resources on the NCS.

4.2 The effect of the proposed tariff reductions on specific petroleum resources is not substantiated

The effects of tariff reductions on resource optimization are very broadly described in the Consultation Paper. The Ministry generally assumes that reduced tariffs will lead to increased exploration activity, the development of marginal petroleum resources, and enhanced recovery in fields on the NCS. No attempt is made in the Consultation Paper to substantiate the existence of any such effects in specific fields or in specific areas of the NCS.

In our view, there is no clear evidence supporting the assumptions made by the Ministry. As pointed out, a reduction in Gassled tariffs will entail a transfer of value from the infrastructure owners to the resource owners, but there is no guarantee that such funds will be used for exploration purposes on the NCS. Positive socio-economic effects occur only where such value transfer contributes to additional activities. A contribution to making otherwise economically viable projects even more profitable, does not qualify from a resource optimization point of view.

Based on input from Pöyry, we below discuss the potential for positive socio-economic effects from tariff reductions in respect of each of the three categories of activities referred to in the Consultation Paper. As evident from our analysis, the very broad assumptions made by the Ministry in respect of positive socio-economic effects from reduced Gassled tariffs cannot easily be substantiated.

Increased exploration activities

In view of the risks and various cost elements involved with drilling operations and subsequent development of discovered resources, it is clear that a lower k-element in the Gassled tariffs will have only a marginal economic effect on exploration activities. Geological risks, drilling costs, development costs and oil and gas prices are the key drivers for investment decisions in this respect and will by far outweigh the effect of the k-element.

The cost elements related to the drilling of an exploration well, and a prospect's modeled development and operations costs have increased substantially and well above general inflation levels during the last decade (the costs attached with drilling of an exploration well have more than tripled in this period). In comparison, the k-element in the Gassled tariffs is escalated based on the general Norwegian Consumer Price Index, thus the relative weight of the k-element in overall costs for exploration and development projects has been gradually reduced over time. Additionally, since 2003, the k-element for area D has been reduced by more than 50 % in real terms in accordance with Section 4 of the Tariff Regulation.

Regardless of these substantial costs increases on the NCS, exploration activities have increased significantly since 2003. This is mainly attributable to higher oil and gas prices, favorable changes in the tax system for exploration activities, introduction of yearly APA license rounds, and exploration successes.

Increased development of resources

There is no clear evidence that marginal discoveries will turn economically viable as a result of the proposed tariff reductions. As mentioned above, positive socio-economic effects arise when an otherwise uneconomical field becomes economically viable and is developed. Against this background, Pöyry has analyzed the potential effects of the proposed tariffs reductions on all current marginal discoveries on the NCS classified as "*development is not very likely*" by the NPD (Resource Class 6).

Pöyry concludes that, although the effects of the proposed tariff reductions vary from field to field, there is no clear example of such reductions contributing significantly to bringing a project above or closer to the return requirements typically sought by resource owners. Based on Pöyry's analysis, the proposed tariff

reductions will not in itself contribute to the increased development of resources on the NCS. The assumptions and further details of the Pöyry analysis are attached as [Appendix 2](#) hereto.

Enhanced oil & gas recovery

There are marginal benefits from the proposed tariff reductions on enhanced oil and gas recovery. The proposed tariff reductions would only have minor effects on tail-end production of producing fields and only to the extent that no large investments are required to then continue production. This is evident from Pöyry's analysis that further indicates that there is no need to reduce tariffs for all stages of field production since the reduction is only effective in the last year of production. Hence, there would be merit in discussing a more targeted approach to address tariffs in the very end of the production period which could be a more appropriate measure while still addressing the optimal resource management concerns of the Ministry.

In respect of investments for the purpose of prolonging plateau production in oil and gas fields, Pöyry concludes that the reduced tariffs may have a marginal positive economic effect but no real impact given the size of the initial investments relative to the tariffs.

4.3 *Are the current Gassled tariffs unreasonably high?*

In view of the fact that specific socio-economic effects of the proposed tariff reductions may prove difficult to substantiate, we would have expected the Ministry to discuss more objectively whether the current tariffs in Gassled are set at a level where negative socio-economic impacts could be expected. A key consideration would be whether such tariffs, in view of expected development costs for new resources and expected future resource prices, may be seen to create an unreasonable hindrance for resource optimization. Surprisingly however, the Consultation Paper does not address the current tariff level in Gassled at all.

An explanation as to why the current level of Gassled tariffs is not addressed in the Consultation Paper can be found in the Ministry's recent White Paper, Meld.St. 28 (2010-2011), "An industry for the future – Norway's petroleum activities". In section 4.6.1 of this document, the Ministry states that the current Gassled tariffs are "relatively low". Similarly, Gassco has concluded in its NCS 2020 study that the current gas infrastructure system is "fairly robust" and that the production from marginal fields will be profitable as long as gas prices exceed 1.20 NOK/Sm³ (which has been the case for the last decade).

In view of the above, the Ministry and Gassco seem to be of the opinion that the current tariff level in Gassled is not in itself a problem, but that already reasonable Gassled tariffs nevertheless shall be further significantly reduced for resource optimization purposes.

4.4 *The proposed tariff reductions may hamper the development of new gas resources and thus hamper resource optimization*

The unpredictable reduction in tariffs for Gassled owners and for independent observers will, as further discussed below, affect the overall perception of regulatory risks on the NCS and more widely the perceived regulatory risks when investing in Norway.

An increase in perceived regulatory risk will entail an increase in the cost of capital which, in the case of investments on the NCS, is likely to impact on investment decisions relating to infrastructure projects and field development, as well as the general cost of funding. As a result, this is likely to alter the willingness of infrastructure investors seeking long term regulated returns to invest on the NCS in the future.

The presence of a diversified base of capital providers on the NCS must be regarded as positive. The recent sale of Gassled interests illustrates how investors with high cost of capital tend to divert their investments away from regulated assets with lower return while being replaced by infrastructure focused investors. This definitely contributes to efficient resource optimization and positive socio-economic effects. To the contrary, increased cost of capital will likely lead to reduced resource optimization and, in turn, reduced tax revenues for the State (i.e. lower activity, increased deductions from financing costs, etc).

The above is illustrated through an analysis of the potential economic welfare effects of the proposed tariff reductions in Gassled, prepared by Thema and included in summary in [Appendix 3](#) hereto.

The proposed tariff reductions may also have additional unexpected effects hampering optimal resource development on the NCS. This relates to complex issues which can only be discussed very briefly within the context of this letter. For example, there are certain challenges in place regarding the effectiveness of the capacity allocation regime applied to Gassled. For historic reasons, the legacy gas producers have booked and control the capacity in critical parts of Gassled for many years to come, providing flexibility in their handling of gas resources. At the same time, such advance (and in some cases surplus) bookings by the large producers hamper the possibility for new resource owners to secure evacuation of their resources.

Assumingly, a substantial tariff reduction would trigger the large gas producers on the NCS to potentially maximize the use of their booking rights in Gassled in order to further enhance the value of their gas resources. The result could be an increased congestion of the Gassled system which could potentially be detrimental for the owners of marginal fields and new discoveries given that less capacity will be available. The resource optimization effects will in such a situation be quite opposite to what is sought in the Consultation Paper.

4.5 *Observations regarding the need to establish a gas pipeline to the Barents Sea*

The need for establishing a new gas pipeline to the Barents Sea is specifically mentioned in the Consultation Paper as a reason for the proposed reduction in Gassled tariffs. Even if one should agree that such a need exists, it is difficult to justify how tariff reductions in the existing Gassled system would contribute to such a development.

Currently, the key challenge for new infrastructure developments in the Barents Sea is the level of economically viable resources discovered in the Barents Sea which is currently not sufficient to lift the substantial investments required. It is unlikely that oil and gas companies would be willing to take the risk on prospective resources in the Barents Sea being discovered and developed, and this is a challenge which is not solved through lowering the tariffs in the existing Gassled system. To the contrary, the actions of the Ministry, should the changes proposed be implemented, will reduce infrastructure investors' appetite for making new long term investments on the NCS.

The irrelevance of the Barents Sea pipeline for the proposal made by the Ministry is evidenced by the fact that such pipeline is not likely to be operational before the very end of the Gassled license period. Further, in the pre-2028 period, the alternate route for Barents Sea gas would be through Polarled to Nyhamna and then through Langeled. This route would only be marginally affected by the proposed tariff reductions due to special tariff regulations in place for these facilities (Pöyry calculations indicate that an 8 % tariff reduction would be offered for resources evacuated through this route). The tariff regime for the period after 2028 is still unknown.

We would not rule out that targeted tariff adjustments would be sensible in order to make sure that the Barents Sea gas will be competitive in the European gas market. This issue should be addressed in due course and with the aim of finding appropriate measures targeted at the undeveloped resources in the Barents Sea.

4.6 *Alternatives to the proposed tariff reductions exist and will provide for a more targeted and efficient approach to applicable resource optimization considerations*

We believe that the various considerations discussed above, indicate that the proposed tariff reductions in Gassled will have only marginal positive effects, if any, on resource optimization. Even based on the Ministry's own assumptions, it is difficult to understand why tariff reductions need to be introduced now and to the extent proposed by the Ministry.

There are several alternative measures which would be more targeted than the general tariff reductions contemplated in the Consultation Paper. Such measures would aim to address long term development of the gas infrastructure on the NCS and to identify efficient and sustainable solutions to any resource sub-optimal effects created by the Gassled tariffs, while avoiding the many disadvantages that follow from the broader approach taken by the Ministry. Such potential alternative measures include:

- **Extension of license period:** The objective is to create a good basis for lower tariffs as existing and upcoming integrity investments (I-element) can be paid back over a prolonged period.
- **Assessment of targeted measures to stimulate production of marginal petroleum resources:** The objective is to incentivize exploitation of resources that may not be possible to realize in the future at the current tariff level. Such incentives could target specifically:
 - Tail-end resource production from developed fields
 - Barents Sea resources considered to be developed

From Infragas' perspective, future targeted measures should most certainly be considered for the purpose of securing resource optimization, in due course, based on transparent criteria and balanced terms. However, a reasonable approach to tackle this would be for the Ministry to engage in discussions with the Gassled owners on how and when such industry challenges should be addressed.

5 Proposed tariff reductions curtail reasonable and expected returns for the Gassled owners

5.1 Introduction

As evident from current regulations and previous administrative practice, the 7 % pre-tax real rate of return policy generally applies as a yardstick upon the initial stipulation of an infrastructure tariff on the NCS. At such point in time, a range of assumptions are made (including the expected volume throughput in the relevant asset) for which the infrastructure owner will normally carry the risk. There would normally not be any subsequent calibration of the tariffs in order to make sure that a specific return target is achieved, other than where specifically stipulated as part of the tariff terms. Subsequent amendments of the tariffs will generally be an intervention on the established rights of the infrastructure owner and will require the presence of new, unpredicted and material circumstances dictating a change in the status quo.

In the Consultation Paper, the Ministry does not discuss in depth the applicable regulatory model for Gassled or the legal limitations in place for changing the Gassled tariffs, but only generally states that reasonable returns have been achieved by the Gassled owners. The stated basis for this conclusion is that the current return from assets included in Gassled (when considering all cash flows since the establishment of the first gas pipeline on the NCS in 1975) is currently 10 % and that such return will be 10.5 % at the expiry of the Gassled license in 2028 on the basis of current capacity bookings. The Ministry also states that the net present value of future cash flows from existing bookings in Gassled exceeds the assumptions made with respect to expected cash flows upon the establishment of Gassled from 2003.

For several reasons, the presumptions made by the Ministry with regards to the achievement of reasonable returns by the Gassled owners are unclear and problematic, and likely irrelevant for material parts. Key comments on this matter are:

- The reference to a real rate of return on investments pre-Gassled has never before been applied to the Gassled system and is partially based on not publicly available information, meaning that the introduction of this principle is a new and unpredicted development.
- The assumptions made upon the establishment of Gassled in 2003 are also not publicly available and we are not aware of any basis for claiming that deviations from such assumptions should lead to tariff reductions.
- When assessed against the principles previously applied when stipulating Gassled tariffs, both current and expected returns of Gassled are reasonable and as expected.

5.2 *The reference to a real rate of return from historic investments or from an agreed asset base for Gassled is not relevant*

The Ministry's reference to a pre-tax real rate of return of 10-10.5 % since historic investments were made in gas pipelines on the NCS during the 1970s and 1980s is irrelevant when assessing returns received by owners of the unitized Gassled system. This statement is proven by the following observations:

- The ownership in the various gas pipelines which were merged into Gassled were diversified, meaning that no unitized pre-Gassled returns exists. The only logical way to present pre-Gassled returns would be to make individual assessment for each pre-Gassled owner.
- Several of the pre-Gassled pipelines, including Statpipe which was the main asset in term of shipped volumes and revenues earned during that period, were unregulated and had no return policy in place. The notion of regulated returns is introduced retrospectively to such assets. The return figures mentioned by the Ministry are highly dependent on the pre-Gassled revenues from such unregulated pipelines, especially Statpipe which represented approximately 50 % of the pre-Gassled revenues and has a pre-tax real return well above the 10 % quoted by the Ministry. These profits were derived by a handful of oil and gas companies which are generally not owners in Gassled today. Other parts of the infrastructure have provided returns far below the stated policy of 7 %, even when considering Gassled cash flows until today, as further illustrated in [Appendix 4](#) hereto.
- Another important observation is that the pre-Gassled pipelines were for a material part, owned by resource owners in similar proportion to their resource ownership, implying that there was a balance between paid and received tariffs.
- The underlying risk profiles of the various pre-Gassled pipelines were different, implying that the returns may validly have differed between such pipelines.

As part of the establishment of Gassled, an agreed asset value base was determined on the basis of expected future revenues of the various pipelines from 2003 onwards. The k-element was established based on such agreed asset value, completely disregarding historic returns, which according to Gassco were already 7.2 % at that time. In view of the above and other considerations in place upon the establishment of Gassled in 2003, an approach based on real rate of return from historical investments is not relevant for Gassled.

As we understand it, the aim of the agreed new tariffs in Gassled was to ensure an economic outcome for each of the stakeholders as much as possible equal to what they would have achieved had the unitization not been implemented. As a result of this principle, previous owners of unregulated pipelines were implicitly allowed to continue to earn previously stipulated high returns in Gassled, since such returns were reflected in their ownership interest allocation. As a result, the Statpipe owners received approximately 50 % ownership of the unitized system.

We are not fully familiar with the assumptions used in 2003 but we are not aware of any agreement made or requirement imposed then on the Gassled owners with respect to a future calibration of the Gassled tariffs in order to meet any specific return target. Based on relevant legal texts and developments since

2003, the risk of not achieving the then stated assumptions was seemingly allocated to the infrastructure owners, as were the benefits attached with the same.

Based on the above, we find it quite clear that the Ministry cannot conclude that the Gassled owners have received a reasonable return from Gassled based on the pre-Gassled cash flows or alleged fulfillment of assumptions made in private in 2003. As further discussed below, the assessment of what is a reasonable rate of return from Gassled, if such term is at all relevant for the rights of the Gassled owners, will need to be based on transparent and clear principles, including publicly known facts and the regulations and policy principles applied previously to Gassled. The application of any other principle would be in clear breach of prior practices and also in breach of basic principles of transparency applicable to administrative processes.

5.3 When assessed against publicly known facts and the principles historically applied to the Gassled tariffs, the proposed tariff reductions were highly unpredictable for investors in Gassled

Infragas is one of several recent infrastructure investors in Gassled who recently have invested in total approximately 32 billion NOK in the gas infrastructure to acquire 45 % of the Gassled interests. The other infrastructure investors are Njord Gas Infrastructure AS, Solveig Gas Norway AS and Silex Gas Norway AS, hereinafter jointly with Infragas referred to as the "Infrastructure Investors".

Infragas has based its investment case on the expectation of a reasonable return going forward and the current Gassled tariffs, without any knowledge of historically high returns enjoyed by others or any other reason why future returns should be curtailed. This means that the radical intervention in Infragas' expected future tariff income proposed by the Ministry, was not predictable when we made our investment decision.

The stability of the tariff regime and the potential for future tariff reductions were key areas of focus when assessing the possibility of investing in Gassled. As a result of our due diligence which included meetings with representative from the Ministry, we understood that Gassled was governed by a stable and consistent regulation regime, that any tariff adjustments would be consistent with law and past practice, and that the process would be consultative and balanced. We also understood that no discussion on the Gassled tariff levels was ongoing at the time.

As part of the available information on which Infragas based its investment decision, aside from the various public documents incorporating the current tariff regime, was valuations of Gassled made by Gassco and approved by the relevant asset owners, and indirectly approved by the Ministry, for the inclusion of new pipelines into Gassled. The methodology applied upon historic valuations of Gassled (the "Gassled Reference Case") has been forward looking only, with reference to current Gassled tariffs for the remaining part of the Gassled license period multiplied by the expected volumes for such period, without any reference to historic returns or historic assumptions made prior to the date of such evaluation.

One would think that external investors looking to acquire an interest in Gassled could safely rely on such valuation methodology as a reasonable reflection, on a forward looking basis, of the net present value of expected future tariff income in Gassled. However, as illustrated in [Appendix 5](#) hereto, an investment with effect from 1 January 2011 (as the case is for Infragas) based on the Gassled Reference Case would yield a

pre-tax real return of 4.5 % if the proposed tariff reductions are introduced. This is substantially below the generally stated return policy on the NCS and the expectations of Infragas.

A third reference point for Infragas was the Ministry's policy statement, Meld.St. 28 (2010-2011), issued in 2011 which includes various measures to be implemented in order to increase the efficiency of Gassled, but no indication whatsoever of any tariff adjustments.

Viewed in hindsight, we find it disturbing that, in 2011, during our due diligence and approbation linked meetings, the Ministry and Gassco may already have had initiated a review of the tariff levels in Gassled. At least that is the impression given by the fact that reports of such process appeared in the public early 2012, only weeks after we had completed our Gassled acquisition. If any process which could reasonably lead up to tariff reductions were initiated in 2011, we would have expected to be informed as part of our discussions with the Ministry.

In its Approval Letter of December 2011, the Ministry has stated that they have the authority to impose future amendments in the Gassled tariffs. This statement did not change the general impression left by the Ministry that no such amendments were imminent or in the planning. Infragas is well aware of the Ministry's legal authority to amend existing tariffs in certain situations, which seemingly is the authority referred to in the approval letter. Of course, the Ministry could not have intended to impose new restrictions on all Gassled owners in a letter sent only to new investors seeking ownership in such asset.

Based on the above, the reasonable assumption when we made our investment decision was that we would be able to receive the existing Gassled tariffs on future bookings. Regrettably, such expectations have been entirely, and in our view unreasonably, set aside by the proposal set forth in the Consultation Paper.

5.4 Stakeholders experience detrimental effects from the proposed tariff amendments, in some cases due to arbitrary effects

The Consultation Paper does not address the impact of the proposed changes on the Infrastructure Investors who entered Gassled in 2011-12 and who currently own most private interests in the pipeline system. We find this lack of consideration to be surprising, given the fact that the proposed tariff reduction mainly affects a limited group of Gassled owners. One would expect that the effects of the proposal for the Infrastructure Investors in particular, who have no balanced interest in the tariff reduction since they are not resource owners, would have been mentioned and considered in the overall assessments made by the Ministry.

Infragas (and several other owners in Gassled) has not benefited from the historical returns referred to in the Consultation Paper and will have its overall return substantially curtailed by the proposed tariff reductions. Based on our calculations, the overall net present value of the proposed tariff reductions in Gassled is NOK 40 billion pre-tax, Infrastructure Investors will assume 45 % of this loss (NOK 18 billion).

Infragas and the other Infrastructure Investors are not the only Gassled owners which stand to lose substantial amounts of money on the proposed radical changes in the tariffs. The proposal creates winners and losers, in some cases in an arbitrary manner. Among the losers will be investors in new infrastructure merged into Gassled after its inception in 2003. These investors had made substantial investments and have subsequently, by request from the Norwegian authorities, traded their rights to a pre-tax 7 % real return from their single asset against a proportional ownership interest in Gassled, with accompanying returns based on the overall tariff income of the system. Some of these investors have no link to pre-Gassled returns, but will also suffer a substantial reduction in the expected returns on their investment as a result of the proposed tariff reductions.

The effect of the proposed tariff reductions on individual investors in Gassled is illustrated by the situation for investors in the Langeled and Gjøa pipelines. The expected rate of return for such investors will be reduced from 7 % to 1 - 4 % if the proposed tariff reductions are implemented. Furthermore, for the Gjøa investors, this loss of income will not be compensated fully through reduced transportation costs, since the Ministry has proposed that the existing k-element tariff shall be maintained for this specific pipeline.

Another category of potential losers from the proposed tariff reductions are those shippers who have currently overbooked capacity either in order to secure flexibility in their future gas sales or which have ended up in such a position due to downward adjustments of their resource base. For these resource owners, although the current tariff level will still be applicable to their bookings, the secondary market pricing for such excess capacity may in principle be reduced by 90 % in line with the proposed changes in tariffs (at least where there is excess capacity in the relevant parts of the Gassled system). Conversely, resource owners who have in the past underweighted their capacity booking compared with their available resources will obtain arbitrary profits if all future capacity bookings are to be made at the reduced tariffs.

Clearly the biggest losses in result of the proposed tariff reductions is taken by the Norwegian State/Petoro, which holds a 45.8 % ownership interest in Gassled and only has 31 % of the NCS resource base. For the Norwegian State, the immediate loss (NPV of future net gains/losses) as a result of the implementation of the new tariff system may be estimated to NOK 9.8 billion. All of these losses appear however to be compensated by the fact that Statoil is benefiting the most from the proposed tariff reductions. While Statoil has already capitalized on the existing tariff levels through the sale of a substantial part of its Gassled interest to Solveig in January 2012 at a price of NOK 17.5 billion, it will now in addition receive a NOK 15.4 billion NPV net gain from the proposed tariff reductions in Gassled. This redistribution of value between the State Treasury and Statoil is not mentioned by the Ministry in the Consultation Paper.

6 The process leading up to the Consultation Paper has not been satisfactory and clearly departs from administrative practises historically applied for the Norwegian petroleum sector

The establishment of Gassled with effect from January 1, 2003, can be seen as a result of the government dialogue based approach successfully applied on the NCS in past decades. The framework for the new organization of the gas infrastructure was established through early discussions between the various stakeholders and with an objective to minimize the use of administrative powers. This approach resulted in

substantial changes of significant socio-economic value, which hardly could have been unilaterally imposed on the gas infrastructure owners under current regulatory principles. Key features of the historic government model with regards to the oil and gas industry have been the emphasis on early consultation with key stakeholders and a step-by-step approach to changes.

A key premise for investments from Infrastructure Investors in the Norwegian gas infrastructure has been the perceived stability of the Norwegian regulatory regime and the Ministry's reputation for involving the industry in discussions on if, how and when possible amendments in statutory regulations should be implemented.

However, the Ministry's handling of the currently discussed tariff reductions sets a new and very negative precedent in this respect. As owners of 45 % of Gassled, Infragas and the other Infrastructure Investors have been concerned since first hearing reports regarding a potential review of the Gassled tariffs. Infragas has since, without success, actively tried to engage with the Ministry in order to obtain information, understand the Ministry's thinking, and constructively discuss potential solutions to address the Ministry's objectives.

The Consultation Paper, which substantially undermines the investment case for Infragas and other investors in Gassled, has been unilaterally prepared by the Ministry without any input from the Gassled owners and the interests of such parties are barely mentioned therein. We are concerned with the approach chosen by the Ministry in this process and the short and long term effects it will have on resource optimization on the NCS.

Our concerns with the approach taken by the Ministry are not limited to the absence of discussions and co-operation with key stakeholders along the way. There have also been gaps in the fulfillment of basic legal rights in the Consultation Process, such as the access to information. The Ministry and Gassco have denied us access to important information upon request. As a party directly affected by the proposed tariff reductions, we would have expected full transparency in respect of factual information of relevance to the considerations set out in the Consultation Paper.

7 Brief on applicable legal considerations

The current Gassled tariffs are regulated through the Tariff Regulation and the overall legal framework for Gassled set out in the Petroleum Act and Chapter 9 of the Petroleum Regulation. In its Consultation Paper, the Ministry refers to Section 4-8 of the Petroleum Act and Section 63 of the Petroleum Regulation as the basis for stipulating and/or amending tariffs in Gassled. In our view, there are certain key limitations to the Ministry's authority to amend previously stipulated tariffs, which are not met nor mentioned in the Consultation paper. Key considerations are:

- Under statutory law, there is no doubt that the Gassled owners' rights under the Tariff Regulation, including the right to receive tariffs at the current rate, benefits legal protection equal to that provided by an individual administrative decision and that such rights may only be interfered with upon the fulfillment of strict requirements.

- The requirements for intervention in the current Gassled tariffs, as reflected inter alia in Section 4-8 of the Petroleum Act, include a need to establish; (i) new, unpredicted and material developments compared to the situation when Gassled was established in 2003; (ii) that tariff amendments are required in order to secure resource optimization in specific petroleum projects; and (iii) that such considerations substantially outweigh the interests of the Gassled owners in receiving the currently estimated returns from its asset ownership and always so that the Gassled owners shall be entitled to a reasonable profit.
- The Tariff Regulation sets out tariffs for the entire Gassled license period up until 2028 and covers already booked capacity and available capacity which are to be booked in the future. The considerations set out above, including the strict requirements for amending previously stipulated tariffs, apply in respect of booked capacity and available capacity the same, but additional and even stricter requirements may apply should the Ministry propose to intervene in established private agreements.

In its Consultation Paper, the Ministry has not discussed in detail the legal basis for its proposed tariff reductions, but the underlying premise seems to be that the Ministry is free to introduce tariff reductions in order to promote general resource optimization interests as long a reasonable return for the Gassled owners is secured.

Section 4-8 of the Petroleum Act and general principles of administrative law, do not allow for tariff amendments based on such a broad approach. The Ministry's past practice regarding tariff reductions (pre-Gassled) clearly provide that the authority to intervene in established tariffs only applies in special circumstances, where an "emergency valve" is needed due to change of circumstance. Section 4-8 and other relevant legal grounds clearly do not provide an instrument for setting aside private interests for the purpose of promoting widely defined policy changes or for calibrating returns to fit assumptions made upon the stipulation of such tariffs, as seemingly attempted through the Consultation Paper.

If anything, the introduction of the Gassled joint venture must be viewed as having limited the Ministry's authority to amend existing tariffs. Previously, the main commercial interest of the pipeline owners was to secure transportation of their own gas and the use of spare capacity by others was only a bi-effect of this main activity. Currently, the link between resource ownership and Gassled ownership is very remote and in some cases non-existent. The core business of the Gassled owners is to make transportation capacity available for others and to receive tariffs for such services. For obvious reasons, the threshold for the Ministry's intervention is higher in the latter situation compared with the situation where spare capacity is offered to third parties as a bi-effect of resource driven activities.

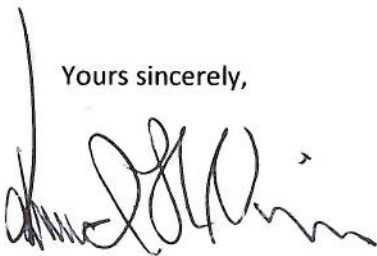
Without pointing to any clear and substantiated need for reducing the Gassled tariffs, the Ministry has chosen to maximize its intervention through reducing future capital tariffs by 90 %. This intervention is clearly disproportional when weighing the expressed general interest of promoting resource optimization against the individual Gassled owner's fundamental right to enjoy its established rights as an owner of the affected infrastructure.

8 Concluding remarks

The implementation of the radical and contested actions proposed by the Ministry in its Consultation Paper will cause substantial losses for the Gassled owners. More particularly, the Gassled owners will immediately be impacted as a result of the Ministry's request to delay the coming capacity booking round in Gassled until May 2013. Assumingly, the proposed substantial reduction in tariff levels may lead to massive bookings by qualified resource owners, extending far beyond what has been experienced in previous booking rounds.

The Ministry's rush to implement the proposed changes clearly cannot be explained by reference to resource optimization considerations, since none of the gas resources qualified for the May 2013 booking round require tariff reductions in order to be produced. In view of this, we strongly request the Ministry to postpone the implementation of the proposed tariff reductions, allowing for dialogue, information exchange and clarification of applicable legal restrictions, before any drastic and unilateral steps are taken. Infragas would welcome the opportunity to contribute constructively to a broad and inclusive process addressing specific alternatives to the Ministry's proposal, resource optimization on the NCS and the role of Gassled in this respect.

Yours sincerely,

A handwritten signature in black ink, appearing to read "Knud H. Nørve".

Knud H. Nørve
CEO
Infragas Norge AS