JMBM | Jeffer Mangels Butler & Marmaro LLP

Benjamin M. Reznik
BMR@jmbm.com

1900 Avenue of the Stars, 7th Floor
Los Angeles, California 90067-4308
(310) 203-8080 (310) 203-0567 Fax
www.jmbm.com

Ref:
62753-0001

August 22, 2005

VIA FAX (562) 436-1579 and OVERNIGHT MAIL

Robert Shannon, Esq.
City Attorney
City of Long Beach
333 West Ocean Blvd., #1100
Long Beach California 90802-4664

Re: Sound Energy Solutions LNG Import Terminal, Pier 126
Port of Long Beach, CA
Long Beach City Council- 8/23/05 Agenda, Item 22

Dear Mr. Shannon:

Sound Energy Solutions ("SES") has learned that the Long Beach City Council (the "Council") has placed an agenda item for its August 23, 2005 City Council meeting (Agenda Item No. 22) regarding SES' contracts with the City of Long Beach for a liquefied natural gas receiving and vehicle fuel terminal (the "Project"). Specifically, we understand that the Council intends to vote on a "[r]ecommendation to request the City Manager to communicate to all pertinent parties" its' "stated preference that the LNG facility not be located in the Port of Long Beach. . . . "

As counsel to SES, we write to place the Council on notice that such an act would breach the City of Long Beach's agreement(s) with SES and result in substantial damages to SES, in excess of the almost forty million dollars ($40,000,000.00) expended to date.

I. SES' Contract With The City of Long Beach

The City of Long Beach, acting by and through its Board of Harbor Commissioners ("BHC"), and SES executed a letter agreement dated May 8, 2003 (the "May 2003 Agreement") which provides for SES' development of a liquefied natural gas receiving terminal and regasification facility on Pier Echo in the Port of Long Beach. The May 2003 Agreement confirms that "[t]he Port of Long Beach and SES have reached agreement on the general business terms attached to this letter of intent as the Summary of Terms" and requires SES to engage in extensive (and expensive) preparations in furtherance of the Project.

For example, the May 2003 Agreement obligates SES to take steps to "develop the Project" including "conduct[ing] certain environmental, engineering and economic feasibility studies regarding the Project." During the initial "Exclusivity Period," the May 2003 Agreement requires SES to "diligently pursue the permits and approvals necessary to develop the Project." Indeed, the City of Long Beach acknowledges that "SES will invest substantial amounts in conducting the feasibility studies and submitting and processing applications for necessary permits and approvals." The May 2003 Agreement also requires SES to pay Long Beach "Guaranteed Minimum Annual Compensation" starting on January 1, 2004.

Accordingly, in reliance upon the May 2003 Agreement, and Long Beach's obligation to act in good faith thereunder, SES has expended nearly forty million dollars ($40,000,000.00) in furtherance of its obligations and rights under the May 2003 Agreement. These amounts include sums paid directly to Long Beach under the May 2003 Agreement as well as sums incurred in the "environmental, engineering and economic feasibility studies" required under the May 2003 Agreement. As you know, the application for an onshore liquefied natural gas receiving terminal requires extensive pre-construction engineering and design of the entire facility. In reliance on the May 2003 Agreement, SES has completed such engineering and design tasks, and, as a result, prepared and submitted extensive and detailed Resource Reports and supplements, as required by applicable laws. The lead agencies, the Federal Energy Regulatory Commission and the Port of Long Beach, intend to circulate the joint draft Environmental Impact Study and draft Environmental Impact Report ("DEIS/EIR") in or about late September 2005.

Thus, SES is far along its successful completion of the regulatory gauntlet contemplated and required by the May 2003 Agreement. The Council's proposed recommendation in Agenda Item 22 threatens to destroy all of SES' efforts on the eve of completion thereof. As detailed below, such action by the Council will result in substantial damages to SES.

II. The May 2003 Agreement Creates Enforceable Obligations, Which the City Would Breach By The Council's Proposed Recommendation.

As an initial matter, the May 2003 Agreement's characterization as a "letter of intent" does *not* mean that the obligations thereunder are unenforceable. *See California Food Serv. Corp. v. Great American Insurance Co.*, 130 Cal. App. 3d 892, 897 (1982) ("A letter of intent can constitute a binding contract, depending on the expectations of the parties."). As the *Great American Insurance* court noted, "[t]hese expectations may be inferred from the conduct of the parties and the surrounding circumstances." *Great American Insurance Co.*, 130 Cal. App. 3d at 897. This conclusion supported by reasoned decisions from numerous courts in California and elsewhere upholding the validity of letters of intent over the argument that they do not create binding obligations. *See, e.g., Entercom Communications Corp. v. Royce Intern. Broadcasting Corp.*, 2003 WL 21002873, at *8 (Cal. Ct. App. May 5, 2003) ("a letter of intent is not necessarily nonbinding;" "the more the LOI includes, the more likely it will be binding."); *In re Ankeny*, 184 B.R. 64 (B.A.P. 9th Cir.) (interpreting California law); *Doll v. Grand Union Co.*, 925 F.2d 1363 (11th Cir. 1991); *Stouffer Hotel v. Teachers Insurance and Annuity Ass'n*, 737 F.

Supp. 1553 (M.D. Fla. 1990); *Young v. Bishop*, 353 P.2d 1017 (Ariz. 1960); *Three-O-Three Investments, Inc. v. Moffitt*, 622 S.W.2d 736 (Mo. Ct. App. 1981); *Goren v. Royal Investments, Inc.*, 516 N.E.2d 173 (Mass. App. Ct. 1987).

The conclusion that the May 2003 Agreement is enforceable is also supported by the numerous authorities which have held that "agreements to negotiate" create enforceable obligations. In *Copeland v. Baskin Robbins, U.S.A.*, 96 Cal. App. 4th 1251 (2002), the Court of Appeal ruled that a contract to negotiate an agreement is distinguishable from a so-called "agreement to agree" and can be formed and breached just like any other contract. *Baskin Robbins*, 96 Cal. App. 4th at 1258. The court held that a party is liable for breach of a contract to negotiate an agreement "if a failure to reach ultimate agreement resulted from a breach of that party's obligation to negotiate or to negotiate in good faith." *Baskin Robbins*, 96 Cal. App. 4th at 1257.

Contract terms must be "reasonably certain" to constitute enforceable agreements. Restatement (Second) of Contracts § 33(1). "The terms of a contract are reasonably certain if they provide a basis for determining the existence of a breach and for giving an appropriate remedy." Restatement (Second) of Contracts § 33(2); *see also Ersa Grae Corp. v. Fluor Corp.*, 1 Cal. App. 4th 613, 623 (1991) (contract to transfer real property sufficiently certain even though some provisions were to be the subject of later documentation).

Refusing to enforce contacts because of purported uncertainty is strongly disfavored under California law. "The law does not favor but leans against the destruction of contracts because of uncertainty; and it will, if feasible, so construe agreements as to carry into effect the reasonable intentions of the parties if that can be ascertained." *McIllmoil v. Frawley Motor Co.*, 190 Cal. 546, 549 (1923).

In analyzing the types of claims which may be asserted, and the measure of damages to be awarded, the California Court of Appeal ruled that:

> We agree a cause of action for promissory estoppel might lie if the defendant made a clear, unambiguous promise to negotiate in good faith and the plaintiff reasonably and foreseeably relied on that promise in incurring expenditures connected with the negotiation. We may also assume for the sake of argument such a cause of action could be based on an implied promise to negotiate in good faith. If these propositions are correct, then promissory estoppel is just a different rubric for determining the enforceability of a contract to negotiate an agreement.

Baskin Robbins, 96 Cal. App. 4th at 1261-62. As such, damages for breach of a contract to negotiate an agreement are measured by "the injury the plaintiff suffered in relying on the defendant to negotiate in good faith." *Baskin Robbins*, 96 Cal. App. 4th at 1262-63. "This

measure encompasses the plaintiff's out-of-pocket costs in conducting the negotiations and may or may not include lost opportunity costs." *Baskin Robbins*, 96 Cal. App. 4th at 1262-63; *see also Swinerton & Walberg Co. v. City of Inglewood-Los Angeles County Civic Center Auth.*, 40 Cal. App. 3d 98 (1974) (public agency which solicited bids and breached its promise to award the contract to the lowest responsible bidder was subject to promissory estoppel claim of plaintiff who reasonably and detrimentally relied upon the agency's promise; plaintiff would be entitled under this theory to the expenses it incurred in reliance on the promise, namely expenses incurred in the fruitless competitive bidding process).

Here, SES will be able to recover millions of dollars from Long Beach if the Council effectively repudiates the May 2003 Agreement by following the recommendation to disavow and reject the Project to "all pertinent parties." Expenses necessarily incurred in good faith, in anticipation of performance or part performance of a contract, may generally be recovered as a part of the damages for its breach. *Crowther v. Metalite Mfg. Co.*, 133 Cal. App. 452, 456 (1933). The *Crowther* court upheld an award of damages that included expenses incurred in the preparation of office facilities and advertising done in anticipation of performance under a contract. *Crowther*, 133 Cal. App. at 454; *see also Walpole v. Prefab Mfg. Co.*, 103 Cal. App. 2d 472, 482 (1951) (expenses incurred in anticipation of, or preparation for, performance, ordinarily are a recoverable element of damage for breach of contract).

> The right to restitution or quasi-contractual recovery is based upon unjust enrichment. Where one obtains a *benefit* which he may not justly retain, he is unjustly enriched. The quasi-contract, or contract 'implied in law,' is an obligation created by the law without regard to the intention of the parties, and is designed to restore the aggrieved party to his former position by return of the *thing* or its equivalent in money.

1 BERNARD E. WITKIN, SUMMARY OF CALIFORNIA LAW, *CONTRACTS* § 91 at 122 (9th ed. 1990). Where one party has paid money or given other consideration under a contract which the other party later fails to perform, restitution is the appropriate remedy. *Mahony v. Standard Gas Engine Co.*, 187 Cal. 399, 405 (1921) (restitution properly awarded where consideration failed).

Even you acknowledged on numerous occasions, including the June 7, 2005 City Council meeting, that SES has a contract with the City of Long Beach regarding the Project. The foregoing authorities mandate that, regardless of the "letter of intent" label, the May 2003 Agreement will be enforceable in a court of law. SES has expended almost forty million dollars ($40,000,000.00) in its efforts to develop the Project, in total reliance upon the City of Long Beach's promises in the May 2003 Agreement and obligation to act in good faith. SES has even made direct payments to the City of Long Beach under the May 2003 Agreement and in reliance upon the City's continued good faith in complying with the parties' agreement. The City of Long Beach required SES to incur substantial obligations under the May 2003 Agreement. SES has complied with each and every one of its obligations. Should the Council decide to reverse

course and essentially repudiate the May 2003 Agreement, SES will use every available remedy to recover the multiple millions of dollars in damages caused by its reliance upon the City of Long Beach's obligation to act in good faith.

III. The Council Cannot Adopt Agenda Item 22 Without Violating SES' Due Process And Fair Hearing Rights

Additional legal requirements prevent the Council from even considering Agenda Item 22. Under California law, the Council will consider any appeal of the BHC's certification of the final EIS/EIR for the Project. Cal. Pub. Resources Code § 21151(c). We understand from Port staff that it intends to circulate the joint Draft EIS/EIR for the Project in late September 2005, with Harbor Commission consideration, and any appeal to the City Council, to occur at a later date.

The Council's Agenda Item 22 purports to recommend the Council's "stated preference that the LNG facility not be located in the Port of Long Beach". Consideration of such a matter before the EIS/EIR could reach the Council on appeal would constitute an illegal and premature pre-judgment of the Project and violate SES' legal rights. In other words, if the Council acts upon Agenda Item 22 at its August 23, 2005 meeting, the Council will have effectively pre-judged a matter which could be before the Council on appeal from the BHC. As a result, such council action would deny SES a fair hearing on the Project's merits. Such a premature action would violate due process and fair hearing principles of federal and state law. *See, e.g., Woodland Hills Residents Association v. City Council of City of Los Angeles*, 26 Cal. 3d 938 (1980); *Pomona College v. Superior Court*, 45 Cal. App. 4th 1716 (1996).

• • • •

We strongly urge you to (1) cause the proposed item to be removed from the Council's agenda, (2) advise the Council that it cannot assert any position on the Project in light of its role as the quasi-judicial decision maker on any appeal of the Harbor Commission's consideration of the Project's EIR and (3) properly advise the Council of its legal obligations to SES under the subject contracts. SES has relied upon the City of Long Beach's good faith in the performance of its obligations under the May 2003 Agreement. As detailed above, SES is confident that the parties' letter agreement will be enforceable -- at least with respect to SES' reliance in expending almost forty million dollars ($40,000,000.00). Accordingly, the Council should not prematurely judge the Project prior to considering the certification of the final EIR/EIS on the Project. To do otherwise would substantially impair SES' rights and embroil the parties in substantial and expensive litigation.

We are available to discuss this matter with you or the Council -- either privately or during the August 23, 2005 Council meeting. This letter is written without waiver of SES' rights and remedies, all of which are expressly reserved. Please call if you have any questions.

Very truly yours,

BENJAMIN M. REZNIK
KENNETH A. EHRLICH,
Professional Corporations of
Jeffer, Mangels, Butler & Marmaro LLP

BMR:KAE:pf
Enclosures

cc: Mayor Beverly O'Neill
City Council Members
City Manager Jerry Miller
Deputy City Manager Christine Shippey