VII. TAX OPINION LETTERS

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Attorney-Client Privileged Communication

EC2 000034132

Ladies and Gentlemen:

We have acted as counsel to Enron Corp. ("Enron") in connection with certain aspects of the transactions more fully described below (collectively, the "Transaction"). In connection therewith, you have requested our opinion as to certain U.S. federal income tax consequences associated with the Transaction under the Internal Revenue Code of 1986, as amended (the "Code").[1]

In rendering our opinions we have relied on the following documents (collectively, the "Transaction Documents"): (i) Assignment Agreement (Membership Interest in Kingfisher) dated as of November 10, 1999 between Enron Corp., Assignor and Houston Pipe Line Company, Assignee; (ii) Agreement of Limited Partnership of HPL Asset Holdings L.P. dated as of November 10, 1999 among Houston Pipe Line Company, as the General Partner and as a Limited Partner and Peregrine I LLC, as a Limited Partner; (iii) Assignment and Contribution Agreement (Bammel Storage Facility Reservoir) effective November 10, 1999 between Houston Pipe Line Company, Grantor, and HPL Asset Holdings L.P., Grantee; (iv) Assignment and Contribution Agreement (Bammel Storage Facility Equipment) effective November 10, 1999 between Houston Pipe Line Company, Grantor, and HPL Asset Holdings L.P., Grantee; (v) Assignment and Contribution Agreement (Houston Loop and Texas City Loop) effective November 10, 1999 between Houston Pipe Line Company, Grantor, and HPL Asset Holdings L.P., Grantee; (vi) Assignment Agreement (General Partnership Interest in HPL Asset Holdings L.P.) dated November 10, 1999 between Houston Pipe Line Company, Assignor, and Blue Heron I LLC, Assignee; (vii) Certificate of Amendment to the Certificate of Limited Partnership of HPL Asset Holdings L.P.; (viii) Letter Agreement dated as of November 10, 1999 between Whitewing Associates L.P. and Houston Pipe Line Company; (ix) Assignment Agreement (Membership Interest in Blue Heron I LLC and Limited Partnership Interest in HPL Asset Holdings L.P.) dated as of November 10, 1999 between Houston Pipe Line Company, Assignor, and Whitewing Associates L.P., Assignee; (x) First Amendment to Limited Partnership Agreement of Whitewing Associates L.P.; (xi) Assignment Agreement (Limited Partnership Interest in Whitewing Associates L.P.) dated as of November 10, 1999 between Houston Pipe Line Company, Assignor, and Kingfisher I LLC, Assignee; (xii) Lease Agreement between HPL Asset Holdings L.P., as Lessor and Houston Pipe Line Company, as Lessee effective as of November 10,

[1]All section references are to the Code or the Treasury regulations promulgated thereunder, unless otherwise notes.

1999; (xiii) Consent of The Bank of New York and Bank of America, N.A. to approve the form and substance of Assumption Agreement and Ratification of Guaranty; (xiv) Assumption Agreement dated as of November 10, 1999 between HPL Asset Holdings L.P. and Houston Pipe Line Company; (xv) Certificate of Formation of HPL Asset Holdings L.P.

I. FACTS

A. The Parties

Whitewing Associates L.P. ("Whitewing") is a Delaware limited partnership that was formerly known as Whitewing Associates L.L.C. Whitewing is owned by Whitewing Management LLC, a Delaware limited liability company, as general partner, and by Kingfisher I LLC ("Kingfisher"), Peregrine I LLC ("Peregrine"), and Osprey Trust, a Delaware business trust, as limited partners.

Houston Pipe Line Company ("HPL"), a Delaware corporation, is a wholly-owned subsidiary of Enron. Among other things, HPL owns (i) the Bammel Storage Facility Reservoir, a depleted oil reservoir natural gas storage facility located in Harris County, Texas, (ii) certain wells, facilities, pipe and equipment located on a contiguous surface area over and around the Bammel Storage Facility, and (iii) the Houston Loop pipelines and the Texas City Loop pipelines, which are high pressure natural gas pipelines and related facilities located primarily in Harris and Galveston Counties, Texas (collectively, the "Bammel Assets").

Kingfisher is a Delaware limited liability company whose sole member is Enron.

Peregrine is a Delaware limited liability company whose sole member is Enron.

HPL Asset Holdings L.P. ("HPL Asset Holdings"), a Delaware limited partnership formed on November 9, 1999, is owned 0.01 percent by HPL, as general partner (the "HPL Asset Holdings General Partnership Interest"), 98.99 percent by HPL, as limited partner (the "HPL Asset Holdings Limited Partnership Interest") and 1.0 percent by Peregrine, as limited partner. In return for the HPL Asset Holdings General Partnership Interest and the HPL Asset Holdings Limited Partnership Interest, HPL assigned and contributed the Bammel Assets, as more fully described in the Assignment and Contribution Agreement (Bammel Storage Facility Reservoir), dated November 10, 1999, the Assignment and Contribution Agreement (Bammel Storage Facility Equipment), dated November 10, 1999, and the Assignment and Contribution Agreement (Houston Loop and Texas City Loop), dated November 10, 1999.

Blue Heron I LLC ("Blue Heron") is a Delaware limited liability company whose sole member is Whitewing.

B. Summary of the Transaction

Pursuant to the terms of the Assignment Agreement (Membership Interest in Kingfisher), dated as of November 10, 1999, between Enron and HPL, Enron assigned and contributed 100 percent of its membership interest in Kingfisher to HPL.

Pursuant to the terms of the Assignment Agreement (General Partnership Interest in HPL Asset Holdings L.P.), dated as of November 10, 1999, between HPL and Blue Heron, HPL assigned the HPL Asset Holdings General Partnership Interest to Blue Heron in return for a membership interest in Blue Heron.

Pursuant to the terms of the Assignment Agreement (Membership Interest in Blue Heron I LLC and Limited Partnership Interest in HPL Asset Holdings L.P.), dated as of November 10, 1999, between HPL and Whitewing, HPL assigned and contributed (i) the HPL Asset Holdings Limited Partnership Interest and (ii) its membership interest in Blue Heron to Whitewing in exchange for a limited partnership interest in Whitewing.

Immediately thereafter, pursuant to the terms of the Assignment Agreement (Limited Partnership Interest in Whitewing Associates L.P.), dated as of November 10, 1999, between HPL and Kingfisher, HPL assigned and contributed its limited partnership interest in Whitewing to Kingfisher.

Thus, after giving effect to the assignments described above, the partnership interests in HPL Asset Holdings are held as follows: (i) the HPL Asset Holdings General Partnership Interest is owned by Blue Heron, (ii) the HPL Asset Holdings Limited Partnership Interest is owned by Whitewing, and (iii) the remaining 1.0 percent limited partnership interest is held by Peregrine.

Pursuant to the terms of the Lease Agreement, effective November 10, 1999, between HPL Asset Holdings and HPL, HPL Asset Holdings leased the Bammel Assets to HPL for an eighteen year term.

II. REPRESENTATIONS

In rendering our opinions herein set forth, the following facts have been represented to us:

1. No election will be made to classify Kingfisher, Peregrine or Blue Heron as an association taxable as a corporation for federal tax purposes.

2. Less than 80 percent of the value of the assets held by HPL Asset Holdings immediately after its formation consist of stock and securities within the meaning of section 351(e)(1)(B).

3. Less than 80 percent of the value of the assets held by Whitewing immediately after the contribution of the HPL Asset Holdings Limited Partnership Interest by HPL consist of stock and securities within the meaning of section 351(e)(1)(B).

4. HPL has a zero basis in the Bammel Assets.

5. The Bammel Assets would have a 15 year applicable recovery period if such assets were newly purchased property that was placed in service at the time of their contribution by HPL to HPL Asset Holdings.

6. The fair market value of the Bammel Assets will exceed HPL's adjusted tax basis in such assets upon contribution to HPL Asset Holdings.

7. HPL Asset Holdings and Whitewing will adopt the remedial method described in Treas. Reg. § 1.704-3(d) with respect to allocations of income, gain, loss or deduction attributable to the Bammel Assets and the HPL Asset Holdings Limited Partnership Interest contributed by HPL to HPL Asset Holdings and Whitewing, respectively.

8. The Bammel Assets will not be disposed of by HPL Asset Holdings before the HPL Asset Holdings Limited Partnership Interest is distributed to HPL in liquidation of its interest in Whitewing.

9. Whitewing will distribute the HPL Asset Holdings Limited Partnership Interest to HPL in liquidation of its interest in Whitewing in [2014].

10. In the year in which Whitewing makes a liquidating distribution to HPL, HPL will have made a section 754 election.

11. A portion of the built-in gain associated with the HPL Asset Holdings Limited Partnership Interest distributed to HPL in liquidation of its interest in Whitewing will not be attributable to depreciation recapture under section 1245 with respect to the Bammel Assets.

Our opinions are conditioned on the initial and continuing accuracy of the representations set forth above, as well as our understanding that the Transaction was carried out in accordance with the Transaction Documents and that there are no agreements, arrangements or understanding among any of the parties to the Transaction Documents other than those reflected in the Transaction Documents.

III. LAW AND ANALYSIS

A. Partnership Formation

Section 721(a) provides that no gain or loss shall be recognized to a partnership or to any of its partners in the case of a contribution of property to the partnership in exchange for an interest in the partnership. However, under section 721(b) the general nonrecognition rule of section 721(a) does not apply to gain realized on a transfer of property to a partnership investment company (within the meaning of section 351) if the contribution results in the diversification of the transferor's assets.[2] Section 722 provides that the basis of an interest in a partnership acquired by a contribution of property to the partnership is the adjusted basis of such property to the contributing partner at the time of the contribution increased by the amount (if any) of gain recognized under section 721(b) to the contributing partner at such time. Section 723 provides that the basis of any property contributed to a partnership by a partner is the adjusted basis of the property in the hands of the contributing partner at the time of the contribution.

In the instant case, the Bammel Assets and the HPL Asset Holdings Limited Partnership Interest should constitute "property" within the meaning of sections 721 and 722. *See, e.g.*, *United States v. Stafford*, 727 F.2d 1043 (11th Cir. 1984) (for purposes of section 721, "the term [property] encompasses whatever may be transferred"). In addition, less than 80 percent of the value of the assets held by Whitewing and HPL Asset Holdings consist of stock and securities as defined in section 351(e)(1)(B). Thus, no gain or loss should be recognized by HPL on either the contribution of the Bammel Assets to HPL Asset Holdings or the contribution of the HPL Asset Holdings Limited Partnership Interest to Whitewing. Moreover, under section 722, because HPL has a zero basis in the Bammel Assets, HPL will have a zero basis in the HPL Asset Holdings Limited Partnership Interest, and, therefore, a zero basis in its interest in Whitewing following the contribution of the HPL Asset Holdings Limited Partnership Interest to Whitewing. In addition, under section 723, the basis of the Bammel Assets in the hands of HPL Asset Holdings is zero, and, therefore, Whitewing's basis in HPL Asset Holdings is zero following the contribution of the HPL Asset Holdings Limited Partnership Interest to Whitewing.

B. Partnership Operations

[2] A partnership generally will be treated as an investment company if, immediately after the transfer or formation, more than 80 percent of its assets are held for investment and consist of "stock and securities," as defined in section 351(e)(1)(B).

Section 704(c)(1)(A) provides that under regulations prescribed by the Secretary income, gain, loss and deduction with respect to property contributed to the partnership by a partner shall be shared among the partners so as to take account of the variation between the basis of the property to the partnership and its fair market value at the time of contribution (*i.e.*, a precontribution gain or loss). In general, allocations with respect to precontribution gain or loss under section 704(c) must be made using a reasonable method that is consistent with the purpose of section 704(c) – namely, to prevent the shifting of tax consequences among partners with respect to precontribution gain or loss. Treas. Reg. § 1.704-3(a)(1).

The Treasury regulations promulgated under section 704 provide three methods of allocating precontribution gain or loss under section 704(c) that are considered generally reasonable: the traditional method, the traditional method with curative allocations and the remedial method. *See* Treas. Reg. § 1.704-3(b), (c) and (d). Under the remedial method, a partnership eliminates distortions caused by the ceiling rule[3] by creating remedial items and allocating those items to its partners. Although remedial items have the same effect as actual tax items on a partner's tax liability and on the partner's adjusted tax basis in his partnership interest, remedial items do not affect the partnership's computation of taxable income under section 703, the partnership's adjusted tax basis in partnership property or partners' book capital accounts. Treas. Reg. § 1.704-3(d)(4).

In the instant case, the Bammel Assets will be considered section 704(c) property with precontribution gain (*i.e.*, built-in gain) upon the contribution of such assets by HPL to HPL Asset Holdings, because the fair market value of the Bammel Assets will exceed HPL's adjusted tax basis in such assets at the time of contribution. Treas. Reg. § 1.704-3(a)(3(i) and (ii). Due to the adoption of the remedial method under Treas. Reg. § 1.704-3(d) by HPL Asset Holdings, HPL initially will be allocated items of income attributable to the built-in gain of the Bammel Assets over 15 years (the recovery period available to HPL if the Bammel Assets were newly purchased property placed in service at the time of contribution by HPL). Treas. Reg. §1.704-3(d)(2)).[4]

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[3]The ceiling rule comes into play where the total income, gain, loss or deduction that should be allocated to the partners for a taxable year with respect to a property under the traditional method exceed the amount realized for tax purposes by the partnership with respect to that property for a taxable year. *See* Treas. Reg. § 1.704-3(b)(1).

[4]It is our understanding that Enron will be allocated the corresponding items of deduction attributable to the built-in gain of the Bammel Assets. Thus, because the remedial items will be allocated to members of the same consolidated group, the remedial allocation should offset as a practical matter.

Thereafter, because HPL will contribute the HPL Asset Holdings Limited Partnership Interest to Whitewing, Whitewing will be allocated the items of income attributable to the built-in gain of the Bammel Assets in the same manner as such items would have been allocated to HPL. Treas. Reg. § 1.704-3(a)(7). Moreover, Whitewing must allocate its distributive share of the built-in gain amounts from the Bammel Assets "in a manner that takes into account the contributing partners remaining built-in gain or loss." Treas. Reg. § 1.704-3(a)(9). Hence, the remedial items of income allocated to Whitewing should, in turn, be allocated to HPL. These income allocations will result in an increase in HPL's adjusted tax basis in its partnership interest in Whitewing. Treas. Reg. § 1.704-3(d)(4). [Therefore, at the end of the book life of the Bammel Assets (15 years), HPL's adjusted tax basis in its partnership interest in Whitewing should equal the initial fair market value of such assets assuming no other allocations of income, gain, loss, deduction or credit over such 15 year period.]

C. Liquidation

1. Liquidating Distribution of HPL's Interest in Whitewing

Section 736(b) provides that if payments made in liquidation of the interest of a retiring partner or a deceased partner are considered as a distribution by the partnership, rather than as a distributive share of partnership income or as guaranteed payments, such payments will be treated as made in exchange for such partner's interest in partnership property. Under section 731(a)(1), in the case of a distribution by a partnership to a partner, gain shall not be recognized by a distributee partner unless such partner receives cash in excess of its adjusted tax basis in partnership property. Section 731(a)(2), in turn, provides that upon a distribution in liquidation of a partner's interest in a partnership, a loss will be recognized by a distributee partner if such partner receives no other property other than cash, unrealized receivables (as defined in section 751(c)) and inventory (as defined in section 751(d)), and the amount of cash and the tax basis of such assets, as determined under section 732, are less than the distributee' partner's adjusted tax basis in its partnership interest.

Section 751(c) provides that the term "unrealized receivables" includes, among other things, section 1245 property. Section 751(f) provides that in determining whether property of a partnership is an unrealized receivable, such partnership shall be treated as owning its proportionate share of the property of any other partnership in which it is a partner. Section 1245(a)(3) provides that "section 1245 property" means, among other things, any property which is or has been property of a character subject to the allowance for depreciation provided in section 167 and is either personal property or certain other depreciable property that was used as an integral part of manufacturing, production or extraction of gas.

Under section 732(b), the basis of property (other than money) distributed by a partnership to a partner in liquidation of the partner's interest shall be an amount equal to the adjusted basis of such partner's interest in the partnership reduced by any money distributed in the same transaction. In the

event basis must be allocated among distributed assets under section 732(b), section 732(c) provides that basis is allocated first to any unrealized receivables (as defined in section 751(c)) and inventory items (as defined in section 751(d)) in an amount equal to the adjusted basis of each such property to the partnership. Thereafter, to the extent basis remains to be allocated, basis is allocated to other distributed properties in an amount equal to such other property's adjusted basis to the partnership and then, to the extent any increase in basis is required in order to have the adjusted bases of such other distributed properties equal such remaining basis:

> (A) first to properties with unrealized appreciation in proportion to their respective amounts of unrealized appreciation before such increase (but only to the extent of each property's unrealized appreciation), and (B) then, to the extent such increase is not allocated under subparagraph (A), in proportion to their respective fair market values.

Section 732(c)(2).[5]

In the instant case, some, but not all, of the HPL Asset Holdings Limited Partnership Interest will be considered an unrealized receivable under section 751(c) because the Bammel Assets constitute section 1245 property, and under section 751(f), Whitewing is treated as owning its proportionate share of the unrealized receivables held by HPL Asset Holdings. However, because property other than solely cash, unrealized receivables and inventory are being distributed to HPL upon the liquidation of its interest in Whitewing, HPL will recognize neither gain nor loss upon the distribution of the HPL Asset Holdings Limited Partnership Interest. *See* section 731(a)(1) and (2).

Under section 732(b), the basis of the HPL Asset Holdings Limited Partnership Interest received by HPL will equal HPL's adjusted basis in Whitewing. Under section 732(c), this basis must first be allocated to any unrealized receivables in an amount equal to the adjusted basis of such property in the hands of Whitewing (through the operation of section 751(f)). Under this methodology, no basis should be attributed to the portion of the HPL Asset Holdings Limited Partnership Interest considered an unrealized receivable because such property has no basis in the hands of HPL Asset Holdings. Thus, under section 732, all of HPL's basis in Whitewing will be allocated to the HPL Holding Limited Partnership Interest.

2. *Basis Adjustment to Bammel Assets*

[5]Section 732(c) states that section 732 shall not apply to the extent that a distribution is treated as a sale or exchange of property under section 751(b). Section 751(b) does not apply, however, to a "distribution of property which the distributee contributed to the partnership." Section 751(b)(2)(A). Therefore, because the HPL Asset Holdings Limited Partnership Interest was originally contributed to Whitewing by HPL, section 751(b) should not apply to recharacterize the distribution by Whitewing of the HPL Asset Holdings Limited Partnership Interest to HPL.

Section 743(b) provides that if a partnership makes a valid section 754 election, the basis of partnership assets is adjusted with respect to a transferee partner upon the transfer of a partnership interest "by sale or exchange or upon the death of a partner." *See also* Treas. Reg. § 1.743-1(a). The amount of the section 743(b) adjustment is equal to the difference between the transferee's initial basis in his partnership interest and his "proportionate share of the adjusted basis of the partnership property." *Id.* If the transferee's basis in his partnership interest is greater than his proportionate share of the basis of the partnership property, the section 743(b) adjustment increases the basis of partnership property with respect to such transferee. Treas. Reg. § 1.743-1(b)(1) If the transferee's basis in his partnership interest is less than his proportionate share of the basis of the partnership property, the section 743(b) adjustment decreases the basis of partnership property with respect to such transferee. Treas. Reg. § 1.743-1(b)(2).

The distribution of the HPL Asset Holdings Limited Partnership Interest to HPL by Whitewing should be considered an exchange for purposes of section 743. Section 761(e)(2). Thus, because (i) HPL Asset Holdings will have made a section 754 election prior to the year of such distribution and (ii) HPL's basis in HPL Asset Holdings is greater than its proportionate share of the basis of the Bammel Assets held by HPL Asset Holdings (zero), HPL Asset Holdings should be permitted to increase the basis of the Bammel Assets with respect to HPL by an amount equal to HPL's basis in HPL Asset Holdings. This increase in basis should be depreciable as if it were newly purchased property under any depreciation method available to HPL for newly purchased property that is placed in service at the time of the distribution. Treas. Reg. § 1.743-1(j)(4)(i)(B).

IV. OPINIONS

Based on the facts, representations, law and analysis set forth above, in our opinion, for federal income tax purposes:

1. Under section 732, the basis of the HPL Asset Holdings Limited Partnership Interest distributed by Whitewing to HPL in liquidation of HPL's interest in Whitewing should be an amount equal to HPL's adjusted basis in Whitewing[, after giving effect to any remedial allocations under section 704(c) attributable to the Bammel Assets.]

2. Upon the distribution of the HPL Asset Holdings Limited Partnership Interest to HPL in liquidation of its interest in Whitewing, HPL Asset Holdings should be permitted to increase the basis of the Bammel Assets with respect to HPL by the excess of HPL's basis in HPL Asset Holdings over HPL's proportionate share of the basis of the Bammel Assets held by HPL Asset Holdings.

Our opinion is based upon the existing provisions of the Code and the Treasury regulations promulgated thereunder, published rulings of the Internal Revenue Service and existing case law. All such authorities are subject to change, and any such change could apply retroactively. Moreover,

we express no opinion as to the tax treatment of the Transaction under the provisions of any other section of the Code that also may be applicable thereto ***[, including, but not limited to, section 731(c)]*** or to the tax treatment of any conditions existing at the time of, or effects resulting from, the Transaction that are not specifically addressed in the foregoing opinion.

This opinion is not to be quoted or otherwise referred to or furnished to any governmental agency without our prior written consent.

Very truly yours,

VINSON & ELKINS L.L.P.

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