

ASX AND MEDIA RELEASE

SIGNING HEADS OF AGREEMENT WITH THE A J LUCAS GROUP AND APPOINTMENT OF CHIEF EXECUTIVE OFFICER

14 January 2008

Sydney Gas Ltd ("Sydney Gas") has today signed heads of agreement with the A J Lucas Group Limited ("Hheads of Agreement") ("Lucas") and intends to appoint Andy Lukas as the new Chief Executive Officer of Sydney Gas.

The transaction has the following key benefits to Sydney Gas:

1. Access to leading management, personnel, and drilling resources in the coal seam methane gas industry with transparent alignment of interests through equity investment and performance based incentives.
2. Up to A\$47.2 million of additional equity capital available for accelerated exploration and development.
3. A new Chief Executive Officer and a new non-executive director, with in-depth coal seam methane gas industry experience.

A meeting of Sydney Gas shareholders will be held in March 2008 to approve key elements of the arrangements.

Heads of Agreement

Under the Heads of Agreement, Lucas will make available drilling and technical resources as required by Sydney Gas to accelerate the development of its gas assets and provide A\$20.0 million upfront, and an additional A\$27.2 million in total over 3 years, of exploration and development capital via taking a 15% shareholding in Sydney Gas, as well as options that could upon their exercise, subject to shareholder approval, over 3 years, increase its shareholding by 40.25 million shares.

There are four key elements under the Heads of Agreement:

1. Upfront capital raising of A\$20.0 million via a private placement to Lucas.
2. Provision of dedicated expert technical services by Lucas.
3. Incentive arrangements to create clear alignment of interests between Sydney Gas shareholder value and Lucas.
4. Raising an additional A\$12.1 million and A\$15.1 million of development capital via exercise of two tranches of performance-linked options which may be exercised:
 - (a) in approximately 2 years time and 3 years time, respectively; and
 - (b) upon Sydney Gas achieving an increase of its 2P reserves by at least 75PJ and 150PJ, respectively, and an increase in its share price to at least 60 cents and at least 75 cents, respectively.

The transaction is structured to create an alignment of interests between Sydney Gas and Lucas by ensuring that Lucas will provide rigs and technical expertise on transparent and competitive terms and share in the upside created through its shareholding and options.

1) Upfront placement

Lucas will subscribe for a placement of approximately 52.5 million Sydney Gas shares (equivalent to 15% of the SGL shares currently on issue) at a price of 38 cents per share, raising \$20.0 million for Sydney Gas and subject to the parties entering into a Technical Services Agreement and Drilling Services Agreement, outlined below.

As part of the arrangements, Allan Campbell, the Executive Chairman of Lucas, will be appointed to the Sydney Gas Board.

2) Provision of dedicated expert technical services

It is expected that Sydney Gas and AJ Lucas Operations Pty Limited ("Lucas Operations") will enter into a Technical Services Agreement and a Drilling Services Agreement. Term sheets have been agreed, subject to full documentation and to compliance with the terms of the joint venture agreements with AGL Energy Limited.

The Technical Services Agreement and Drilling Services Agreement will oblige Lucas to make available drilling and technical resources as required by Sydney Gas. Such resources include, but are not limited to, two fully manned rigs for a period of up to 2 years (to add to the one rig Sydney Gas and AGL have operating in Camden, bring total number of rigs under operation to three), experienced drilling personnel to operate the rigs, and specialist coal seam gas expertise to assist in evaluating and developing the gas assets.

3 & 4) Incentives and additional development capital

In order to incentivise Lucas and further strengthen the alignment of interests between Lucas and Sydney Gas, Sydney Gas will grant options to issue 40.25 million shares to Lucas. There will be two tranches of options, each being 20.125 million shares (equating to approximately 5% of the SGL shares on issue following the placement):

- the first tranche of options will have an exercise price of 60 cents and will be exercisable upon the earlier of 2 years after their issue (i.e., expected to be exercisable after March 2010) or upon an increase in the 2P reserves of Sydney Gas of at least 75PJ from today's level and an increase in Sydney Gas' share price to at least 60 cents.
- the second tranche of options will have an exercise price of 75 cents and will be exercisable upon the earlier of 3 years after their issue (i.e., expected to be exercisable after March 2011) or upon an increase in the 2P reserves of Sydney Gas of at least 150PJ from today's level and an increase in Sydney Gas' share price to at least 75 cents.

The options may be exercised earlier under certain trigger events. If Lucas exercises the options, Sydney Gas will have raised an additional \$27.2 million of equity capital.

The Heads of Agreement calls for detailed documentation to be negotiated and signed by the end of January 2008. A meeting of Sydney Gas shareholders will be held in March 2008 to approve key elements of the arrangements.

Appointment of Chief Executive Officer

Further to the Heads of Agreement, subject to the placement of Sydney Gas shares, Andy Lukas will resign from his Company Technical Director position with Lucas and take up the Chief Executive Officer position of Sydney Gas.

Andy has over thirty years experience in the pipeline and drilling industry across the USA and South East Asia. He pioneered the development of Horizontal Directional Drilling (HDD) in 1990 (HDD is the basic technique behind the surface-to-inseam drilling technology (SIS)), commencing operation of Australia's first rigs and then developed SIS to enable safe coal seam methane extraction for coal and gas producers. He has been instrumental in developing Lucas to its present position as a world market leader in this specialised field and the largest coal seam degasification company in Australia. Andy is recognised as Australia's leading authority on HDD and SIS technologies which are expected to be widely adopted in developing Sydney Gas' gas assets.

Dr John Saunders, the Executive Chairman of Sydney Gas, said "Today's agreements are key steps in the development of Sydney Gas. We have potentially great resources in Camden and the Hunter and the involvement of Lucas, which has an outstanding record in coal seam gas, will provide the expertise and support that we need to make Sydney Gas the success that it deserves to be".

Allan Campbell, the Executive Chairman of Lucas, said "We are delighted to strengthen our ties with Sydney Gas and to assist further in the commercialisation of its coal seam gas. We are already drilling at Camden where we have significantly increased gas production assets since we commenced our involvement. We believe that our participation in the Hunter Project can add further significant value. We look forward to working with Sydney Gas in the further exploration and development of the Sydney Basin."

About Sydney Gas Ltd

Sydney Gas Ltd is an Australian energy company listed on the Australian Stock Exchange Ltd (ASX code: SGL). SGL sold 50% of its assets to AGL in 2005 and has entered into a Joint Venture (JV) with AGL for the development of its tenements. SGL and AGL Gas Development have entered into a Gas Sales Agreement with AGL Wholesale Gas Limited for 10 years with an option to renew for a further period of 4 years. Under the Gas Sales Agreement, the JV is to deliver up to 14.5 PJ per annum to AGL Wholesale Limited from 2008, thereby becoming a major producer of gas for the growing New South Wales (NSW) market. The JV is currently completing Stage II of the Camden Gas Project and it is continuing to refine its existing completion techniques to ensure that the minimum surface footprint for its activities occurs. The Hunter Gas Project is currently in the planning and appraisal stage with the drilling of coreholes and seismic acquisition programs being the current focus of its exploration activity in the area taking fully into account technical, environmental and social benefits – cost considerations.

About A J Lucas Group Limited

Lucas is the market leader in Australia in drilling and coal seam gas services. Lucas staff have been actively involved in coal seam degasification projects in all the coalfields of Australia and overseas in China, India and North America. Lucas pioneered horizontal drilling applications in the Australian civil engineering and pipeline industry and today holds many world records. Lucas has been applying this expertise to the challenge of surface-based coal seam degasification and surface to in-seam coal bed methane

extraction. Lucas has developed equipment and systems that enable gas to be extracted from the coal with long drainage times for effective degasification. Lucas currently owns and operates 52 rigs in the Bowen Basin, Hunter Valley, Camden and Gunnedah Basin and has developed proven world class proprietary gas drainage, HDD technology and innovative drilling techniques, including:

- Longest SIS holes in Australia
- Deepest successful SIS holes in Australia
- Engineering and design approach to decrease \$/GJ development costs

Lucas has in-depth knowledge of Sydney Gas' assets through providing drilling services to the Sydney Gas / AGL joint venture in Camden and providing coal seam degasification services to coal mining companies in the Hunter area.

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