

FOR SETTLEMENT PURPOSES ONLY

PURSUANT TO FEDERAL RULE OF EVIDENCE 408

Term Sheet for Settlement of Tax Sharing Agreement Issues

- I. This term sheet shall reflect the terms of a settlement among National Energy & Gas Transmission, Inc. (“NEGT”), NEGTEnterprises, Inc. (“Enterprises”), National Energy Holdings Corporation (“Holdings Corporation”), NEGTEnergy Company, LLC (“NEGT Energy”), National Energy Generating Company, LLC (“NEGT Generating”), USGen New England, Inc. (“USGenNE”) and the Official Committee of Unsecured Creditors of USGen New England, Inc. (“Official Committee”).
- II. USGenNE agrees:
  - A. to provide NEGTEnergy Company, LLC with a properly executed IRS Form 1122 no later than June 16, 2004, pursuant to which USGenNE and all subsidiaries of USGenNE agree to join the consolidated federal income tax return filing group of which NEGTEnergy Company, LLC will be the common parent, which group shall come into existence upon the deconsolidation of NEGTEnergy Company, LLC and USGenNE from PG&E Corporation (“PG&E”),
  - B. to undertake any other actions reasonably requested by NEGTEnergy Company, LLC to cause USGenNE and such subsidiaries to join in such consolidated group, and
  - C. not to take any action which would cause USGenNE and such subsidiaries to fail to join or continue as a member of such consolidated group; provided, however, that (i) the agreement shall not prevent the cancellation of USGenNE’s existing common stock pursuant to the consummation of a confirmed bankruptcy plan and (ii) NEGTEnergy Company, LLC hereby agrees to cause all of the members of its affiliated group to consent to a deconsolidation of USGenNE immediately following the consummation of USGenNE’s bankruptcy plan (the “USGenNE Plan”) in the event that such Plan provides that USGenNE will continue to operate on a stand-alone basis, and retain all or substantially all of its assets.
- III. NEGTEnergy Company, LLC agrees to make the following payments to USGenNE. The payments shall not be conditioned on recovery of tax sharing payments by NEGTEnergy Company, LLC from PG&E Corporation.
  - A. For the tax year ending December 31, 2003, and the partial tax year ending upon the deconsolidation during 2004 of NEGTEnergy Company, LLC and USGenNE from PG&E (together, the “Agreement Period”):
    1. to the extent USGenNE generates or has generated net operating losses on a stand-alone basis during the Agreement Period that, in the aggregate, do not exceed the sum of \$113,124,475, then NEGTEnergy Company, LLC shall pay to USGenNE an amount equal to 35% thereof, provided, however, that such amount paid to USGenNE pursuant to this paragraph shall not exceed \$33,835,279;

2. to the extent USGenNE generates or has generated aggregate net operating losses on a stand-alone basis during the Agreement Period above \$113,124,475, then NEGT shall pay to USGenNE an amount equal to 35% of NEGT's tax savings that result from the use of such excess losses, provided, however, that NEGT shall be deemed to use losses available from all other members of its group (and NEGT itself) prior to its use of any USGenNE losses (i.e., the USGenNE losses shall be considered used on a "last loss" basis); and
  3. to the extent USGenNE generates or has generated net taxable income on a stand-alone basis during the Agreement Period, no amounts shall be paid pursuant to paragraphs A.1 and A.2 above, and USGenNE shall pay NEGT an amount equal to 35% thereof, plus the amount of any additional consolidated, unitary and combined state and local income tax liability actually payable by NEGT as a result of its ownership of USGenNE.
- B. For all subsequent tax years during which USGenNE remains a member of the consolidated group of which NEGT is the common parent:
1. to the extent USGenNE generates a net operating loss on a stand-alone basis, and the consolidated group of which NEGT is the common parent actually realizes a benefit from such loss, applied on a "last loss" basis, consistent with III.A.2, then NEGT shall pay to USGenNE an amount equal to 35% of NEGT's tax savings that are deemed to result from the use of such loss; and
  2. to the extent USGenNE generates taxable income on a stand-alone basis, then USGenNE shall pay to NEGT an amount equal to 35% thereof, plus the amount of any additional consolidated, unitary and combined state and local income tax liability actually payable by NEGT as a result of its ownership of USGenNE.
- C.
1. To the extent that (i) USGenNE has generated positive taxable income and incurred liability pursuant to III.A.3 and/or III.B.2, and (ii) in a later period USGenNE generates a taxable loss which, on a stand-alone basis, it could carry back against the income referred to in (i), then the amount due under III.B.1 shall be determined (x) without reference to the "last loss" limitation contained therein and (y) with regard to the actual federal, state and local tax refunds USGenNE could have obtained in respect of such loss, rather than the 35% amount referred to in III.B.1.
  2. If any loss for which USGenNE receives compensation under paragraph III.A.1, III.A.2 or III.B.1 above is used to offset USGenNE taxable income on a stand-alone basis in a future tax year, then USGenNE shall pay to NEGT the amount received pursuant to such paragraph (as applicable) on account of such loss.

- D. NEGТ shall provide reasonable protection as reasonably agreed upon by the Board of Directors of USGenNE for amounts due pursuant to III.B.1, limited, however, to \$33,835,279 (less any amounts paid pursuant to III.A.1) plus additional amounts paid by USGenNE under III.A.3 (but only from the time of payment in the case of the additional amounts); provided, however, that to the extent the parties cannot agree by July 15, 2004, the bankruptcy court shall determine what constitutes reasonable protection.
- E. In the event that as a result of the consummation of NEGТ's Modified Third Amended Plan of Reorganization confirmed by the Bankruptcy Court by order dated May 2, 2004, the basis of USGenNE's assets is reduced pursuant to Treas. Reg. §1.1502-28T by more than the Target Amount (hereafter defined), the amounts payable to NEGТ under III.B.2 shall be limited to the amount that would be payable if the attribute reduction were limited to the Target Amount. The Target Amount shall mean the lesser of (i) \$300 million or (ii) 120% of the amount that NEGТ determines in good faith as the USGenNE asset basis reduction pursuant to such regulation within 20 days of the date hereof.
- F. To the extent an audit by a taxing authority results in an adjustment to the items upon which the payments are based, the parties shall make corresponding adjustments to the amounts payable pursuant to the settlement agreement; provided, however, that (i) NEGТ shall make a reasonable effort to defend against any such proposed adjustment which relates to the utilization of USGenNE's tax attributes, and (ii) to the extent that the adjustments relate to tax positions taken in respect of USGenNE, NEGТ shall inform and consult with USGenNE and reasonably consider their views in defending any tax audit or controversy in connection therewith; provided, that NEGТ shall alone have the right to determine the strategy in the conduct of such audit, and the basis upon which to settle with the taxing authorities.
- IV. The Official Committee, USGenNE, NEGТ, Enterprises, Holdings Corporation, NEGТ Energy, and NEGТ Generating agree that the existing tax sharing agreements shall be terminated, and except as herein provided, no amounts shall be paid or payable pursuant thereto, or in respect of tax benefits and obligations of the parties.
- V. USGenNE and the Official Committee agree that they shall not seek the entry of an order restricting NEGТ from claiming a worthless stock deduction for its shares in USGenNE by reason of the restriction in IRC §382(g)(4)(D), and will actively oppose any effort by any other person to obtain such an order, provided, that, to the extent that the worthless stock deduction causes the limitation in whole or part of any tax attributes (including, without limitation, net operating less carryovers under IRC §382) of USGenNE, then NEGТ shall indemnify and hold USGenNE harmless against the loss of any such tax attributes to the extent that USGenNE can reasonably demonstrate that such attributes would have been usable by it but for such limitation, and any calculations required under the terms of this agreement shall be made without regard to any such limitations.

- VI. The parties hereby agree that if USGenNE deconsolidates from the NEGТ consolidated federal income tax group as a result of the consummation of a USGen Plan pursuant to which USGenNE expects to operate on a stand-alone basis, the deductions generated by USGenNE on the effective date of the USGen Plan (“Effective Date”) and the issuance by USGenNE of consideration to creditors in connection therewith (other than amounts necessary to pay administration expenses) will be allocated to the portion of the Effective Date prior the deconsolidation. Therefore, such deductions shall belong exclusively to NEGТ and shall be consistently treated by USGenNE and the NEGТ consolidated federal income tax group as arising on the Effective Date, while USGenNE is a member of the NEGТ consolidated federal income tax group, pursuant to Treasury Regulation § 1.1502-76(b)(1)(ii)(A)(I).
- VII. USGenNE undertakes to use its best efforts to assure that to the maximum extent practicable all payments made in connection with such Plan will be so deductible. USGenNE shall reasonably consult with NEGТ and its advisors in furtherance of the foregoing.
- VIII. This term sheet shall be subject to bankruptcy court approval in both the USGenNE bankruptcy case and the NEGТ bankruptcy case and shall be incorporated in and be part of the plan confirmed in the USGenNE bankruptcy case. The bankruptcy court shall retain jurisdiction over the subject matter of this term sheet.
- IX. Except as otherwise provided, payments hereunder shall be due 3 business days prior to the date that the payment to the relevant taxing authority is due, whether as a payment of estimated tax, or a final payment of tax. In the case of an amount due by reason of a carryback, the payment shall be due 3 business days following the date that the refund is received, or the refund is obtained by offset or credit against other amounts due. The parties shall cooperate reasonably in the preparation and filing of tax returns, the determination of taxes due and the conduct of any audit or tax proceeding. Information shall be made available in sufficient time to permit timely computations of tax due, timely completion of tax returns and otherwise as reasonably requested, including in connection with any tax proceeding. Notwithstanding the foregoing, payment pursuant to III.A. shall be made only after income or loss for the Agreement Period has been determined. NEGТ shall make such computation within 180 days following the close of the Agreement Period. Payments hereunder that are not made when due shall bear interest at the short term applicable federal rate under IRC § 1274(d).
- X. This term sheet shall be governed by the internal laws of New York. This term sheet shall, when approved by court order in the bankruptcy cases, be binding on the parties and their respective successors and assigns, provided, that neither party shall have the right to assign its rights or obligations hereunder.

- XI. The agreement reflected by this term sheet shall remain in effect through December 31, 2006. Following such date, neither party shall have any obligation to the other as a result of such agreement, provided, that, III.C. and IX. shall remain in effect. If, following December 31, 2006, NEGТ and USGenNE remain as members of an affiliated group filing consolidated tax returns the parties shall endeavor to enter into a further tax sharing agreement.