

1 Daniel H. Slate (State Bar No. 78173)
2 HUGHES HUBBARD & REED LLP
3 350 South Grand Avenue
4 Los Angeles, California 90071-3442
5 Telephone: (213) 613-2800

50-275/323

6 Attorneys for Viacom Inc.

7
8 UNITED STATES BANKRUPTCY COURT
9 NORTHERN DISTRICT OF CALIFORNIA
10 SAN FRANCISCO DIVISION

11 In Re:
12 PACIFIC GAS & ELECTRIC COMPANY,
13 a California corporation,
14 Debtor.

15 Federal I.D. No. 94-074260

CASE NO. 01-30923 DM

THE HONORABLE DENNIS MONTALI
CHAPTER 11 CASE

**NOTICE OF MOTION AND MOTION OF
VIACOM INC. FOR ENTRY OF AN
ORDER FOR RELIEF FROM STAY AND
FOR ADEQUATE PROTECTION WITH
RESPECT TO THE DAILEY DALE
PROJECT POWER PURCHASE
AGREEMENT**

**[MEMORANDUM OF POINTS AND
AUTHORITIES AND DECLARATION OF
STEVE R. DEAN FILED
CONCURRENTLY]**

Date: October 1, 2001

Time: 1:30 p.m.

Place: 235 Pine Street, 22nd Floor,
San Francisco, California

23
24 PLEASE TAKE NOTICE that on October 1, 2001, at 1:30 p.m., or as soon
25 thereafter as the matter may be heard in the Courtroom of the Honorable Dennis Montali, located
26 at 235 Pine Street, 22nd Floor, San Francisco, California, Viacom Inc. ("Viacom" or "Movant")
27 will and hereby does move (the "Motion"), pursuant to sections 105(a), 362(d)(1) and 365(d)(2)
28

NOTICE OF MOTION AND MOTION OF VIACOM INC. FOR ENTRY OF AN ORDER FOR RELIEF FROM STAY AND FOR
ADEQUATE PROTECTION WITH RESPECT TO THE DAILEY DALE PROJECT POWER PURCHASE AGREEMENT
L.A. 508607_1

11
Aool Add: Kids Ogc Mail Center

1 of title 11 of the United States Code (11 U.S.C. § 101 et seq.) (the "Bankruptcy Code") and
2 Rules 2002, 4001, 9006 and 9007 of the Federal Rules of Bankruptcy Procedure (the
3 "Bankruptcy Rules") and B.L.R. 4001-1, for entry of an order compelling Pacific Gas & Electric
4 Company (the "Debtor" or "PG&E") to (a) provide the DAI Oildale Project (the "Project") with
5 adequate protection with respect to its interest in its Power Purchase Agreement with the Debtor,
6 dated as of May 7, 1984 (the "PPA"), effective on August 2, 2001, (b) confirm that the
7 reasonable rate in determining administrative payments for electricity going forward, pending
8 assumption or rejection of the PPA by the Debtor, shall be the contract rate (energy and capacity)
9 provided in the PPA, all other provisions of the PPA remaining in full force and effect, and
10 (c) effective on August 2, 2001, require the Debtor to make semi-monthly payments equal to no
11 less than 5% (per month) of the prepetition default claim until the Debtor assumes or rejects the
12 PPA; and within 30 days of the date of its order, require the Debtor to establish a date certain for
13 the Debtor to assume or reject the PPA, and to file a statement of intention as to when the Debtor
14 intends to so assume or reject (collectively, the "Motion").¹

15 This Motion is based on the allegations contained herein, the accompanying
16 Memorandum of Points and Authorities, the accompanying Declaration of Steve K. Dean (the
17 "Dean Decl."), the records and files of this Chapter 11 case and any admissible evidence
18 presented to this Court in connection with the hearing on this Motion.

19 Pursuant to B.L.R. 9014-1(c)(1), any opposition to this Motion must be filed and
20 served no later than September 17, and any reply must be filed and served no later than
21 September 24.

22 OVERVIEW

23 1. Movant is aware of the Court's recent ruling of June 29, 2001 (the "June
24 29th Order") entered with respect to the motion filed by Mid-Set Cogeneration Company,
25 Coalinga Cogeneration Company, Salinas River Cogeneration Company and Sargent Canyon

26 ¹ Movant is simultaneously investigating the possibility of entering into agreements with
27 the Debtor similar to the ones approved by this Court with respect to Calpine Corporation, et al.

1 Cogeneration Company. By this Motion, Movant seeks at least the relief provided in the June
2 29th Order.

3 2. The Project is a 29,000 kw gas-fired cogeneration qualifying facility
4 located in Oildale, Kern County, California. (Dean. Decl. ¶ 3.) The Project was conceived,
5 designed, built and financed on the basis of the Debtor's 20-year obligation to purchase
6 electricity from the Project pursuant to the PPA. (Id. ¶ 8.) Indeed, the viability of the Project's
7 operations during its eleven years of existence has at all times been, and currently is, dependent
8 on the revenue from the PPA. (Id. ¶¶ 7-8.) Any prolonged failure of the Debtor to pay for
9 electricity, such as occurred prepetition, materially compromises the Project's ability to continue
10 operating the facility and producing electricity as a going concern.

11 3. During the months of February and March 2001, prior to the
12 commencement of this Chapter 11 case, the Debtor elected not to pay the Project for energy and
13 capacity as required by the PPA, but instead made only partial payments of roughly 15% of the
14 total amounts due for the months of December 2000 and January 2001. Furthermore, the Debtor
15 made no payments at all for energy and capacity delivered by the Project in February and March
16 of 2001. (Id. ¶ 10.) As of April 6, 2001 (the "Petition Date"), the Debtor had withheld
17 approximately \$8,807,797 in payments owed under the PPA (the "Prepetition Debt"), even
18 though the Project had dutifully performed all of its obligations thereunder and had produced the
19 required levels of electricity and delivered same to the Debtor.

20 4. The Debtor's non-payment of the Prepetition Debt has resulted in severe
21 financial losses for the Project. Having been stripped of its primary source of revenue, the
22 Project was unable to fund the purchase of natural gas. On or around February 15, 2001, its
23 supplier, BP Energy Company ("BP"), suspended delivery of natural gas to the Project pursuant
24 to a certain Natural Gas Sales Agreement, as amended, (the "NGSA") dated as of September 5,
25 1997, by and between BP (formerly Amoco Energy Trading Company) and State Street Bank
26 and Trust Company of California, N.A. ("State Street"), as Owner Trustee for the benefit of
27 Movant. (Id. ¶¶ 11-12.)
28

1 5. On January 18, 2001, DAI Oildale Inc. ("DAI") as the agent for State
2 Street, received a facsimile from the Debtor entitled "Notice to Qualifying Facility Owners"
3 asserting that the Debtor was invoking the *force majeure* provision of the PPA between the
4 Debtor and State Street. (Id. ¶ 9.) On February 6, 2001, the Debtor defaulted on the PPA, by
5 non-payment to the Project of the entire amount due for energy and capacity delivered in
6 December 2000. Instead, the Debtor merely tendered a partial payment of \$560,867.74 for
7 December 2000 energy and capacity due – roughly 15% of full amounts due for that month. On
8 March 7, 2001, the Debtor further defaulted on the PPA, by again making only a partial payment
9 for energy and capacity delivered in January 2001. This time, the Debtor tendered a partial
10 payment of \$620,649.71, again, approximately 15% of full amounts owed for that month. (Id.
11 ¶ 10.)

12 6. In response to these extraordinary and unforeseen events, State Street
13 received a demand for assurances from BP, dated February 12, 2001, which would require State
14 Street to provide a credit facility or cash reserves approaching \$10 million within 3 business
15 days. This amount was essentially equal to the total dollar amount of fuel purchased by the
16 Project from BP in all of 2000. The Project was not in a financial position to be able to comply
17 with BP's new payment demands, or to be forced to bear the brunt of a squeeze play essentially
18 brought about by the Debtor's changed circumstances. (Id. ¶ 11.)

19 7. DAI as Buyer's Designee for State Street therefore had no alternative but
20 to invoke, by letter dated February 15, 2001, the *force majeure* provisions in the NGSA and
21 provided notice to BP regarding the Project's inability to perform due to causes beyond its
22 control. BP elected to suspend further delivery of gas to the Project. Thereafter, DAI, as
23 Operator of the facility, shut down the facility and initiated necessary maintenance. (Id. ¶ 12.)

24 8. On March 1, 2001, the Project defaulted on its debt financing. Its
25 unrestricted operating cash reserves were depleted. However, at this time the Project arranged
26 for the loan of certain funds to the Project for the necessary cash pre-payment to secure natural
27 gas for limited peak period operations. This initiative on the part of Movant was undertaken in
28 consideration of the various pleadings from various State elected and regulatory officials for

1 electric power production, as well as the sense that concrete steps were being taken to resolve the
2 crisis and cure the payment defaults of the Debtor under the PPA. Such limited operations
3 continued through the Petition Date. (Id. ¶ 13.)

4 9. Given the Project's inability to meet its obligations to its gas suppliers, its
5 lenders and other creditors – all directly and proximately caused by the Debtor's prepetition
6 defaults under the PPA – the Project was compelled to accept the Debtor's offer to advance
7 \$1,450,000 ("Advance") in order that natural gas could be purchased and the facility restarted, as
8 reflected in the Debtor's letter to DAI dated May 23, 2001. In accordance with the terms of this
9 letter agreement, this Advance must be repaid over the next six months. (Id. ¶ 16.) While the
10 Advance temporarily replenishes the Project reserves to permit the cash prepayment of natural
11 gas for facility operations for one month, it does nothing to help cure the Project's continuing
12 outstanding obligations to BP, its lenders and other creditors. Only payments of prepetition
13 obligations will answer these issues. (Id. ¶ 17.)

14 10. Movant is not requesting that the Court invalidate or otherwise abrogate
15 the PPA; to the contrary, the relief sought herein is necessary to preserve the PPA. Under such
16 circumstances, fixing a date within 30 days of the date of an order requiring the Debtor to
17 establish a date certain by when the Debtor must assume or reject, and to file a statement of
18 intention as to when the Debtor intends to assume or reject the PPA, constitutes a "reasonable"
19 period within which to make this decision. Furthermore, pending its decision on assumption or
20 rejection of the PPA, it is proposed that the Debtor shall make semi-monthly payments equal to
21 no less than 5% (per month) of the Prepetition Debt effective on August 2, 2001. In addition, it
22 shall be confirmed that the reasonable rate in determining administrative payments for electricity
23 going forward, pending assumption or rejection of the PPA by the Debtor, shall be the contract
24 prices provided in the PPA, all other provisions of the PPA remaining in full force and effect
25 (including, for example, capacity payments during any period of *force majeure*, as well as
26 scheduled maintenance periods). Given the magnitude of the Debtor's past defaults, which have
27 had the effect of causing BP to suspend fuel deliveries and the Project to cease operations until
28 the Advance by the Debtor, it is stating the obvious to note that the Project will continue as a

1 going concern only with the forbearance of its various creditors. Prepetition natural gas
2 liabilities, which the Project is unable to pay, total approximately \$4,660,000. The Project needs
3 to provide some relief and certainty to its lenders and other creditors if there is to be a PPA for
4 the Debtor to assume or reject and a Project to perform thereunder.

5 11. While a debtor's decision to assume or reject an executory contract need
6 not ordinarily be expedited, the current situation is anything but ordinary. The Debtor's actions
7 to date have created an unworkable and already disastrous situation for the Project. Without this
8 Court's immediate intervention as requested herein, the Project may be unable to reasonably
9 address its financial distress, the Debtor may lose a potentially valuable asset in the form of the
10 PPA, and the California power grid may be short another 29 megawatts of electricity, as the
11 summer months continue.

12 JURISDICTION AND VENUE

13 12. This Court has jurisdiction over this Motion and the issues raised hereby
14 pursuant to 28 U.S.C. §§ 157 and 1334. This is a core proceeding pursuant to 28 U.S.C.
15 §§ 157(b)(2)(A), (D), (G), and (M).

16 13. Venue is proper in this Court pursuant to 28 U.S.C. § 1409.

17 FACTUAL BACKGROUND

18 14. The relief sought herein is premised on the following allegations, which
19 are supported by and set forth in greater detail in the accompanying Dean Declaration:

20 A. The Project's Contractual Relationship With the Debtor.

21 15. The Project supplies power to the Debtor pursuant to the PPA, which has
22 approximately nine of its original 20-year term remaining. The PPA is between the Debtor and
23 State Street as Owner Trustee for the Benefit of Viacom (successor in beneficial interest to
24 Dexzel Inc.). DAI is the agent for State Street as Owner Trustee, as well as operator of the
25 facility. The Project is dependent upon revenue from a single utility (in this case, the Debtor)
26 which is the sole purchaser of its electricity. (Dean Decl. ¶ 5.) Historically, more than 95% of
27 the Project's revenue comes from electricity sales to the Debtor, the remaining portion resulting
28 from the Project's oil production facilities. (Id. ¶ 7.) Such revenues are used to purchase natural

1 gas (the single largest cost of production) as fuel to run the facility and to pay the other costs
2 associated with the operation and financing of the facility. (Id.)

3 16. On May 7, 1984, Catalyst/Kern River West Cogeneration Partnership, the
4 corporate predecessor of State Street, entered into the PPA with the Debtor. (Id. ¶ 4.) In
5 compliance with the avoided cost requirements under the Public Utilities Regulatory Policies Act
6 of 1978 (16 U.S.C. § 824a-3 et seq.) (“PURPA”), the PPA provides for energy and capacity
7 payments based on the Debtor’s avoided cost. (Id. ¶ 6.)

8 B. The Debtor’s Breach of the PPA and the Effect on the Project.

9 17. Without explanation or justification, the Debtor made only partial payment
10 of the amounts due under the PPA for December 2000 and January 2001, and no payment at all
11 for the amounts due under the PPA for February 2001, or for electric power delivered in March
12 2001. (Id. ¶ 10.) The current outstanding payment obligation owed by the Debtor to the Project
13 for the prepetition period exceeds \$8,807,797. (Id. ¶ 14.)

14 18. The Debtor’s breaches of the PPA have had a severe impact on the
15 Project. On or around February 15, 2001, BP suspended deliveries of natural gas as a result of
16 BP’s reaction to the change in the Debtor’s circumstances. (Id. ¶ 12.) BP demanded that the
17 Project provide a credit facility or cash reserves in an amount approaching \$10 million dollars
18 within 3 business days. This amount was essentially equal to the total dollar amount of fuel
19 purchased by the Project from BP, its chief supplier, in all of 2000. (Id. ¶ 11.)

20 19. The Project has also defaulted on its working capital loans and other debt
21 financing. (Id. ¶ 13.) As a consequence, the Project is now exposed to the risk of foreclosure
22 and may soon require some form of protection to preserve its assets and business. (Id. ¶ 19.)

23 20. Moreover, the Project’s cash in unrestricted accounts except for the
24 Advance, is substantially exhausted. (Id. ¶ 18.)

25 THE COURT SHOULD REQUIRE PG&E TO SET A DATE TO TIMELY
26 ASSUME OR REJECT MOVANT’S PPA AND TO MAKE ADEQUATE
PROTECTION PAYMENTS

27 21. As set forth further in the accompanying Memorandum, section 365(d)(2)
28 of the Bankruptcy Code provides that “the trustee may assume or reject an executory contract . . .

1 at any time before confirmation of a plan, but the court, on the request of any party to such
2 contract . . . may order the trustee to determine within a reasonable period of time whether to
3 assume or reject such contract. . . .” 11 U.S.C. § 365(d)(2).

4 22. What constitutes a “reasonable time” is left to the bankruptcy court’s
5 discretion in light of the circumstances of the case, including:

6 “The nature of the interests at stake, the balance of the hurt to the litigants,
7 the good to be achieved, the safeguards afforded those litigants, and
8 whether the action to be taken is so in derogation of Congress’ scheme
9 that the court may be said to be arbitrary.”

10 Matter of Dunes Casino Hotel, 63 B.R. 939, 949 (D. N.J. 1986) (quoting In re GHR Energy
11 Corp., 41 B.R. 668, 676 (Bankr. D. Mass. 1984)).

12 23. In this case, the Debtor’s prepetition default is not simply substantial; it is
13 devastating for the Project. As catalogued in the accompanying Dean Decl., the Debtor’s
14 prepetition defaults have stripped the Project of performance under the NGSA, depleted its cash
15 resources, and created a precarious situation whereby the amounts that the Debtor now seeks to
16 pay the Project for power are insufficient to service, much less satisfy, the debt created by the
17 Debtor’s prepetition breaches or the new requirements of the Project’s suppliers. (Dean Decl.
18 ¶¶ 17 and 18.)

19 24. Except for the Advance, the Project has had no resources with which to
20 satisfy the new credit requirements of its suppliers. Moreover, it may not be able to make natural
21 gas purchase commitments consistent with prudent risk management (such as the procurement of
22 one month’s natural gas at a firm as opposed to daily spot price) in the foreseeable future absent
23 this Court’s intervention. (Id. ¶ 18.)

24 25. The Project has only one primary source of revenue: the PPA. (Id. ¶ 7.)
25 On the other side of the ledger, the Project has obligations to, among other creditors, its natural
26 gas supplier, and its lenders in addition to normal operational expenses. (Id. ¶ 19.)

27 26. On or around February 15, 2001, BP suspended deliveries of natural gas.
28 (Id. ¶ 12.) The Project was unable to meet the requirements set by BP as assurances of payment
in the near future. Assurances could not be provided directly due to the Debtor’s inability to

1 provide assurances of payment going forward consistent with the new terms stipulated by BP.
2 These new terms had nothing to do with the then financial condition or payment history of the
3 Project. Rather, they were imposed by BP strictly to contend with the Debtor's crisis. (Id. ¶¶ 11
4 and 12.). .

5 27. As a direct result of the Debtor's failure to pay the Project for delivered
6 electricity preceding the commencement of this Chapter 11 case and, except for the Advance, the
7 Debtor's failure to take any meaningful remedial action since, the Project is now caught between
8 the proverbial "rock and a hard place." The Debtor has not provided the Project with the relief it
9 needs to rejuvenate its distressed financial situation and meaningfully address its outstanding
10 obligations to BP, its lenders and other creditors. (Id. ¶¶ 16-18.) Under such circumstances,
11 Movant is entitled to an order from this Court directing the Debtor within 30 days of the date of
12 its order to establish a date certain for the Debtor to assume or reject the PPA, and to file a
13 statement of intention as to when the Debtor intends to so assume or reject, and pending that
14 decision to make semi-monthly payments equal to no less than 5% (per month) of the Prepetition
15 Debt, as well as contract rate payments from the Petition Date and going forward for electricity
16 delivered to PG&E from the Project.

17 CONCLUSION

18 28. For the foregoing reasons, Movant respectfully requests that this Court enter an order
19 (i) compelling PG&E to (a) provide the Project with adequate protection with respect to its
20 interest in its PPA with the Debtor effective August 2, 2001; (b) confirm that the reasonable rate
21 in determining administrative payments for electricity going forward, pending assumption or
22 rejection of the PPA by the Debtor, shall be the contract rate (energy and capacity) provided in
23 the PPA, all other provisions of the PPA remaining in full force and effect; and (c) effective on
24 August 2, 2001, require the Debtor to make semi-monthly payments equal to no less than 5%
25 (per month) of the Prepetition Debt until the Debtor assumes or rejects the PPA; (ii) within 30
26 days of the date of its order, require the Debtor to establish a date certain for the Debtor to
27
28

1 assume or reject the PPA, and to file a statement of intention as to when the Debtor intends to so
2 assume or reject; and (iii) granting such other and further relief as the Court deems just.

3 Dated this day of July 30, 2001.
4

5 Respectfully Submitted.

6 HUGHES HUBBARD & REED LLP

7 By Daniel H. Slate INC

8 Daniel H. Slate
9 Attorneys for Viacom Inc.

10

11

12

13

14

15

16

17

18

19

20

21

22

23

24

25

26

27

28

PROOF OF SERVICE

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

STATE OF CALIFORNIA, COUNTY OF LOS ANGELES

I am employed in the County of Los Angeles, State of California. I am over the age of 18 and not a party to the within action. My business address is 350 South Grand Avenue, Los Angeles, CA 90071.

On July 30, 2001, I served the foregoing document described as **NOTICE OF MOTION AND MOTION OF VIACOM INC. FOR ENTRY OF AN ORDER FOR RELIEF FROM STAY AND FOR ADEQUATE PROTECTION WITH RESPECT TO THE DAI OILDALE PROJECT POWER PURCHASE AGREEMENT**, on the interested parties in this action by placing true and correct copies thereof enclosed in sealed envelopes addressed as indicated on the:

SPECIAL NOTICE LIST

BY MAIL: I am "readily familiar" with the firm's practice of collection and processing correspondence for mailing. Under that practice it would be deposited with U.S. postal service on that same day with postage thereon fully prepaid at Los Angeles, California in the ordinary course of business. I am aware that on motion of the party served, service is presumed invalid if postal cancellation date or postage meter date is more than one day after date of deposit for mailing in affidavit.

BY PERSONAL SERVICE: I caused the above-mentioned document to be personally served to the offices of the addressee.

BY FACSIMILE: I communicated such document via facsimile to the addressee as indicated on the attached service list.

BY FEDERAL EXPRESS: I caused said document to be sent via Federal Express to the addressee as indicated on the attached service list.

Executed this 30th day of July, 2001, at Los Angeles, CA.

(STATE) I declare under penalty of perjury under the laws of the State of California that the above is true and correct.

(FEDERAL) I declare that I am employed in the office of a member of the bar of this court at whose direction the service was made.

Catherine Ryan