

Information Material

Trustee for Elsam's
sale of virtual capacity

November 2004

TRANSLATION

Table of contents

1. Background
2. Description of the trustee's duties
3. The competencies of the trustee etc.
4. Tender form
5. Time schedule and process for the submission of tenders
6. Particulars concerning the submission of tenders

1. Background

On 24 March this year, the Danish Competition Council (Konkurrencerådet) approved the merger between Elsam A/S and NESA A/S. The merger was approved in the light of a number of commitments, including a commitment undertaken by Elsam to sell virtual central power plant capacity (also referred to as "Virtual Power Plants" or VPP in short).

The production and sale of electricity in the wholesale market in Denmark – a summary

A vast majority of the Danish production of electricity stems from the large central power plants that are owned and operated by Elsam A/S (Jutland and Funen) and Energi E2 A/S (Zealand), respectively. A minor part of the production stems from decentralised heating and power plants and wind turbines of which Elsam and Energi E2 own a part. However, as a consequence of one of the commitments undertaken in connection with the merger, Elsam is in the process of selling its shares in all gas-fired district heating and power plants.

Denmark is connected to the Nordic electricity market via electricity cables to Sweden and Norway and to the German market via cables to Germany. At present Jutland/Funen and Zealand are not connected via electricity cables.

As a part of the liberalisation of the European electricity market, electricity may in principle be freely traded between the countries, and cable capacity constitutes the only limitation.

Electricity is traded either directly between the seller and the purchaser as longer term current contracts, the so-called "Over The Counter Contracts" or "OTC-Contracts" in short, or on the spot market via the Nordic Power Exchange, Nord Pool. A minor part is traded as regulating power and reserve capacity. In addition, financial electricity is traded.

Electricity traded on the Nord Pool Exchange is delivered the following day. The Nord Pool works in the way that the players in the various price areas make bids for a price/quantity curve (a supply curve for suppliers and a demand curve for the other players wishing to purchase electricity) to the exchange for each individual hour. These bids can only be observed by the exchange. After the deadline, i.e. at 12.00 noon every day, the exchange aggregates the various curves and sets the system price (the equilibrium price) according to which all "elspot" bought and sold will be settled, provided that the cables between the individual price areas do not constitute bottlenecks.

Germany has a similar exchange, the EEX.

TRANSLATION

Nord Pool reduces the price differences between the individual price areas by transmitting electricity through the cables from an area with low prices to an area with high prices. Thus, a bottleneck will arise in the event that cable capacity availability is insufficient to equalise the price differences. This will contribute to the creation of high prices in the importing area and low prices in the exporting area.

Nord Pool handles bottlenecks by splitting the market into independent “el-spot” price areas (the so-called market splitting mechanism).

In a situation where no bottlenecks exist between two or more of Nord Pool’s price areas, the price will be the same in all price areas (the system price).

Approximately half of all trade in electricity in the Nordic Countries takes place through the Nord Pool Power Exchange.

As regards the Nordic connections, 100% of the commercial capacity for spot trade is reserved via the exchange. This means that no bilateral physical trade can take place between the Nordic countries (Norway, Sweden, Finland and Denmark). At present, the German connections are not reserved for trading via an exchange.

The connection to Germany is more frequently limited by capacity problems than connections in the Nordic countries. At the same time the liquidity of the German exchange is slightly tighter than the liquidity of the Nordic Exchange due to the fact that the German market to a larger extent is characterised by long-term contracts.

Elsam’s VPP commitment – summary

In order to strengthen competition in relation to Elsam and Energi E2, Elsam undertook to sell an annual quantity of 600 MW central power plant capacity via auctions in a fair, open and non-discriminatory manner.

The first such auction will be held in the 4th quarter of 2005 with effect for the 1st quarter of 2006. Subsequently, 4 auctions will be held every year. The total quantity tendered in auction is to be gradually increased as follows:

- In 2006 a quantity of 250 MW will be tendered;
- In 2007 a quantity of 500 MW will be tendered; and
- In 2008 and the following years a quantity of 600 MW will be tendered annually.

Virtual capacity contracts with a duration of 3 months, 1 year and 3 years, respectively, will be tendered. A 100 MW contract with a duration of 1 year

TRANSLATION

thus entitles the buyer to have 100 MW produced in each of the relevant hours within a one-year period. However, during the first year (contracts with effect in 2006) only contracts with a duration of 3 months will be tendered.

2. Description of the trustee's duties

In general

In cooperation with Elsam and the Danish Competition Authority the Trustee undertakes a number of specific duties in order to create a well-functioning market for the sale by Elsam of virtual capacity. Solely the Competition Authority is empowered to instruct the trustee.

Elsam defrays all expenses in relation to the trustees and the practical realisation of the auctions, however, it is assumed that the trustee(s) appointed work(s) cost-effectively. The Competition Authority may from time to time give notice of termination to the trustees and after having consulted Elsam appoint new trustees.

In order for the trustee to fulfil its duties in the best way possible, principles for control and procedures for the development, implementation and holding of virtual auctions will be prepared shortly after the appointment of the trustee.

Steering group

In order to ensure that both Elsam and the Competition Authority are kept informed of and involved in all issues of significance, a steering group will be established in which Elsam and the Competition Authority participate.

The object of the steering group is to discuss and clarify problems during the entire process. A schedule of meetings in the steering group will not be established in advance, as the meeting dates will be fixed from one meeting to the next. The trustee participates in steering group meetings subject to agreement with the Competition Authority.

The Competition Authority has the final say as regards steering group decisions.

The trustee's duties

The overall duty of the trustee is to ensure that Elsam fulfils its commitment to sell 600 MW virtual capacity, see box 1 below.

Box 1: Extract of Elsam's commitment to sell virtual capacity

Elsam sells 600 MW virtual central heating and power plant capacity (virtual capacity) a year in order to allocate the supply of physical electricity to more ac-

TRANSLATION

tors. The commitment is not limited in time. Auctions take place in a fair, open and non-discriminatory manner.

Virtual capacity will be tendered for periods of 3 months, 1 year and 3 years and will be allocated at 4 annual auctions. The first auction will be held in the 4th quarter of 2005 with effect for the 1st quarter of 2006.

From 2006 (phase 1) a quantity of 250 MW will be tendered annually on 3-month contracts. From 2007 (phase 2) a quantity of 500 MW will be offered annually in respect of the products specified above. From 2008 (phase 3) a quantity of 600 MW will be offered annually in respect of the products specified above. The trustee distributes the various products with a view to meeting the following objectives, listed in order of priority:

1. to create a market for all products;
2. to ensure that the entire capacity tendered is sold; and
3. to ensure that the sale generates a reasonable contribution margin to Elsam in respect of the capacity sold.

The trustee may change the distribution between the various products if there turns out to be a special interest in particular products.

All participants must be approved by the Danish Competition Authority prior to each auction. The sale of virtual capacity can only be effected to purchasers that are Elsam's actual competitors. Unless a general requirement is introduced regarding the provision of security in the form of a bank guarantee in connection with the auctions, Elsam must be allowed the possibility to verify the creditworthiness of each participant. Elsam, Elsam's subsidiary, E2 or other of Elsam's associated companies or Elsam's owners (excluding owners with a minor individual shareholding) are not entitled to participate in the auction.

At the auction the participants bid on the capacity price, i.e. the price that the players are willing to pay for an option for production capacity. This constitutes payment for being able to draw on Elsam's power plants. There is no minimum capacity price.

The energy price is the price that has been fixed and disclosed in advance and that the players must pay for each MWh exercised under the option. The energy price corresponds to the marginal costs for Elsam's most cost-efficient power plant from time to time. The principles for calculating the marginal costs appear in Appendix 2 to the commitments. The parameters in Appendix 2 may be adjusted by the trustee if called for by specific circumstances, including market issues, production technologies or Elsam's costs. The calculations are made prior to each auction. Once the energy price has been fixed, it will not be modified during the option period. Prior to each auction, the price must be approved by the trustee appointed. In this connection the trustee must have access to all necessary material in order to be able to verify the calculations. In the event of dis-

TRANSLATION

agreement as regards the calculation of the relevant marginal cost, such amount will be fixed by the Danish Competition Authority.

The acquisition by each buyer of virtual capacity on the auction cannot exceed 50% of the capacity offered.

Buyers of virtual capacity must every day before 2:00 p.m. submit notification of the quantities required by them for following day (number of MW, hour by hour, with one 1 decimal). However, in the event that the quantities required differ from hour to hour with more than 40% of the capacity purchased at the auction, such notification must be given before 11:00 a.m. The aforesaid times must be altered in the event that Eltra or Nord Pool changes the times for submission of the daily notifications to them. Deliveries are made physically to the 150/400 kV grid in Western Denmark (Eltra).

Source: The Danish Competition Authority (March 2004) "The Merger between Elsam and NESAs", page 46f.

The trustee's two most important duties are in cooperation with Elsam and the Danish Competition Authority to develop the auction design and to monitor the entire development and implementation process. The trustee may decide to outsource the auction design to a third party. If the trustee chooses to do so, the party to whom the responsibility for designing the auction is given must be approved by the Competition Authority.

It should be noted that in the event of any doubt arising so as to the commitment, the wording of the original commitment applies.

Generally, the trustee must ensure that Elsam respects its commitment regarding the sale of virtual capacity. In this connection the trustee has the following duties:

1. The trustee prepares the principles for control and procedure for development, implementation and holding of virtual auctions and ensures that a realistic time schedule is set up.
2. The trustee ensures that all relevant legal documents are drafted, including for instance
 - qualification/registration of tenderers;
 - nomination of the winners of an auction; and
 - contracts with the winners of an auction ensuring reasonable terms of credit.
3. Following discussions with Elsam and the Competition Authority, the trustee prepares a proposal for an auction design including the design of

TRANSLATION

- auction rules; and
 - software to carry out the auction.
4. The trustee ensures that the auction is implemented and held in such a manner that contributes to the emergence of a well-functioning market for the options. This also includes preparing and placing at the disposal of all potential bidders all relevant information material.
 5. The trustee ensures that the auction is adapted to prevailing market conditions on a current basis.
 6. The trustee ensures that the energy price etc. is fixed correctly in the entire period.
 7. The trustee ensures that all relevant information is submitted to the Competition Authority.

Principles, procedures and time schedule

Initially the trustee shall ensure that a time schedule is prepared covering the entire process indicating the dates for the finalisation of each step of the process.

Another of the trustee's duties is to prepare principles for monitoring Elsam's performance of its commitment as well as procedures for the development, implementation and holding of the virtual auctions.

Legal documents

The trustee shall ensure that all relevant legal documents are prepared.

Among other things, the trustee shall prepare clear and unambiguous rules governing the requirements to be met by potential buyers in order to qualify as bidder on the auction.

In addition, clear and unambiguous directions so as to the identification of the winner of an auction must be available. The trustee must also ensure that standard contracts be prepared applying to the exercise of the option that a winner of an auction buys with its bid. The contracts must be drafted in an easily understandable language allowing others than the traditional players in the market to comprehend the terms of the contracts.

Auction design

Following discussions with Elsam and the Competition Authority, the trustee prepares a proposal for an auction design. Following negotiations with the Competition Authority and Elsam, the auction design will be chosen; the Competition Authority has the final say as regards auction design.

The auctions shall be designed in such a manner that they first and foremost ensure the sale of the full virtual capacity, provided that no single purchaser

TRANSLATION

acquires in excess of 50% of the capacity offered. Thus, in 2006 no purchaser can acquire in excess of 125 MW, in 2007 no one can acquire in excess of 250 MW, and as from 2008 no one can acquire in excess of 300 MW.

Furthermore, the trustee must ensure that software for carrying through the auction be developed or acquired. Such software must allow for the carrying out of a web-based auction in such a way that all potential bidders can participate in the auction via the internet.

In connection with the proposal for auction design, the following issues must be considered:

- The quantities in MW to be tendered.
- The distribution of 3-month, 1-year and 3-year contracts from 2007. The distribution shall be effected with a view to creating a well-functioning market.
- The most expedient form of auction (e.g. closed/open, first bid/second bid)
- Process for the auction (submission of bids – how, when and in what form).

The implementation and holding of the auction

Well in advance of the first auction, the trustee will prepare information material informing potential bidders of all relevant aspects of the auction.

The trustee must also ensure that the auction concerning the virtual capacity is efficiently held.

Moreover, the trustee must ensure smooth completion of all relevant contractual issues, including procedure for the contracting party's notification of the quantity of virtual capacity required as well as issues regarding delivery, payment, etc.

Adapting the auction to the market

From 2007 three different kinds of contracts will be offered, i.e. 3-month contracts, 1-year contracts and 3-year contracts. No decision has as of yet been made with regard to the individual distribution between the three kinds of contracts.

The distribution between 3-month contracts, 1-year contracts and 3-year contracts shall be made with a view to meeting the following objectives listed in order of priority:

1. to create a market for all products;
2. to ensure that the entire capacity tendered is sold; and

TRANSLATION

3. to ensure that the sale generates a reasonable contribution margin to Elsam for the capacity sold.

The trustee can on a current basis ensure that the distribution between the three kinds of contracts is carried out in an efficient manner.

The trustee shall ensure that the contracts/options are completed satisfactorily. Any omission to use the option shall give rise to considerations of a different composition of 3-month contracts, 1-year contracts and 3-year contracts as well as a reconsideration of the form of auction.

Supervise the parameters in the energy price formula etc.*Energy price*

The buyers of the virtual capacity must pay (in addition to the capacity price/the option price) for the quantity of electricity they require to be produced. Such payment is effected at the so-called energy price. The energy price is thus the so-called strike price for the option. The energy price is known and constant throughout the entire term of the option.

The energy price is a price fixed and disclosed in advance that the players must pay for each MWh exercised of the virtual capacity. The energy price corresponds to the marginal costs on Elsam's most efficient power plant from time to time.

The principles for calculating the energy price/marginal costs are listed in Appendix 2 to the commitments made by Elsam. The parameters in the energy price/marginal costs formula can be adjusted by the trustee if called for by specific circumstances. For instance, the forward price for coal and CO₂ is included in the formula. As regards the CO₂ price in particular it must be defined which price is to apply

Price formulae

In connection with the development of the auction design it may turn out that the most advantageous solution is simultaneous auctions, i.e. to hold auctions simultaneously as regards the options for contracts with a duration of three months, one year and three years, respectively.

In the event that the auction design chosen is simultaneous auctions, the connection between the price of an option for a 3-month contract, the price of an option for a 1-year contract and the price of an option for a 3-year contract must be fixed. In this case the trustee must ensure an appropriate connection between the prices for the various options, i.e. currently revise and optimise the price formulae.

Information and cooperation

The trustee will ensure that the Competition Authority receives all relevant information.

TRANSLATION

Furthermore, the trustee will be working closely with the steering group. Particularly in the initial phase, a number of important decisions will have to be made involving the steering group, e.g. decision regarding auction form.

By the end of 2007, the trustee must prepare a report to the steering group concerning advantages and disadvantages in the auction design and the sale of options for virtual capacity as well as the exercise of the options. The report must include potential proposals for improving the situation surrounding Elsam's sale of virtual capacity.

3. The competencies of the trustee etc.

In order for a tenderer to be considered as trustee, the tenderer must be able to demonstrate its independence from Elsam. Independence from Elsam will among other things be established by the setting up of so-called "Chinese Walls" in the tenderer's company.

In the selection process particular emphasis will be placed on the trustee possessing various competencies guaranteeing the trustee's capability to solve the assignment efficiently and with the highest possible objectivity.

Also, in the selection process importance will be attached to the following competencies:

- The trustee has good experience with conditions in the Danish and the Nordic electricity market.
- The trustee has in-depth knowledge of design, implementation and holding of auctions.
- The trustee works cost-effectively.
- The trustee has experience with financial products, particularly options.
- The trustee is in a position to use significant resources whenever required.

The assignment will be given to the tenderer that possesses the best possible overall competencies and that has an understanding of and insight into the contents and character of the work.

4. Tender form

The tenderer shall supply the following information when submitting the tender:

TRANSLATION

- Name, address, telephone and fax numbers as well as e-mail address and name of contact person with the tenderer.
- List of all employees that will participate in solving the assignment, such employees' CVs and their actual role in solving the assignment.
- Name of any cooperation partners that the tenderer intends to involve in the solving of the assignment, information of which assignments such cooperation partners are to solve as well as the names and CVs of any contact persons. Commitment documents from any such cooperation partners should be enclosed.
- The tendered hourly rate as well as a noncommittal estimate of the total number of hours to be used.
- A description of the tenderer's understanding of the assignment, including an account of the competencies in accordance with the section, "The trustees' competencies", including an account of the trustee's independence from Elsam.
- Preferably, a draft contract should be submitted together with the tender.

5. Time schedule and process for the submission of tenders

An information meeting will be held for all interested tenderers on 19 November, at 10:00 a.m., at the offices of the Competition Authority in Nyropsgade 30, DK-1780 Copenhagen V, Denmark. At the meeting both the Competition Authority and Elsam will supply information as to the nature of the assignment. Questions as to the position of trustee are welcome.

Additional information can be obtained from Carsten Smidt in the Competition Authority (CS@KS.DK, tel. +45 72 26 81 73) and Leif Winum in Elsam (LWI@ELSAM.COM, tel. +45 76 22 23 10).

The tender must reach Elsam on 6 December 2004 at the latest. The tender must be submitted to: Elsam, Overgade 45, Skærbæk, DK-7000 Fredericia, Denmark, Attn.: Leif Winum. A copy of the tender must be forwarded to the Competition Authority, Nyropsgade 30, DK-1780 Copenhagen V, Denmark, Attn.: Carsten Smidt.

By 17 December it will be decided which of the tenderers will be selected to fulfil the position of trustee. The tenderer will receive notification by letter.

TRANSLATION

The tenderer must maintain its tender until 21 December 2004.

All rights are reserved to alter the dates indicated.

6. Particulars concerning the submission of tenders

Submission of tender

The tender must be submitted in Danish or English in six copies. Elsam and the Competition Authority shall each receive three copies. The tenderer bears all costs relating to the preparation of the tender.

Cancellation

All rights are reserved to cancel the call for tender in the event that no qualified tenders are received or if any unforeseen events should arise impeding the call for tender.

Processing the tenders

The tenderers must be willing to give an oral presentation of their tender.

The tenderers shall not discuss their tender with any unauthorised persons, including competitors. Furthermore, the tenderers shall not supply information to unauthorised persons in respect of matters of which the tenderer may gain knowledge in connection with this call for tender process.

The tenderers will not be entitled to be present at the opening of tenders nor to receive information of the tenders submitted by competitors.

Selecting the trustee

Once the tender has been submitted, the Competition Authority and Elsam reserve the right freely to contact one or more tenderers with a view to clarifying any question of doubt or alteration before an agreement is entered.

The tender submitted must be prepared in such a way that the selection of trustee in principle can take place without any prior discussions between the tenderer and Elsam/The Competition Authority. Thus, the tenders must address all relevant issues, contain all necessary information and be accurate in all respects.

The trustee is selected on the basis of the criteria described in the section captioned "The trustees' competencies". The trustee is selected following discussions between Elsam and the Competition Authority of the tenders received. In the event of any disagreement between Elsam and the Competition Authority regarding the selection of a trustee, the Competition Authority has the final say.

Contractual issues

TRANSLATION

The final agreement is regarded as having been concluded once a contract has been signed by Elsam and the tenderer, subject to the Competition Authority's approval.

The trustee prepares a draft contract that must be approved by the Competition Authority after discussions with Elsam. The draft contract is prepared immediately after the tenderer has received notification that Elsam – with the Competition Authority's acceptance – wishes to appoint the tenderer as trustee.

The trustee commences fulfilling its duties as trustee immediately after the contract has been approved by the Competition Authority and signed by Elsam and the tenderer. Costs relating to the trustee are defrayed by Elsam.

The term of the trustee position runs until 31 March 2008.