



MEMORANDUM

TO: RAE McQUADE, GISB
FROM: MARCIA GREENBLATT
SUBJECT: GISB STANDARD 6.3.1
DATE: 12/11/01

Sempra Energy Trading Corp. has reviewed the proposed new GISB Base Contract for the Sale and Purchase of Natural Gas and the General Terms and Conditions.

We approve of GISB having one agreement for both short term and long term Transactions. We also approve of the Canadian addendum. However, in reviewing the contract as a whole we have certain comments.

1. Texas Law Default.

We strenuously believe that, although many of the participants in GISB are from Texas, this is not an appropriate selection for the type of Transactions contemplated by the GISB Contract. We believe that either there should be no default provision, as it was in the prior agreement, or the default be New York. We favor New York law for the following reasons:

a) Consistency with Power and Financial Transactions. Both the EEI Master Agreement, which is fast becoming the industry standard form of agreement for power agreements, and the ISDA Agreement, which is the industry standard for financial transactions, are both governed by New York law.

b) New York law is commercially reasonable. For participants selecting Oral Transaction Procedures, it is important that the applicable law recognize such procedure as legally binding. Unlike other states, New York specifically provides that such Transactions are binding. New York has amended their version of the Uniform Commercial Code, that provides that all oral agreements for qualified financial transactions, which includes both physical commodity transactions and derivatives, are legally binding. All that is required is some proof of the transaction. Additionally, New York has a large body of case law interpreting commodities contracts.

c) A nexus with New York is not required. Under the New York General Obligations Law, the parties to a contract with a total consideration of not less than \$250,000 may agree that New York law will govern. In today's market it is unlikely that any contract for the purchase and sale of any commodity would be less than the threshold.

We acknowledge that Texas law is only an option. However, by having this as a default, will make negotiations needlessly difficult, even though these same counterparts select New York for both power transactions and financial transactions. Accordingly, we request that GISB either have no default choice of law or change it to New York.

2. Payment of Non-performance Damages.

Neither the new version nor the prior version of the GISB states when non-performance damages under Section 3 will be paid. Although we favor an accelerated payment due date for these damages, we approve of the EEI method of having an option for when these will be paid.

3. Netting.

We approve of the netting provision in the new version of the GISB. However, we believe the words “on the same day” should be added after the words “due and owing” on the second line. Non-performance damages could be due on a date other than the payment due date, and would not be netted with normal payment.

4. Forward Contract Damages.

We believe that this provision would have been strengthened if it also provided that all Transactions entered into by the parties will be deemed to be one integrated contract.

Additionally, we were truly perplexed by the option of having no Forward Contract damages, and can think of no situation where a party would reasonably want to opt out of the Forward Contract Damages provision. As evidenced by the recent bankruptcy of Enron, even the biggest can fall. Although this is only an option, we are concerned that by requiring parties to make an election, we are creating a point of negotiation where none should exist. As such, we strongly believe that the option should be deleted, and any individual company that wishes to delete this provision do so in its Special Provisions.

5. Credit Assurances

Although physical Transactions had traditionally been entered into on an open credit basis, this is not true any more. On the power side, the EEI, for example, contains margining provisions and increasingly counterparts are seeking comparable protections under physical gas agreements as well. We propose that GISB consider a standard addendum governing margin.