



Escondido Gas Storage, LLC

A Torch Energy Company

ESCONDIDO PROJECT SUMMARY

Introduction

Escondido Gas Storage, LLC (Escondido) announced a non-binding open season beginning January 9 for its Escondido Gas Storage Project (the Escondido Project, the Project) under development in the depleted Atkinson Gas Reservoir southeast of San Antonio, Texas in Live Oak and Karnes counties. The facility design includes 18 Bcf of working gas capacity with an injection rate of 275,000 Mcf/d and a withdrawal rate of 335,000 Mcf/d, allowing for 3 to 4 cycles per year. Based on market demand, the Escondido Project's capacity could be expanded. The Escondido Project is projected to be in service for the 2010 injection season

Ownership Structure

Escondido is owned by Torch Energy Advisors, Incorporated and will be developed by Torch Energy Services, Inc.

Torch Energy Advisors, Incorporated is a privately held, Houston-based energy company. Founded in 1981, Torch has a long history of owning, operating and maximizing value from large energy-related projects. During its twenty-five year history, Torch has been directly responsible for the investment and management of over \$3 billion in energy assets.

Torch Energy Services, Inc., a wholly owned subsidiary of Torch Energy Advisors, Incorporated, is experienced in midstream and greenfield project development, and currently operates both upstream and midstream assets.

Escondido Storage Project – Facilities

The Escondido Project will be a state-of-the-art gas storage facility consisting of compression, dehydration and bi-directional meters. The Project is approved for development by the Texas Railroad Commission (TRC) and is soliciting interest from multiple market sources. Potential pipeline connections include CPS Energy, Enterprise Texas Pipeline LLC, Gulf South Pipeline Company, Houston Pipe Line Company LP, Kinder Morgan Texas Pipeline LLC and Transcontinental Gas Pipe Line Corporation (Transco). Depending on customer requirements, Escondido may also offer interruptible hub service on its header system and additional pipeline connections. Escondido will offer intrastate storage services pursuant to the rules and regulations of the TRC. Pending the results of the open season, Escondido may also file a Section 311 Application with the Federal Energy Regulatory Commission to provide firm and interruptible storage service and interruptible hub services to interstate markets.

Project Location

The Escondido Project will be located in south central Texas, approximately 65 miles north of the Aqua Dulce production hub in Nueces County. The Agua Dulce hub is connected to at least two pipelines that could be connected to the Escondido Project header system; the Project will be the nearest storage facility to that hub.

Through its potential pipeline connections, the Project will access market and production hubs in Texas, along the gulf coast, and into the midwest and eastern United States. The Escondido Project is ideally situated to mitigate transportation and storage constraints that will occur as new gulf coast LNG terminals become operational. Further, the counties surrounding the Project are home to 27 gas-fired electric generating plants, most of which are served by one or more of the pipelines accessible to the Escondido Project.

Industry Overview

The North American natural gas industry is segmented into distinct businesses along a value chain that begins upstream with a large number of natural gas producers at the wellhead and ends downstream with the end user. Gas production facilities are connected to intrastate and interstate gas pipelines delivering gas into local distribution systems or end users. In addition to gas production facilities, the gas supply chain also includes imports delivered into LNG terminals. There are currently five LNG terminals in various stages of development along the Texas gulf coast.

From the gas distribution system, gas is delivered to a diverse range of natural gas consumers, including residential, commercial, industrial and power generation concerns. Natural gas storage facilities balance supply and demand across the value chain. Specifically, gas storage provides supply reliability and peak day demand coverage without unnecessary investment in excess natural gas production, processing, transmission and distribution capacity. Gas storage also serves as a physical hedge against supply disruptions and gas price volatility. Currently there are an estimated 440 underground natural gas storage facilities in North America, about 40 of which are in Texas.

Natural Gas Storage

Underground storage is a critical component of the U.S. natural gas supply chain. Storage facilities like the Escondido Project provide a source of physical natural gas to balance relatively flat production and weather-driven, highly seasonal natural gas demand. There are three conventional types of underground storage facilities: depleted reservoirs, aquifers and salt caverns. Reservoir storage facilities are most common. They are located throughout the U.S. and comprise the largest share of working gas capacity.

Underground natural gas storage facilities such as the Escondido Project provide the most cost effective means of controlling natural gas demand volatility. Without gas storage, natural gas production, processing, transmission and distribution systems would need to be oversized to meet demand peaks; they would be greatly underutilized at all other times. In addition, producers would be forced to curtail production except during periods of high market

demand. Analysis of recent natural gas market behavior concludes that current North American natural gas storage capacity is constrained in its ability to meet demand and must undergo significant expansion to meet growing needs.

Most of the existing gas storage facilities were developed between 1955 and the early 1980's, responding to the overall growth in natural gas consumption, in particular the growth in seasonal demand from the residential and commercial sectors. Evidence confirms that demand on natural gas storage is exceeding current gas storage capabilities creating strong interest in new facilities. Natural gas price behavior shows that current levels of storage injection and withdrawal capacity is a constraining factor -- commodity prices soften considerably at storage limits, indicating limited capacity to absorb incremental production. Prices typically peak at the end of the withdrawal season, indicating limited ability to supply more natural gas into the market.

Short-term natural gas commodity prices currently exhibit great volatility; this trend is projected to continue into the future. The extrinsic value of storage reflects a facility's ability to capture the option value inherent in the operating capabilities of various gas storage facilities relative to the degree of short-term price volatility. A storage facility with greater physical and operational capabilities, typically multi-cycle facilities like the Escondido Project, can offer the capacity holder greater ability to capture extrinsic value.

Conclusion

The Escondido Project, an 18 Bcf facility capable of 3 to 4 turns per year, is poised to provide the market with strategic additional storage. It will provide a cost effective way to balance seasonal supply and demand and a physical hedge against supply disruptions and price volatility. With access to multiple interstate and intrastate pipelines, the Escondido Project's state-of-the-art facility will provide its natural gas customers supply stability and market opportunity.