

50-275/323

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13 UNITED STATES BANKRUPTCY COURT
14 NORTHERN DISTRICT OF CALIFORNIA

15 In re
16 PACIFIC GAS AND ELECTRIC
17 COMPANY, a California corporation,
18 Debtor.

No. 01-30923 DM
Chapter 11 Case
Date: October 9, 2001
Time: 9:30 a.m.
Place: 235 Pine Street, 22nd Floor
San Francisco, California

19 Federal I.D. No. 94-0742640

20 DEBTOR'S NOTICE OF MOTION AND MOTION FOR ORDER
21 APPROVING SALE OF KERN FACILITY FREE AND CLEAR OF LIENS AND
22 INTEREST; SUPPORTING MEMORANDUM OF POINTS AND AUTHORITIES

23 [SUPPORTING DECLARATIONS OF PAUL V. HOLTON AND MICHAEL J.
24 RUFFATTO FILED SEPARATELY]

25 Note: BNY Western Trust Company should take special notice that the
26 relief requested in this Motion includes, under conditions specified in the
27 Motion, the sale, pursuant to 11 U.S.C. §363(f), of the Kern Facility
28 described in this Motion free and clear of the lien asserted by BNY Western
Trust Company in the Kern Facility.

A001 Add: Kids Ge Mail Center

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1 INTRODUCTION

2 By this Motion, Pacific Gas and Electric Company, the debtor and debtor in
3 possession in this Chapter 11 case ("PG&E" or the "Debtor"), seeks an order pursuant to
4 Section 363(b) and 363(f) of the Bankruptcy Code (11 U.S.C. §363(b), (f))¹ authorizing the
5 sale free and clear of liens of certain real property located in Kern County, California
6 formerly operated as a power generation plant (the "Kern Facility") to North American
7 Power Group, Ltd. ("NAPG"). The only known lien on the property is the lien of BNY
8 Western Trust Company in its capacity as Trustee under the Indenture described in Part III
9 below. The sale will result in a cash payment to PG&E of \$550,000, plus, for all practical
10 purposes as a by-product of the sale transaction, the transfer from PG&E to NAPG of at least
11 approximately \$8 million in liabilities associated with the Kern Facility. In addition, NAPG
12 has agreed to refurbish and restart a non-operational power plant located on the property,
13 thereby increasing the supply of electricity available to California consumers.

14 Prior to PG&E's Chapter 11 filing, PG&E applied to the California Public
15 Utilities Commission ("CPUC") for authorization to sell the Kern Facility pursuant to
16 applicable provisions of the California Public Utilities Code. Despite the significant benefits
17 of the proposed transaction to PG&E, the CPUC refused to authorize the sale. PG&E
18 formally requested reconsideration of that decision on the grounds that it was erroneous as a
19 matter of law and unjustified as a matter of public policy. While such reconsideration
20 request remained pending, and with no action having been taken on it by the CPUC for
21 several months, California Governor Gray Davis on July 30, 2001 issued Executive Order
22 No. D-44-01 (the "Executive Order"), which vacates the CPUC's decision and authorizes the
23 sale of the Kern Facility on certain conditions specified in the Executive Order as described
24 more fully below, including the approval of this Court. A true and correct copy of the
25 Executive Order is attached as Exhibit A to the Declaration of Paul V. Holton filed
26

27 ¹Unless otherwise indicated, all statutory references in this Motion are to the United
28 States Bankruptcy Code (Title 11 of the United States Code).

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1 concurrently herewith (hereinafter referred to as the "Holton Declaration" and cited as the
2 "Holton Decl.").

3
4 I.

5 FACTUAL BACKGROUND²

6 A. The Property

7 The Kern Facility is located in Bakersfield, California. It was the site of a power
8 plant that was built in 1945-50. PG&E operated the plant from 1948 to 1985, when PG&E
9 placed the plant in cold stand-by due to the availability of less expensive sources of energy
10 and capacity. The plant was in cold stand-by until 1994, when the generation production
11 assets were retired from PG&E's books and the plant was shut down. All operational
12 permits associated with the plant have long since expired.

13 The property to be sold consists of approximately 124 out of 155 acres of land
14 owned by PG&E at the site. The Kern Facility, like PG&E's other generating facilities, was
15 built as an integrated utility facility, and the site therefore contains a mixture of generation,
16 transmission and distribution assets. Thus, PG&E will retain approximately 31 acres that are
17 associated with existing transmission and distribution assets at the site and for probable
18 expansion of substations within the next 10 years. PG&E also will retain certain easements
19 on or respecting some portion of the 124 acres to be sold, which easements are necessary for
20 PG&E's transmission substations. With such easements retained, PG&E has no need or
21 reason to maintain fee ownership of the 124 acres that are the subject of the sale.

22 B. The Bidding Process

23 Having determined that it was in PG&E's best interests for PG&E to sell the Kern
24

25 ²The evidentiary basis and support for the facts set forth in this Motion are contained in
26 the Holton Declaration and in the Declaration of Michael J. Ruffatto (hereinafter referred to
27 as the "Ruffatto Declaration" and cited as the "Ruffatto Decl.") filed concurrently herewith.
28 Where there is no citation supporting a particular fact, the evidentiary basis for such fact is
contained in the Holton Declaration. Where, on the other hand, the evidentiary basis for a
particular fact is contained in the Ruffatto Declaration, we will specifically cite to the
Ruffatto Declaration.

1 Facility, PG&E prior to its Chapter 11 filing employed an auction process to obtain the best
2 price from the most qualified buyer. Similar auction processes have been used by PG&E
3 and approved by the CPUC on previous occasions in connection with the divestiture of
4 generation assets. The Kern Facility auction was advertised in the Wall Street Journal and in
5 letters to 300 power companies and real estate developers. These entities had either
6 expressed interest in the property or were identified as potential purchasers. Interested
7 bidders were required to submit a statement of financial and operational qualifications,
8 including audited financial statements, with an explanation how the purchase would be
9 financed, among other items of information. PG&E then provided a Confidential
10 Memorandum and form of Purchase and Sale Agreement to all qualified bidders, which
11 provided an overview of the Kern Facility and the required contractual provisions.

12 All qualified bidders were eligible to submit bids. NAPG prevailed because it
13 presented the highest bid at the auction. The terms of the sale are substantially the same as
14 those proposed to all bidders.³ NAPG and PG&E executed the Purchase and Sale
15 Agreement on August 14, 2000, subject to CPUC approval pursuant to applicable provisions
16 of the California Public Utilities Code. (A true and correct copy of the Purchase and Sale
17 Agreement dated August 14, 2000, as amended to date, is attached as Exhibit B to the
18 Holton Declaration, and, as the same may hereafter be modified consistent with this Motion,
19 hereinafter is referred to as the "Purchase/Sale Agreement.")

20 C. The Purchaser

21 NAPG is a privately held corporation headquartered in Englewood, Colorado.
22 NAPG subsidiaries have offices in Irvine, California. NAPG was formed in late 1992 and
23 began operations in 1993. NAPG develops, owns and operates independent or non-regulated
24 electric generation and energy-related projects in the United States and Canada, and is a full
25

26 ³PG&E did not initially anticipate that the purchaser would restart and operate the Kern
27 Facility. Rather, PG&E assumed that the purchaser would develop new generation at the
28 site. NAPG's plans to restart the existing facility therefore required minor amendments to
the proposed Purchase/Sale Agreement, such as the agreement to move a 70 kV bus
structure and certain water lines.

1 member of the Western Systems Coordinating Council ("WSCC"). It currently owns (alone
2 or in partnership with others) and manages six power generation facilities in California,
3 whose combined output is approximately 158 MW. NAPG also has over 900 MW of sited
4 and fully-permitted power facilities ready for construction within the WSCC region. NAPG
5 also is the sponsor of over 300 miles of additional high voltage transmission lines to improve
6 WSCC reliability. NAPG has no relationship to PG&E or its officers.

7 NAPG's stated plans in purchasing the Kern Facility are to refurbish it and return
8 it to operation as a power generation plant. Ruffatto Decl. ¶4. Having reviewed the
9 Executive Order, NAPG believes it can and will comply with the conditions stated in the
10 Executive Order. Id. ¶3.

11 D. The Purchase/Sale Agreement

12 Under the terms of the Purchase/Sale Agreement, the Kern Facility is being sold
13 "as is." NAPG will bear the costs and risks of restarting the facility, including a major
14 refurbishment of the power plant. As with PG&E's other generation asset divestitures,
15 PG&E will retain its existing environmental liabilities for soil and groundwater
16 contamination to the extent caused by PG&E's operations on the site.

17 The sales price is \$550,000 cash. Further, in connection with the Purchase/Sale
18 Agreement, NAPG for all practical purposes is assuming non-environmental
19 decommissioning obligations for the Kern Facility⁴ of approximately \$8 million.⁵ In
20 addition, as described in more detail in the Purchase/Sale Agreement, PG&E retains
21 responsibility only for environmental costs attributable to any hazardous substances released

22
23 ⁴Although this is a quite complicated regulatory and accounting area, generally stated
24 "non-environmental decommissioning obligations" are the estimated costs to tear a plant
25 down and haul the parts and materials away. They do not include the costs of any
26 environmental remediation.

25 ⁵PG&E has accrued approximately \$10 million for non-environmental
26 decommissioning expenses for the Kern Facility as of July 2000. Upon completion of the
27 sale, this amount will be credited to the Transition Cost Balancing Account ("TCBA").
28 While this \$10 million benefit is not a source of cash, it is a reduction to a future liability
that PG&E would have had absent the sale of the Kern Facility and therefore is of substantial
benefit to PG&E and its bankruptcy estate. Approval of the sale will free up these reserves
for other uses.

1 by PG&E and present on the site as of the closing; NAPG is assuming any other
2 environmental costs.⁶

3 E. The CPUC's Refusal To Authorize The Sale

4 The proposed sale of the Kern Facility was the subject of proceedings before the
5 CPUC prior to the filing of this Chapter 11 case.

6 As a result of AB 1890, PG&E sold its fossil generation assets through an auction
7 process approved by the CPUC. Similar to those sales, PG&E filed an application to sell the
8 Kern Facility with the CPUC on May 15, 2000, pursuant to California Public Utilities Code
9 Sections 367(b) and 851. Holton Decl. Ex. B. The application described the competitive
10 auction process that PG&E would use to obtain the best value and divest itself of the Kern
11 Facility, consistent with the requirements of AB 1890. *Id.*

12 The Office of Ratepayer Advocates ("ORA") did not oppose the application. *Id.*
13 Ex. C. At the time of the filing, PG&E already had notified potential bidders of its intention
14 to auction the Kern Facility as a non-operating generation facility. PG&E indicated in the
15 filing that it began providing the Confidential Information Memorandum and Purchase/Sale
16 Agreement to bidders on April 17, 2000 and final bids were expected by July 21, 2000. The
17 Purchase/Sale Agreement was expected to be executed in August 2000. Consistent with
18 usual practice, PG&E would then file a Supplemental Filing announcing the results of the
19 auction and winning bidder upon execution of the Purchase/Sale Agreement.

20 On December 13, 2000, PG&E filed its Supplemental Filing announcing NAPG
21 as the winning bidder and indicating the intent of NAPG to restart the Kern Facility.

22
23 ⁶The Purchase/Sale Agreement may need to be amended in various technical respects
24 prior to closing, which are either technical and non-material, or beneficial to PG&E. For
25 example, the Purchase/Sale Agreement will be amended to include the requirement in the
26 Executive Order that NAPG enter into cost-based contracts for five years to sell the power
27 produced at the Kern Facility. As another example, PG&E may update the disclosure
28 section to include some recent developments related to environmental conditions at the plant
site. The Purchase/Sale Agreement and sale transaction that PG&E ask this Court to
approve by this Motion include the Purchase/Sale Agreement and transaction as amended by
such amendments, and PG&E by this Motion seeks the authority to proceed to document and
execute such amendments.

1 Although PG&E and NAPG executed the Purchase /Sale Agreement on August 24, 2000,
2 PG&E had to develop an Amendment to the Purchase/Sale Agreement granting both parties
3 easements necessary for NAPG's operation of the facility. Although ORA did not oppose
4 PG&E's original application, it responded to PG&E's Supplemental Filing by requesting
5 that NAPG be required to sell its entire output to PG&E for at least two years at a price that
6 reflects NAPG's actual operating costs. NAPG met with ORA and eventually agreed to this
7 condition.

8 On March 12, 2001, the CPUC issued a draft Decision. The draft Decision held
9 that the proposed sale of the Kern Facility was barred by ABX 6, which amended California
10 Public Utilities Code Section 377. As amended, such Section 377 provides that "no facility
11 for the generation of electricity owned by a public utility may be disposed of prior to January
12 1, 2006. The commission shall ensure that public utility generation assets remain dedicated
13 to service for the benefit of California ratepayers." The opinion also ordered PG&E to
14 restart the Kern Facility itself.

15 Both PG&E and ORA filed comments on the draft Decision, strongly disagreeing
16 with the conclusion that the sale was barred by ABX 6. In their comments, they noted that it
17 is clear from the language of ABX 6 that it was not intended to and does not completely
18 govern PG&E's divestiture of utility property through 2006. While AB 1890 broadly
19 applied to "generation-related assets," ABX 6, by contrast, applies only to "facilities for the
20 generation of electricity." The intent behind AB 1890 was to allow the utilities to recover
21 "stranded costs" associated with any assets that had once been associated with generation,
22 whether or not they remained so associated. Simply stated, if the California Legislature had
23 meant ABX 6 to apply to all of the assets covered by AB 1890, it would have used the same
24 language. Moreover, there is legislative history indicating that ABX 6 was never intended to
25 apply to a property such as the Kern Facility, which had not been operating or producing
26 power for many years.⁷

27 _____
28 ⁷The Legislature's intent in enacting ABX 6 was to require PG&E and Southern

(continued . . .)

1 Moreover, PG&E and ORA demonstrated to the CPUC that PG&E did not have
2 the financial capability to restart and operate the Kern Facility. Restarting the facility would
3 have required PG&E to forego the revenue from the proposed sale and to expend
4 approximately \$50-70 million to restart the Kern Facility and millions more to operate it on
5 an ongoing basis. The CPUC had not provided for those expenditures in retail rates, nor was
6 PG&E able to raise the money from capital markets. Further, NAPG was better positioned

7 (. . . continued)
8 California Edison to retain for a five-year period utility generation facilities that are
9 currently in use to meet retail load. The purpose of the legislation was to preclude for a
10 specified period the CPUC from approving a sale of the remaining utility generation to third
11 parties. Thus, ABX 6 amended California Public Utilities Code Section 377 to read: "The
12 commission shall ensure that public utility generation assets remain dedicated to service for
13 the benefit of California ratepayers." (Emphasis added.) Accordingly, the target of ABX 6,
14 for PG&E, was Diablo Canyon and PG&E's hydro facilities, both of which are sources of
15 power that are currently in use and, according to ABX 6, should be dedicated to meeting
16 retail load.

17 The Bill Analysis prepared by the Senate Energy, Utilities and Communications
18 Committee confirms the intended scope of the ABX 6. It states: "The generation assets in
19 question — those that are retained by the utilities — are Pacific Gas and Electric Company's
20 hydroelectric system and its Diablo Canyon nuclear plant, SCE's hydroelectric system, its
21 interest in the San Onofre nuclear plant and its interest in the Mohave coal-fired plant in
22 Arizona; and SDG&E's interest in the San Onofre nuclear plant."

23 The Kern Facility, by contrast, had not been used to generate electricity since 1985
24 and was removed from rate base in 1994. Thus, the Kern Facility did not currently produce
25 power for PG&E's retail customers and had not done so for over 15 years. The Kern
26 Facility also no longer held a permit for the generation of electricity from the California
27 Energy Commission. In short, the Kern Facility, having not been dedicated to service for the
28 benefit of California ratepayers since 1994, was not subject to the disposition limitations in
California Public Utilities Code Section 377, requiring that currently operating generation
facilities continue in utility service. The force of these arguments was acknowledged in a
second draft CPUC Decision issued on March 27, 2001, holding that Section 377 did not
apply to the Kern Facility.

 PG&E reserves the right to challenge the legality and constitutionality of ABX 6 as
it would apply to PG&E's operating generating facilities that were removed from CPUC
regulation by operation of state law in effect prior to ABX 6. However, given the
Governor's Executive Order waiving the applicability of ABX 6 to the Kern Facility, the
issue of legislative intent as it affects the sale of the Kern Facility has been mooted.

1 to restart the facility more quickly and efficiently than PG&E. In fact, NAPG estimated that
2 it could have begun operating the plant as early as Summer 2001 had the sale been approved
3 by the CPUC. Given the fact that NAPG was willing to provide the output from the Kern
4 Facility on a cost-of service basis for a period of two years, the sale clearly amounted to the
5 best option for all parties involved, including California's ratepayers.

6 Nevertheless, on April 4, 2001, the CPUC issued its final Decision holding that
7 California Public Utilities Code Section 377 precluded the sale, and ordered PG&E to
8 restore the Kern Facility to operational status as soon as possible.

9
10 F. The Governor Overturns The CPUC's Decision And Authorizes The Sale Of The
11 Kern Facility To NAPG

12 On April 16, 2001, PG&E filed an Application For Rehearing of Decision 01-04-
13 004. NAPG also filed a Motion for Reconsideration and Rehearing on April 16. In addition,
14 NAPG approached various legislators in an effort to resolve the issue via new legislation.
15 Although noticed several times on its public meeting agenda, the CPUC delayed issuing a
16 decision on the two applications for rehearing.⁸ The California Senate and Assembly
17 eventually passed ABX2-19 on July 12 and July 14, respectively. ABX2-19 would have
18 exempted the Kern Facility from California Public Utilities Code Section 377(b) and
19 allowed the sale to NAPG to occur conditioned upon NAPG entering into a contract
20 approved by the CPUC to sell the power produced by the Kern Facility at cost-based rates.
21 However, ABX2-19 was withdrawn before Governor Davis could sign it.

22 Instead, on July 30, 2001, Governor Davis signed the Executive Order pursuant
23 to the California Emergency Services Act, California Government Code 8550 et seq., and
24 thereby at once mooted the need for ABX2-19 and overrode the CPUC. The Executive
25 Order specifically found that "the prohibition against the sale of generation assets in Public
26

27 ⁸As of the date of this Motion, the CPUC has not issued a decision addressing the
28 Applications for Rehearing filed by PG&E and NAPG.

1 653, 659 (B.A.P. 9th Cir. 1996) (“valid business justification”); In re Lady H Coal Co. Inc.,
2 193 B.R. 233, 243 (Bankr. S.D. W. Va. 1996) (“sound business purpose”); WBQ P’ship v.
3 Commonwealth of Virginia Dept. of Med. Assistance Servs. (In re WBQ P’ship), 189 B.R.
4 97, 102 (Bankr. E.D. Va. 1995) (adopting the “‘sound business purpose’ test”); In re
5 Weatherly Frozen Food Group, Inc., 149 B.R. 480, 482-83 (Bankr. N.D. Ohio 1992) (“sound
6 business purpose”); see also Abel v. Shugrue (In re Ionosphere Clubs, Inc.), 184 B.R. 648,
7 653 (S.D.N.Y. 1995) (§363(b) “sales are not limited to emergencies”); In re America West
8 Airlines, Inc., 166 B.R. 908, 912 (Bankr. D. Ariz. 1994) (considering whether transaction is
9 “in the best interests of the estate”); In re Wilde Horse Enterprises, Inc., 136 B.R. 830, 841
10 (C.D. Cal. 1991) (requiring articulated business reason and finding that “sale is in best
11 interest of the estate”).

12 In applying the sound business purpose test, courts consider four elements: (1) a
13 sound business reason or emergency justifying a pre-confirmation sale; (2) good faith; (3)
14 adequate and reasonable notice to interested parties; and (4) fair and reasonable purchase
15 price. In re WBQ P’ship, 189 B.R. at 102; see also In re Lady H Coal Co., 193 B.R. at 243;
16 Titusville Country Club v. Pennbank (In re Titusville Country Club), 128 B.R. 396, 399
17 (Bankr. W.D. Pa. 1991). Each of these elements are met in the present case.

18 A. PG&E Has Articulated a Sound Business Reason for the Sale

19 The Kern Facility is currently inoperative and does not present a viable source of
20 income for PG&E. In fact, PG&E faces large liabilities related to the cost of non-
21 environmental decommissioning. The proposed sale will eliminate these liabilities
22 (expected to amount to approximately \$8 million) and provides PG&E with proceeds of
23 \$550,000. In addition, NAPG has agreed to provide to California the electricity that it
24 generates on a cost-of-production basis.

25 Finally, the sale makes good sense. The public interest may be taken into account
26 in determining whether a sound business reason for the sale exists. In In re Lady H Coal
27 Co., 193 B.R. at 243 & 245, for example, the court approved the sale of a coal mine over
28 piecemeal liquidation of assets in part because the purchaser expected to operate the mine,

1 employ people in the community, retain 25% of the debtor's union workforce, and make
2 substantial capital expenditures to improve the productivity of the property.

3 Similarly, the sale of the Kern Facility will provide an additional source of energy
4 for consumption by California's citizens and businesses in the quickest and most efficient
5 manner available. The importance of this deal to the State of California is clearly evidenced
6 by the Governor's Executive Order aimed specifically at facilitating the sale notwithstanding
7 the CPUC's refusal to approve the transaction.

8 B. The Sale Has Been Proposed In Good Faith

9 "Good faith encompasses fair value, and further speaks to the integrity of the
10 transaction. Typical bad faith or misconduct, would include collusion between the seller and
11 buyer, or any attempt to take unfair advantage of other potential purchasers." 240 North
12 Brand Partners, 200 B.R. at 659 (quoting In re Wilde Horses, 136 B.R. at 842).

13 The Purchase/Sale Agreement is the result of a public auction process that has
14 been used by PG&E and approved by the CPUC on previous occasions in connection with
15 the divestiture of generation assets. As described in detail in Part IA above, this process
16 produced the best bid from a qualified arm's-length purchaser among a pool of qualified
17 purchasers.

18 The method of choosing the purchaser and the neutral terms of the sale
19 demonstrate that the sale is proposed in good faith. See, e.g., In re Weatherly Frozen Food
20 Group, Inc., 149 B.R. at 483 (finding good faith because offer negotiated at arms' length and
21 no director of debtor held any interest or was otherwise related to the prospective purchaser).

22 C. Interested Parties will Receive Adequate and Reasonable Notice

23 In the context of a Section 363(b) sale, "notice is sufficient if it includes the terms
24 and conditions of the sale, if it states the time for filing objections, and if the estate is selling
25 real estate, it generally describes the property." In re WBQ Partnership, 189 B.R. at 103
26 (quoting In re Karpe, 84 B.R. 926, 930 (Bankr. M.D. Pa. 1988)).

27 PG&E is noticing this Motion to, and serving it and the accompanying
28 Memorandum of Points and Authorities on, the full Special Notice List established pursuant

1 to the Case Management Order entered in this case. This satisfies the reasonable and
2 adequate notice requirement because such served documents describe the property, include
3 the terms and conditions of the sale, and state the time for filing any objections or opposition
4 thereto.

5 D. The Purchase Price Is Fair and Reasonable

6 The highest bid procured at a public auction is, by definition, a fair and
7 reasonable price for property. In New Haven Radio, Inc. v. Meister (In re Martin-Trigona),
8 760 F.2d 1334 (2d Cir. 1985), for example, the Second Circuit held that a bid procured at a
9 public auction was reasonable, even assuming that the appraisal value was higher. See also
10 In re Abbotts Dairies, Inc., 788 F.2d 143, 149 (3d Cir. 1986) (“[g]enerally speaking, an
11 auction may be sufficient to establish that one has paid ‘value’ for the assets of a bankrupt”);
12 In re WBQ P’ship, 189 B.R. at 104 (“a public auction can serve the interests of creditors
13 more than a private deal reached between a Chapter 11 debtor and a prospective buyer”); In
14 re Ohio Corrugating Co., 59 B.R. 11, 12 (Bankr. N.D. Ohio 1985) (holding that method of
15 sale providing fullest measure of fairness is a public auction).

16 PG&E conducted a public auction by a process used and approved in the past by
17 the CPUC for the divestiture of generation assets. NAPG’s bid was the highest bid received
18 at that appropriately publicized auction and therefore constitutes a fair and reasonable price
19 for the property on the terms proposed to all bidders by PG&E.

21 III.

22 THE COURT SHOULD AUTHORIZE THE SALE OF THE KERN
23 FACILITY FREE AND CLEAR OF ALL LIENS AND INTERESTS

24 PG&E requests that this Court approve the sale of the Kern Facility to NAPG free
25 of all liens and interests pursuant to Bankruptcy Code Section 363(f).

26 Section 363(f) allows for sales of property of the estate “free and clear of any
27 interest” if any one of the following five conditions are met:

- 28 1. applicable nonbankruptcy law permits sale of such property free

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- 1 and clear of such interest;
- 2 2. such entity consents;
- 3 3. such interest is a lien and the price at which such property is to
4 be sold is greater than the aggregate value of all liens on such
5 property;
- 6 4. such interest is in bona fide dispute; or
- 7 5. such entity could be compelled, in a legal or equitable
8 proceeding, to accept a money satisfaction of such interest.

9 11 U.S.C. §363(f). These conditions are stated in the disjunctive and satisfaction of any one
10 of the five conditions will justify a sale free and clear of liens and interests pursuant to this
11 section. See, e.g., Citicorp Homeowners Servs., Inc. v. Elliott (In re Elliott), 94 B.R. 343,
12 345 (E.D. Pa. 1988); Hargrave v. Township of Pemberton (In re Tabone, Inc.), 175 B.R.
13 855, 858 (Bankr. D.N.J. 1994).

14 PG&E is only aware of one lien on the Kern Facility. That is the lien on
15 substantially all assets of PG&E in favor of BNY Western Trust Company in its capacity as
16 the successor trustee (the "Trustee") under that certain Indenture dated December 1, 1920 as
17 amended to date, which is the subject of that certain "Stipulation (I) Authorizing and
18 Restricting Use of Cash Collateral Pursuant to 11 U.S.C. §363 and Bankruptcy Rule 4001
19 and (II) Granting Adequate Protection Pursuant to 11 U.S.C. §§361 and 363" entered into
20 between PG&E and the Trustee on May 9, 2001 (the "Cash Collateral Stipulation") and
21 approved by the Bankruptcy Court by its Order thereon dated the same date. As part of the
22 Cash Collateral Stipulation, the Trustee and PG&E agreed as follows:

23 Except for transactions in the ordinary course of its business or except
24 as otherwise permitted in the Indenture or authorized by an order of
25 this Court (after notice to the Indenture Trustee), the Debtor shall not
26 sell, transfer, lease, encumber or otherwise dispose of any Pre-Petition
27 Collateral or Post-Petition Collateral without the prior written consent
28 of the Indenture Trustee, and no such consent shall ever be implied
from any other action, inaction or acquiescence by the Indenture
Trustee or any Bondholder. The Indenture Trustee expressly
authorizes the Debtor to sell assets pursuant to Section 363(f) of the
Bankruptcy Code free and clear of any liens, claims or encumbrances
of the Indenture Trustee to the extent such sales are permitted by the
Indenture and so long as the liens, claims or encumbrances of the
Indenture Trustee shall attach to the proceeds of such sales with the

1 same validity and priority as the liens, claims and encumbrances of the
2 Indenture Trustee in the assets subject to such sales, until the
3 disposition of such proceeds in accordance with the Indenture and
4 applicable bankruptcy law. (Cash Collateral Stipulation ¶13)

5 Pursuant to the Cash Collateral Stipulation, PG&E will comply with the
6 applicable provisions of the Indenture regarding the release/reconveyance of the Trustee's
7 lien on property to be sold, which in this case will result in (i) PG&E delivering a Board
8 resolution, an opinion of in-house counsel and certain certificates to the Indenture Trustee
9 pursuant to the Trust Indenture, and (ii) PG&E agreeing in escrow instructions that the net
10 proceeds of sale (i.e., the \$550,000 gross proceeds minus the direct costs of sale paid
11 through escrow) be delivered to the Trustee upon closing as a condition to the title
12 company's entitlement to rely on and record the appropriate release/reconveyance that the
13 Trustee will deliver into escrow. Further, in order to flesh out the application of the Cash
14 Collateral Stipulation to this sale and move forward with this sale with the consent of the
15 Trustee, PG&E has agreed with the Trustee (and hereby incorporates into the Motion) that
16 the net proceeds of the sale of the Kern Facility to be paid over to the Trustee upon closing
17 will be held by the Trustee in a segregated account as cash collateral for PG&E's obligations
18 under the Indenture, and such proceeds shall not be released to PG&E unless and until either
19 (i) the Trustee has consented in writing to the release of such proceeds to PG&E, or (ii) this
20 Court orders the Trustee to release such proceeds following a noticed motion and hearing
21 thereon, any such motion to be served upon the Trustee no less than 28 days prior to the
22 scheduled hearing date. In connection with any such motion, PG&E reserves the right to
23 argue that the Trustee is required pursuant to the applicable provisions of the Indenture to
24 release some or all of the net proceeds of this sale that are held by the Trustee as cash
25 collateral, and/or that the Trustee's interest in PG&E's property is adequately protected
26 without regard to such cash collateral; and the Trustee reserves the right to oppose any or all
27 such arguments and to make any and all adequate protection arguments that it deems
28 appropriate.

Although PG&E is not aware of any other liens on the Kern Facility, PG&E notes

1 that a number of courts have held that failure to object to the sale after notice and a hearing
2 constitutes implied consent sufficient to satisfy the requirement of Section 363(f)(2). See,
3 e.g., Veltman v. Whetzal, 93 F.3d 517, 521 (8th Cir. 1996) (noting that some courts have
4 found implied consent upon a failure to object); Elliott, 94 B.R. at 345 (holder of first
5 mortgage on debtor's property "consented to the sale by failing to make any timely objection
6 after receiving notice of the sale. . . . [I]mplied consent is sufficient to authorize a sale under
7 §362(f)(2)"); In re Tabone, Inc., 175 B.R. at 858 ("As the Township did not offer any
8 objection, it may be deemed to have consented to the sale for purposes of section
9 363(f)(2)"); In re Shary, 152 B.R. 724, 725 (Bankr. N.D. Ohio 1993) ("[T]he State's failure
10 to object to the sale, or the confirmation of the sale, implicitly conveyed its consent to the
11 sale as found under §362(f)(2)"); but see In re Roberts, 249 B.R. 152, 157 (Bankr. W.D.
12 Mich. 2000) (rejecting implied consent theory despite the fact that "every published opinion
13 and the leading bankruptcy treatises support the . . . contention that the consent required by
14 Section 363(f)(2) may be implied by the lienholder's failure to object").

15 Therefore, to the extent there are any other holders of liens or other interests in
16 the Kern Facility who are on notice of this Motion and who fail to object to this Motion,
17 their consent may be implied and the sale authorized free and clear of those liens and
18 interests pursuant to Section 363(f)(2).

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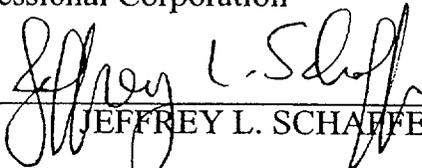
CONCLUSION

For all of the foregoing reasons, PG&E respectfully requests that this Court exercise its power pursuant to Sections 363(b) and (f) of the Bankruptcy Code to authorize the sale of PG&E's Kern Facility to NAPG free and clear of liens and interests on the terms and conditions specified in the Purchase/Sale Agreement.

DATED: September 5, 2001

Respectfully,

HOWARD, RICE, NEMEROVSKI, CANADY,
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A Professional Corporation

By:  _____
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