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UNITED STATES OF AMERICA
BEFORE THE
NUCLEAR REGULATORY COMMISSION

DOCKETED
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OFFICE OF SECRETARY
RULEMAKINGS AND
ADJUDICATIONS STAFF

In the Matter of Pacific Gas and Electric Company Application for License Transfers and Conforming Administrative License Amendments for Diablo Canyon Power Plant, Units 1 and 2	Docket Nos. 50-275, 50-323

PETITION OF THE CALIFORNIA PUBLIC UTILITIES COMMISSION FOR LEAVE TO INTERVENE, AND MOTION TO DISMISS APPLICATION, OR IN THE ALTERNATIVE, REQUEST FOR STAY OF PROCEEDINGS, AND REQUEST FOR SUBPART G HEARING DUE TO SPECIAL CIRCUMSTANCES

February 5, 2002

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Exhibit A: "California Public Utilities Commission's Objection to Proposed Disclosure Statement for Plan of Reorganization Under Chapter 11 of the Bankruptcy Code for Pacific Gas and Electric Company Proposed by Pacific Gas and Electric Company and PG&E Corporation," filed on November 27, 2001 in the case, *In re Pacific Gas and Electric Company*, United States Bankruptcy Court Northern District of California, San Francisco Division, Case No. 01-30923 DM

Exhibit B: "Objection To Pacific Gas & Electric Company's Second Motion For Order Further Extending Exclusivity Period For Filing Plan Of Reorganization To Permit The California Public Utilities Commission To File An Alternate Plan Of Reorganization," filed on January 8, 2002 by the California Public Utilities Commission in the case, *In re Pacific Gas and Electric Company*, United States Bankruptcy Court Northern District of California, San Francisco Division, Case No. 01-30923 DM

Exhibit C: "The Commission's Memorandum In Further Support Of Its Objection To Proposed Disclosure Statement For Plan Of Reorganization Under Chapter 11 Of The Bankruptcy Code For Pacific Gas And Electric Company," filed on January 8, 2002 by the California Public Utilities Commission in the case, *In re Pacific Gas and Electric Company*, United States Bankruptcy Court Northern District of California, San Francisco Division, Case No. 01-30923 DM

Exhibit D: "Motion for Summary Disposition, or in the Alternative, Protest and Request for Consolidation and Hearing, of the Public Utilities Commission of the State of California," filed on January 29, 2002 in *Pacific Gas and Electric Company, et al.*, Federal Energy Regulatory Commission, Docket Nos. EC02-31-000, EL02-36-000 and CP-02-38-000

Exhibit E: "Motion to Dismiss, or, in the Alternative, Protest and Request for Hearing, and Comments of the Public Utilities Commission of the State of California," filed on January 29, 2002 in *Pacific Gas and Electric Company, et al.*, Federal Energy Regulatory Commission, Docket No. ES02-17-000

Exhibit F:	"Motion for Summary Disposition, or in the Alternative, Protest and Request for Consolidation and Hearing, of the Public Utilities Commission of the State of California," filed on January 29, 2002 in *Electric Generation LLC*, Federal Energy Regulatory Commission, Docket No. ER02-456-000
Exhibit G:	Declaration of David R. Effross
Exhibit H:	*Oakland Tribune*, February 1, 2002, copy of newspaper article, "New Terror Attacks on U.S. Predicted/ Nuclear reactor seen as possible target"
Exhibit I:	Diablo Canyon Independent Safety Committee, Annual Report, covering July 1, 2000 through June 30, 2001

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In the Matter of Pacific Gas and Electric Company Application for License Transfers and Conforming Administrative License Amendments for Diablo Canyon Power Plant, Units 1 and 2	Docket Nos. 50-275, 50-323

PETITION OF THE CALIFORNIA PUBLIC UTILITIES COMMISSION FOR LEAVE TO INTERVENE, AND MOTION TO DISMISS APPLICATION, OR IN THE ALTERNATIVE, REQUEST FOR STAY OF PROCEEDINGS, AND REQUEST FOR SUBPART G HEARING DUE TO SPECIAL CIRCUMSTANCES

Pursuant to 10 CFR §§ 2.1306, 2.1309 and 2.1329(b), the Public Utilities Commission of the State of California ("CPUC") hereby petitions for leave to intervene in the pending Application of the Pacific Gas and Electric Company ("PG&E") to transfer the operating licenses for the Diablo Canyon Power Plant ("DCPP") Units 1 and 2 to a new operating and generating company named Electric Generation LLC ("Gen") and to transfer the ownership of the DCPP units to a new, wholly owned subsidiary of Gen named Diablo Canyon LLC ("Diablo") submitted in the above-captioned dockets (the "Application"), moves to dismiss the Application, or, in the alternative, requests a stay of the proceedings, and requests the United States Nuclear Regulatory Commission ("NRC" or "Commission") to conduct a hearing on the Application.

Communications to the CPUC in this matter should be addressed to:

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In support of its Petition for Intervention, its Motion to Dismiss the Application, or, in the alternative, to stay the proceedings, and its request for a subpart G hearing due to special circumstances, and pursuant to 10 CFR § 2.1306, the CPUC identifies herein below, and in the various Exhibits hereto, the issues it seeks to raise, as well as (i) a demonstration that these issues are within the scope of the proceeding, (ii) a demonstration that these issues are relevant to the findings that the NRC must make in order to grant PG&E's requested transfer, (iii) a statement of the facts and expert opinion supporting the CPUC's position and its requests, and (iv) information showing that a genuine dispute exists with PG&E on material issues of fact and fact.

Finally, if and when the Commission moves forward in this matter, the CPUC also requests, pursuant to 10 C.F.R. §2.1329(b), due to the "special circumstances concerning the subject of the hearing" that the Commission hold a substantive subpart G hearing. The CPUC contends that due to the complex nature of the legal, policy and factual issues it raises, as set forth herein below, the application of subpart M, particularly in cross examination and discovery, would not serve the purposes for which the rule was intended -- full and fair hearing on license transfer on an expedited basis. The CPUC contends that upon careful examination of the materials provided herein below and attached hereto, the Commission will have an adequate basis to determine that the matters in this license transfer are not strictly "financial in nature" as contemplated in the promulgation of Subpart M. In this regard, the Commission's ruling in *Niagara Mohawk Power Corporation, New York State Electric & Gas Corporation, and AmerGen Energy Company, LLC* (Nine Mile Points, Units 1 & 2), 50 NRC 333, 1999 NRC LEXIS 115 at *18-19 (December 22, 1999), is distinguishable from the instant case. In this case, there are fundamental legal issues at stake, as well as important considerations of public policy, national security and public health and safety, not merely administrative determinations concerning the paper transfer of a the license and conforming of technical specifications to reflect such a mere paper change.

The CPUC contends that the Commission will completely abdicate its responsibility to protect public health and safety, and thereby abdicate its duty to safeguard the national interest under the Atomic Energy Act, §§ 105, 184, 189a, if it permits the license transfer at issue to go forward as a purely ministerial determination without considering the extensive substantive issues surrounding this particular proposed license transfer. Such issues will only receive adequate attention in the context of a full adjudicatory hearing process with the right to call for evidence, present evidence, and cross examine evidence.

In support of the above motions and requests, the CPUC sets forth as follows:

I. THE INTERESTS OF THE CPUC IN THIS MATTER AND MOTION TO DISMISS

The CPUC is a constitutionally established agency charged with the responsibility for regulating electric corporations within the State of California. In addition, the CPUC has a statutory mandate to represent the interests of electric consumers throughout California in proceedings before the Commission. The CPUC currently exercises regulatory authority over DCPP. As is set forth in detail below, these fundamental interests and responsibilities of the CPUC are directly threatened by the proposed license transfer at issue in this Application.

A. PG&E's NOVEMBER 30 FILINGS

On November 30, 2001, PG&E submitted this Application, as well as a voluminous and complex series of filings before the Federal Energy Regulatory Commission ("FERC"), (collectively, the "November 30 Filings") as part of the implementation of PG&E's proposed Plan of Reorganization under Chapter 11 of the Bankruptcy Code ("Plan"). The Plan was jointly filed by PG&E and its holding company parent, PG&E Corporation ("Parent"), with the Bankruptcy Court on September 20, 2001. PG&E's Plan involves a complex disaggregation of various businesses within PG&E and the spin-off of its distribution business to a Reorganized PG&E, which will be a separate company that will no longer be affiliated with the remainder of the disaggregated businesses. In effect, the current vertically-integrated PG&E will become a distribution company only and its generation, electric transmission and gas storage and transmission operations will be unbundled into separate companies that remain affiliated with one another under the Parent, but unaffiliated with Reorganized PG&E. Under this Plan, only this Reorganized PG&E will be subject to CPUC regulation. Indeed, as the CPUC has recently stated in its November 27, 2001 bankruptcy filing in response to PG&E's proposed disclosure statement:

> "Through its Plan and Disclosure Statement PG&E seeks to affect a regulatory jailbreak unprecedented in scope in bankruptcy annals. Under the guise of section 1123(a)(5) of the Bankruptcy Code and through a misapplication of the debtor protection provisions of chapter 11, PG&E seeks sweeping preemptive relief primarily in the form of no fewer than fifteen affirmative declaratory and injunctive rulings, each designed to permanently dislocate various state and local laws and regulations affecting PG&E's operation of its public utility. (Fn omitted). PG&E's Plan is concerned only secondarily with adjusting debtor-creditor relations and restoring its utility operations to financial health. To be sure, if those were PG&E's primary concerns, then it would have proposed a much more straightforward reorganization strategy. PG&E has as its own agenda an escape from CPUC and State regulation.[1]"

The November 30 Filings are highly controversial. The various applications before the FERC, together with this Application before the NRC, are inextricably linked, and the November 30 Filings involve complex legal issues that will be heavily contested. The NRC and the FERC will be required to carefully scrutinize these applications, as they raise difficult legal issues in order to ultimately determine whether PG&E's filings

[1] "California Public Utilities Commission's Objection to Proposed Disclosure Statement for Plan of Reorganization Under Chapter 11 of the Bankruptcy Code for Pacific Gas and Electric Company Proposed by Pacific Gas and Electric Company and PG&E Corporation," filed November 27, 2001, *In re Pacific Gas and Electric Company*, United States Bankruptcy Court Northern District of California, San Francisco Division , Case No. 01-30923 DM, at 3. A copy of the CPUC's November 27, 2001 filing in that case is attached as Exhibit A to this pleading.

are in the public interest, and meet related statutory requirements. PG&E has not sought state-required approvals for any of its proposals, asserting that all state law is preempted by section 1123(a)(5) of the Bankruptcy Code. This assertion is being vigorously challenged by the CPUC, the State of California, and other parties before the Bankruptcy Court.

The CPUC submits that the November 30 Filings, including this Application, are premature and must be dismissed. The November 30 Filings seek to implement PG&E's Plan of Reorganization ("Plan") on file with the Bankruptcy Court. The November 30 Filings thus assume the legal validity of the Plan, and assume that the Plan will move forward. Both of these critical assumptions underlying the November 30 Filings may be, and in the CPUC's view are, incorrect. Moreover, the Bankruptcy Court is expected to issue rulings on these matters in the near future. The Bankruptcy Court's ruling on certain facial preemption issues, discussed further below, will determine whether PG&E's plan is lawful and may move forward at all. The Bankruptcy Court's ruling on whether the CPUC may file an Alternative Plan, also discussed below, will bear on, if lawful, whether and to what extent PG&E's Plan moves forward. Accordingly, PG&E's pending Application in this matter should be dismissed pending orders from the Bankruptcy Court. In the alternative, the Commission should stay all proceedings in this matter, and should defer taking any action on PG&E's Application herein until the complex legal issues being addressed in the Bankruptcy Court -- which issues directly bear on PG&E's authority even to submit this Application -- are resolved. A failure to deny this motion will necessarily result in wasteful, expensive and possible useless proceedings, the results of which, depending on the rulings of the Bankruptcy Court, could well have to be undone.

B. THE ALTERNATIVE PLAN

On January 16, 2002, the Bankruptcy Court held a hearing on PG&E's motion to extend the period in which PG&E has an exclusive right to propose plans of reorganization beyond February 4, 2002. The CPUC, the State of California on behalf of various state agencies, and others opposed PG&E's motion. The CPUC has developed and is prepared to file in short order an Alternative Plan of Reorganization ("Alternative Plan"). Unlike the PG&E Plan, the Alternative Plan does not require disassembling the nation's largest public utility, and does not require either the Bankruptcy Court or FERC to reject the application of century-old state regulatory statutes critical to health, safety, and welfare of thirty million citizens. The Bankruptcy Court did not issue a final ruling on the motion at the January 16 hearing. Rather, the Bankruptcy Court provided the CPUC until February 13, 2002 to provide the Bankruptcy Court with a term sheet demonstrating that the CPUC's proposed Alternative Plan is feasible.[2] Upon review of the term sheet, the Bankruptcy Court will rule on whether the CPUC will be permitted to file the Alternative Plan.

A copy of the CPUC's "Objection To Pacific Gas & Electric Company's Second Motion For Order Further Extending Exclusivity Period For Filing Plan Of Reorganization To Permit The California Public Utilities Commission To File An Alternate Plan Of Reorganization" is attached hereto as Exhibit B. The following are

[2] The Bankruptcy Court extended the exclusivity period as to all parties other than the CPUC to June 30, 2002.

certain of the significant provisions of the CPUC's Alternative Plan:

- PG&E's short-term borrowings incurred during the energy crisis would be paid in full in cash (including accrued and unpaid interest through the effective date) by the first quarter of 2003 through a combination of PG&E's cash on hand (approximately $4.9 billion as of November 30, 2001 according to PG&E's most recent 8-K filing with the SEC)[3] and PG&E's residual revenues after deducting authorized revenue requirements from billed revenues ("residual revenues");

- all of PG&E's remaining indebtedness would be reinstated or refinanced;

- PG&E's creditworthiness and financial viability would be restored – the Commission would adopt a post-bankruptcy rate structure consistent with state law that would provide PG&E with an opportunity to earn a reasonable return that would allow it to maintain an investment-grade credit rating;

- valuable claims against the Parent (which under PG&E's Plan are to be released)[4] and other assets such as PG&E's refund claims pending before FERC would be preserved and transferred to a litigation trust or similar entity and prosecuted for the benefit of PG&E's ratepayers;

- costly and time-consuming preemption litigation would be avoided;

- PG&E would emerge promptly from chapter 11;

- the Commission and State of California would continue to regulate PG&E's operations;

- PG&E's integrated operations would not be disaggregated;

- rates would not increase, and may be reduced in 2003 (or earlier);

- utility assets would not be diverted to pay the Parent's expenses; and

- costly litigation at the FERC, NRC and SEC would be avoided.

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3 The CPUC expects this number to increase over time.

4 These claims include, among others, claims that the Parent has violated the "first priority" condition imposed upon the Parent by a Commission order approving PG&E's holding company structure and claims that PG&E declared and paid dividends to its Parent while it was insolvent.

The Alternative Plan reflects the fact that wholesale market prices have declined during the last six months, while the CPUC has increased PG&E's retail rates by over 30% since January 2001. As press reports have noted,

> "The PUC came up with a straightforward plan based on cash flow to put Southern California Edison back in the black. Why can't it do the same with PG&E? If it can, the court should pay attention. Bankruptcy court is supposed to be about debtors paying creditors, not about debtors seeking to shed regulation."

Sacramento Bee, Editorial: "PG&E solution: Nothing? Cash flow may easily resolve bankruptcy," Jan. 10, 2002.

If, as the CPUC anticipates, the Bankruptcy Court terminates PG&E's exclusivity period and permits the CPUC to file the Alternative Plan, it will be impossible to know which, if either, of the two plans the Bankruptcy Court will approve. If the Alternative Plan is approved, the November 30 Filings, including this Application, will be moot.[5]

The November 30 Filings assume PG&E's view of the world. It is far from certain that that view will prevail in the Bankruptcy Court. Should the proceedings in this matter nonetheless proceed, both the NRC and the parties will be required to expend very significant resources vigorously litigating proceedings which may well become moot.[6] There is a better course. The NRC should dismiss PG&E's Application in this

[5] An illustrative example of how such circumstances should play out is demonstrated by the decision of the FERC in the case of *Committee of Certain Members of Cajun Electric Power Cooperative, Inc.*, 87 FERC ¶ 61,129 (2001) ("*Cajun*"). In *Cajun*, FERC dismissed as premature a petition which was "based on the possibility that the Bankruptcy Court may adopt" one of two pending, competing plans of reorganization. Id. The same result should obtain in this case, both before the FERC and before the NRC.

[6] Such premature litigation is to the detriment of PG&E and its creditors as well as to protesting parties and FERC. For instance, for the month of November 2001, outside counsel involved in the preparation of PG&E's Section 7 filing CP02-39-000 et al. (Winston & Strawn), billed the estate $358,222.38. Counsel involved in the preparation of the ETrans filing, ER02-455-000 (Skadden, Arps), charged PG&E, $410,790.87, for October 2001, and $382,252.71

matter, without prejudice, as premature. PG&E could subsequently re-file any applications necessary to implement an approved bankruptcy reorganization plan at the appropriate time. One thing, however, is sure; in the event that the CPUC's Alternative Plan is adopted, any application to the NRC for a license transfer for DCPP will look very different from PG&E's present Application.[7]

C. THE PREEMPTION HEARING

PG&E's Plan relies heavily on its assertion that central features of the California Public Utilities Code, which are generally applicable to all public utilities in the state, are preempted by the Bankruptcy Code, and consequently that PG&E needs neither to seek nor to obtain approval by the state of any part of the transactions proposed in the November 30 Filings and in the Plan. The CPUC, the State of California, representing other state agencies, and others have objected that PG&E's unlawful misuse of the Bankruptcy Code renders the Plan unconfirmable on its face. That is, under existing law, the Bankruptcy Court cannot lawfully approve the Plan as proposed. The Ninth Circuit has held in *Baker & Drake Inc. v. Public Service Commission of Nevada, 35 F.3d 1348 (9th Cir. 1994), that the Bankruptcy Code does not preempt state sta*tutes or regulations intended to protect the public safety and welfare. According to the Ninth Circuit, state statutes may be preempted by the Bankruptcy Code only if, at a minimum, they are directed narrowly and solely at economic regulation, and if certain other factors apply.

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for November 2001. These figures do not even include amounts billed by Dewey Ballantine, counsel on the Section 203 and other applications.

[7] At the January 16, 2002, hearing the Bankruptcy Court also issued an oral order to show cause as why PG&E and the CPUC should not be required to enter into court appointed mediation, which would be paid for by the Debtor's estate. The Bankruptcy Court has asked these two parties to respond by January 25, 2002.

The provisions of the Public Utilities Code that PG&E seeks to preempt protect the public safety and welfare, and accordingly preemption cannot occur. That is true even if enforcement of the challenged provisions of state law would make a bankruptcy reorganization more difficult, or even impossible. A copy of the CPUC's "Memorandum In Further Support Of Its Objection To Proposed Disclosure Statement For Plan Of Reorganization Under Chapter 11 Of The Bankruptcy Code For Pacific Gas And Electric Company" is attached hereto as Exhibit C.

The Bankruptcy Court held a hearing on the preemption issues on January 25, 2002 and took the issues raised during the hearing under review. A ruling on these issues is expected to occur within the next few weeks. A ruling in the CPUC's favor would doom PG&E's Plan, as it would not be feasible as a matter of law. Such a ruling would require submission, either by PG&E or another party, of a new, lawful, Plan, and moot the November 30 Filings, including PG&E's Application herein. In any event, it is expected that the Court's ruling on these preemption issues are likely to be appealed, and a final resolution of these issues could be many months in the future. It would therefore be an extraordinary waste of resources to proceed on this Application pending the Bankruptcy Court's ruling on the facial preemption issue and the outcome of any appeals of that ruling. Accordingly, the CPUC submits that the NRC should dismiss this Application without prejudice until these preemption issues are finally resolved.

D. ALTERNATIVE MOTION TO STAY PROCEEDINGS

In the alternative, in the event that the NRC declines to dismiss this Application, the NRC should issue an order staying the proceedings in this matter. For the same reasons set forth above, there is little reason for the parties or the NRC to expend the resources necessary to litigate these proceedings given the current uncertainty as to whether PG&E's plan is lawful, and whether the CPUC will be permitted to submit its Alternative Plan as an alternative plan to PG&E's current Plan.

If the Bankruptcy Court rules against PG&E on preemption, PG&E's Plan falls apart and the November 30 Filings, including this Application, are moot. If the Bankruptcy Court permits the filing of an alternative plan, it will be impossible to know which, if either, of the two plans the Bankruptcy Court will approve.

Accordingly, if the NRC does not determine to dismiss these proceedings altogether, the NRC should certainly to hold the matter in abeyance until the Bankruptcy Court's rulings on the preemption issue and on the filing of the Alternative Plan have been finalized.

II. THE REQUEST FOR AUTHORIZATION TO TRANSFER NUCLEAR DECOMMISSIONING TRUST FUNDS MAY NOT LAWFULLY BE APPROVED BY THE NRC

In its application, PG&E states that decommissioning funding assurance for DCPP is provided by an external Nuclear Decommissioning Trust, as authorized under the Commission's regulations at 10 CFR 50.75(e)(1)(ii), and that PG&E will "transfer" to Diablo the "beneficial interest" in those portions of the CPUC Qualified and Nonqualified Nuclear Decommissioning Trusts (the "Trusts") "associated with" DCPP. Unfortunately, in its filing, PG&E has failed to inform the Commission that it does not have the legal authority to make this transfer. If PG&E cannot transfer its interest in the Trusts to Diablo, the proposed licensee has no decommissioning funding assurance, and the Commission cannot approve the requested license transfer, because decommissioning funding assurance is a *sine qua non* of Commission approval of any such license transfer.

The reasons why PG&E's beneficial interest in the Trusts cannot be transferred, and thus, the requested license transfer cannot be approved, are as follows: (1) the NRC does not have any direct jurisdiction over these Trusts and accordingly cannot authorize their assignment; (2) the proposed assignment cannot be accomplished without approval of the CPUC, which opposes the transfer; (3) it would be unjust and unreasonable to the California ratepayers who have funded these Trusts to authorize their assignment to a holding company that has no explicit obligation to those ratepayers and that could loot or exploit the Trusts' assets to its own advantage, and to the ratepayers' disadvantage; and (4) the Trusts provide funds for the eventual decommissioning of other PG&E assets -- specifically, Humboldt Bay Nuclear Unit No. 3 ("HB-3") -- which will be retained by PG&E, as well as for the eventual decommissioning of DCPP; thus, on purely practical grounds, the proposed assignment will create serious difficulties and potential inequities in terms of allocating the Trusts' assets as between the needs of DCPP and those other assets.

A. THE NRC LACKS JURISDICTION TO AUTHORIZE ANY ASSIGNMENT OF PG&E'S INTERESTS IN THE TRUSTS

Because the Trusts are not NRC-jurisdictional agreements, the NRC has no authority to approve the transfer proposed by PG&E, nor does PG&E claim that the NRC has any direct jurisdiction over these Trusts (although NRC regulations clearly do require that such trusts be in effect and do impose certain requirements relating to such trusts).

Rather, the Trusts were developed in a vertically integrated environment in which PG&E's nuclear facilities provided energy at retail to California consumers, under CPUC regulation. The parties to the Trust agreements are PG&E, the CPUC and the Trustee, Mellon Bank, N.A. The NRC is not a party to these agreements. The Trusts themselves provide that they were established pursuant to the regulatory authority of the CPUC and the NRC. *See also* Cal. Pub. Util. Code §§ 8321-8330 (the California Nuclear Facility Decommissioning Act of 1985). Any disposition of the Trusts' assets must be pursuant to CPUC order, and to the extent applicable, NRC order.

PG&E does acknowledge that authorization of the assignment of PG&E's beneficial interests in the portions of the Trusts associated with DCPP is "an essential element of the Transaction as the NRC requires Diablo Canyon LLC to have adequate assurance of decommissioning funding." *See* PG&E's Section 203 application to FERC, Docket EC02-31-000, at 72-73. PG&E is correct, of course, that the assignment of the DCPP portion (whatever that is) of PG&E's interests in the Trusts may be necessary under the Atomic Energy Act and NRC regulations to effectuate the transfer of DCPP to Diablo Canyon LLC, but the NRC lacks the authority to "authorize" the assignment of PG&E's interests in the DCPP portion of these trusts to Diablo Canyon LLC or to any other entity.

This is true regardless of any order the Bankruptcy Court may or may not issue. In a footnote in its FERC Section 203 application, PG&E indicates that it will ask the Bankruptcy Court to "compel" the CPUC to approve the transfer or to "deem" the approval to have been granted by the CPUC. *Id.*, at 74, n.57. However, the funds contained in the Trust are not subject to creditors' claims (except, of course, for claims relating to decommissioning activities for which a proper Disbursement Certificate is submitted to the Trustee)[8] and are therefore outside the purview of the Bankruptcy Court. The Bankruptcy Court therefore has no authority to "break" the contact as part of its approval of a reorganization plan. In any event, even if the Bankruptcy Court may or indeed does issue an order of the type contemplated by the PG&E footnote, such an order would in no way bestow jurisdiction over these Trusts on the NRC.

B. NO TRANSFER OF THE TRUSTS MAY BE ACCOMPLISHED WITHOUT THE APPROVAL OF THE CPUC

As noted above, the Master Trust Agreements that govern the management of the Trusts are contracts between the CPUC, PG&E and the Trustee, Mellon Bank, N.A. The Master Trust Agreements are, by their terms, irrevocable and not transferable. Section 2.07 of the Master Trust Agreement for the Qualified Decommissioning Trust (the larger of the two in terms of asset value) provides as follows:

> "The interest of the Company [PG&E] in the Master Trust is not transferable by the company, whether voluntarily or involuntarily, nor subject to the claims of the creditors of the Company, <u>provided, however</u>, that any creditor of the Company as to which a Disbursement Certificate has been properly completed and submitted to the Trustee may assert a claim directly against the Master Trust in an amount not to exceed the amount specified on such Disbursement Certificate. Nothing herein shall be construed to prohibit a transfer of the Company's interest in the Master Trust upon sale of all or part of the Company's ownership interest in any Plant or Plant's; <u>provided, however, that any such transfer shall be subject to the prior approval of the CPUC</u>." (Emphasis added.)

[8] *See* discussion *infra.*

Section 2.06 of the Master Trust Agreement for the Qualified Decommissioning Trust sets forth identical language.

The Master Trust Agreements thus explicitly deny PG&E the authority to transfer its interest in the Trusts either voluntarily or involuntarily. The only exception is in connection with a sale of PG&E's ownership interest in the plant. However, in such a case, the Master Trust Agreement specifically provides that "any such transfer shall be subject to the prior approval of the CPUC." In its Application in this matter, at page 11, PG&E states that it is seeking to obtain approval from FERC via its Section 203 filing for this transfer of interests in the Trusts to Diablo, without first seeking the approval of the CPUC. However, PG&E's effort to circumvent the required CPUC approval of a transfer of the Trusts by its appeal to FERC on its face violates the terms of its contractual agreement and is accordingly a void and unlawful act.

Ultimately, PG&E's request that FERC "authorize" its assignment of its DCPP-related interests in the Trusts to Diablo is an idle and futile exercise. The one leading authority cited in section V of PG&E's Section 203 application to FERC, which deals with this issue, *Niagara Mohawk Power Corp.*, 89 FERC ¶ 61,124 (1999) in no way supports PG&E's "authorization" request with respect to assignment of PG&E's DCPP-related interests in the Master Trust Agreements. Indeed, if anything, the *Niagara Mohawk* decision undermines the basis for PG&E's request.

In *Niagara Mohawk*, the co-tenants of the proposed transferee of a majority interest in the Nine Mile Point II power plant protested the proposed transfer based on concerns that the proposed transferor might have insufficient funds to meet its portion of eventual decommissioning expenses, and complained in this regard that the transferor failed to seek FERC approval for the transfer of nuclear decommissioning funds. In its decision, FERC found that there was no need to separately address whether such authorization was needed in that case, and noted that the financial ability of the proposed transferee to fund nuclear decommissioning was a matter to be addressed in an NRC proceeding. Moreover, in *Niagara Mohawk*, FERC explicitly recognized that the proposed transaction was "subject to review by the New York State Commission, and no state commission has argued that the proposed transaction would impair state regulation." *See* 89 FERC, at 61,347. Thus, PG&E's citation to this FERC decision attempts to turn the plain language of the decision inside out. PG&E is attempting to use a finding that holds that the specific authorization of the transfer of decommissioning funds is a matter, not requiring specific FERC approval, for other agencies (the NRC and, in the case of DCPP, the State of California) to decide into a pretext for de facto preemption of the state's clear contractual right to make that policy judgment.

C. ASSIGNMENT OF THE TRUSTS' ASSETS WOULD NOT BE IN THE PUBLIC INTEREST

PG&E contends, at page 74 of its Section 203 application to FERC, without any evidentiary support or analysis, that the assignment of its beneficial interests in the portions of the Trusts associated with DCPP "is consistent with the public interest and is in the public interest." In fact, the opposite is closer to the truth. For instance, the U.S. General Accounting office has just released a report (GAO-02-048, January 2002) finding that the NRC has been approving licensing transfers and related decommissioning efforts even though new owners and operators are unable to assure regulators that the money for decommissioning will be there when reactors are ready for burial.

The specific question of whether the transfer of a nuclear decommissioning fund would be in the public interest, was examined in detail by the CPUC several years ago in a case, A.97-12-039, involving the application of San Diego Gas and Electric Company (SDG&E) for authority to sell its share of the San Onofre Nuclear Generating Station ("SONGS"). There, even SDG&E's partner in SONGS, Southern California Edison Co. ("Edison") expressed concern regarding the proposed transfer, questioning how ratepayers can be assured of protection if a decommissioning trust fund is dissipated by a new, non-utility owner after the transfer. (*See* RT of October 21, 1999 hearing in CPUC Docket A-97-12-039, at 22.) PG&E does not even suggest an answer to that question, either in its Application in this matter or in its voluminous Section 203 application to FERC, which also addresses the proposed transfer of PG&E's beneficial interest in the Trusts to Diablo. However, this question is as compelling today in the context of the transfer that PG&E is requesting the Commission to authorize herein as it was 2½ years ago in the SONGS proceeding.[9]

It should also be noted that California's decommissioning law is stricter than required by the NRC. Pursuant to the California Nuclear Facility Decommissioning Act of 1985 (Pub. Util. Code §§ 8321 through 8330), California's nuclear power plants generally have considerably more money in their decommissioning trust funds than do

[9] It should be noted that on November 5, 1999, SDG&E withdrew its request to divest its interest in SONGS. *See, In the Matter of the Application of San Diego Gas & Electric Company (U-902-E) for Authority to Sell Electrical Generation Facilities et al.*, D.00-10-054, 2000 Cal. PUC LEXIS 760 (2000).

the plants in most other states. This is because most other states typically only require compliance with NRC rules. Under this California law, not only must more money be put into such funds (the maximum contribution allowed pursuant to section 468A of the U.S. Internal Revenue Code, and applicable regulations adopted pursuant thereto), but also California has the oversight authority to make sure that the decommissioning work gets done in a timely fashion. Under CPUC oversight, PG&E has been a good steward of the Trusts, to date.

However, there is absolutely no guarantee that a Diablo Canyon LLC or some other entity that is not regulated by the CPUC would maintain that stewardship. And yet, the transfer of PG&E's "beneficial interest" in the portions of the Trusts associated with DCPP will effectively put much of the Trusts assets in the hands of such a less reliable and less trustworthy entity, over which, in PG&E's view, neither FERC nor the CPUC would have regulatory authority. Such an unregulated entity would have a strong financial incentive to delay performing the decommissioning as long as possible, in order to make as much money for itself, using ratepayer provided funds. It would not be in the public interest, and it would be unjust and unreasonable to PG&E's ratepayers, who have footed the bill for the eventual decommissioning of DCPP, to allow such a situation to arise.

D. THE IMPRACTICALITY OF ASSIGNING THE TRUSTS' ASSETS

Based on information contained in the most recent annual report (for calendar year 2000) from PG&E's Nuclear Facilities Decommissioning Master Trust Committee ("NFDMTC"), there is currently a total of some $1.462 billion of assets in the Trusts. At page 11 of the Application, PG&E states that approximately $1.101 billion of this sum is the "liquidation value" of the DCPP portion of the Trusts. It is important to note, however, that the Trusts are intended to cover decommissioning costs for the shut down of both HB-3 and the DCPP units. By their terms, the Trust documents do not allocate any given amount of the funds controlled by the Trusts to either plant.

PG&E attempts to sweep this serious problem under the rug by blithely asserting in a footnote (at page 11 n.10 of the Application) that all of the funds in the Trusts associated with HB-3 will be "segregated" from the DCPP components of the Trusts as part of the larger transaction that PG&E is requesting FERC to approve. Unfortunately, nothing in the Application indicates how this "segregation" will take place. Nor does PG&E explain how such a "segregation" is consistent with, or permitted by, the Trust documents.

Even if it were both lawful and achievable to so segregate the Trust funds, given the unpredictable nature of decommissioning activities, it would be unreasonable and impractical to attempt to allocate the Trusts into separate HB-3 and DCPP components without a detailed study of the likely scope of the decommissioning effort required for each facility. Such a study would be a lengthy, complicated and expensive endeavor. However, without a proper allocation of Trust assets to HB-3 and DCPP based on a prudent and thorough analysis of the likely costs of decommissioning for both facilities, there is a significant likelihood that one or the other of the facilities would have too few funds to properly complete decommissioning, thereby resulting, especially in the case of HB-3, in an unnecessary, unjust and unreasonable adverse impact on PG&E's ratepayers, and potential health, safety, and welfare concerns for California citizens. Thus, assuming, *arguendo*, that some entity other than the CPUC had the authority to divide the corpus of the Trusts and to assign some share of the Trusts' assets that would be allocated to DCPP to Diablo, and notwithstanding PG&E's unsupported statement of the liquidation value of the DCPP component of the Trusts, it would be improper, imprudent and impractical to do so absent the results of a detailed study which has not yet even been commenced.

III. The Proposed Transferee is Not Financially Qualified to be the NRC's Licensee for the DCPP

The license for DCPP should not be transferred to Gen, because, as the discussion below amply sets forth, Gen's finances are highly questionable. It is accordingly uncertain that Gen will have the resources to carry out the critical plant maintenance and public safety-related functions that will enable the DCPP to continue to meet the Commission's rigorous regulatory requirements. It would be imprudent in the extreme to license untested, financially unstable entities to own and operate a commercial nuclear reactor, an installation that must meet critically high standards of operations and maintenance.

As part of its Reorganization Plan, PG&E would divest most of its generation assets, including DCPP, to Gen, and would then enter into a Purchase & Sale Agreement ("PSA") to buy back the power output of DCPP for the next twelve years. This proposal is seriously flawed, because the rates proposed in the PSA are unjust and unreasonable, and FERC cannot legally or properly approve them. Assuming that FERC properly determines that Gen should only be allowed to collect cost-based rates for DCPP, there will simply not be enough money coming in to both operate the plant properly, and to service the debt to be incurred by Gen under the Plan. Under such circumstances, Gen will be in no position to satisfy the requirement of the Commission's regulation, at 10 CFR 50.33(f)(2), that a non-utility applicant (such as Gen would be) must have reasonable assurance of obtaining the funds necessary to cover the plant's estimated operating costs.

The CPUC is currently attempting to thwart this scheme in a motion contesting PG&E's Federal Power Act Section 203, 204 and 205 filings with FERC, as well as before the Bankruptcy Court. Copies of the CPUC's filings in these three FERC Dockets, EC02-31-000 (the "203 application")[10], ES02-17-000 ("the 204 application")[11] and ER02-456-000 (the "Gen 205 application")[12] are attached hereto as Exhibits D, E and F, respectively. The CPUC incorporates the substance of those filings by reference, as if fully set forth herein. Should the CPUC prevail on any of the issues it has raised in those FERC proceedings (or on the legal and policy issues the CPUC has raised in the Bankruptcy Court, which are discussed above), the house of cards on which PG&E's applications, both to this Commission and to FERC, are based, will quickly collapse. In

[10] In its 203 application, PG&E requests, among other things, that FERC authorize it to transfer to Diablo Canyon LLC, one of the subsidiaries of Gen, its beneficial interest in the Nuclear Decommissioning Trusts associated with DCPP.

[11] Gen plans to finance acquisition of DCPP through the issuance of bonds, which it asks FERC to authorize in the 204 application. However, under §204 of the Federal Power Act, FERC clearly lacks jurisdiction to do so. FERC must accordingly deny PG&E's 204 application on its merits.

[12] In the Gen 205 application, PG&E seeks, among other things, approval by FERC of a power sales agreement whereby Gen would enter into a 12-year contract to sell the power output of DCPP to PG&E for a specified price.

such event, Gen will not be a financially viable entity, and will thus be rendered, beyond any doubt, unqualified to hold the license for DCPP. For this reason alone, the Commission should dismiss the application under review in this proceeding, or, at least, hold the requested license transfer in abeyance until the disposition of PG&E's restructuring plan is settled by the Bankruptcy Court. The Declaration of David R. Effross, which is attached hereto as Exhibit G, provides evidentiary support for the following analysis showing why Gen will not be a financially viable entity.

A. GEN WILL NOT BE A FINANCIALLY VIABLE ENTITY

PG&E's Plan proposes to transfer PG&E's electric generation, electric transmission, and natural gas transportation facilities to PG&E's Parent, PG&E Corporation, leaving a Reorganized PG&E to emerge from bankruptcy as an under funded distribution-only utility possessing only assets and liabilities not desired by the corporate parent. Included is a proposal to transfer all of PG&E's hydroelectric and its operating nuclear generation facilities (*i.e.*, DCPP) to Gen, and then to transfer Gen to the corporate Parent by means of an unlawful stock dividend in violation of § 305 of the Federal Power Act (*see* Exhibit D).

Should the various transactions proposed in PG&E's Plan be approved, PG&E proposes that Gen enter into a proposed Purchase & Sale Agreement ("PSA") with Reorganized PG&E. Under the PSA, Gen proposes to sell all of the output of the (former) PG&E generation facilities to Reorganized PG&E for an eleven year period at an unjust and unreasonable price, approaching double the rates PG&E would receive for the output of the facilities in the absence of the proposed transactions, and justified only by the need to service the unnecessary debt which Gen proposes to incur upon receipt of the facilities (the PSA includes a twelfth year for approximately half of the facilities' output). Under this Plan, as noted in part I above, only Reorganized PG&E would be subject to CPUC regulation.

The terms of the PSA are spelled out in PG&E's Gen 205 application. The CPUC's preliminary review of the Gen 205 application (which is summarized in Exhibit F) discloses strong indications that the pricing, terms and conditions of the PSA are not just and reasonable, and thus, may not be approved by FERC.

PG&E has wholly failed to meet FERC's standards applicable to power sales agreements between affiliates. Moreover, under the circumstances here, the applicable standards must be applied with extraordinary scrutiny. The PSA was not reached at arm's-length by entities with competing interests, but rather was developed by the same counsel working simultaneously for all the (affiliated!) parties, one of which is essentially non-existent. PG&E concedes that the PSA was developed, on behalf of both the "buyer" and "seller" by a single "Team [which] developed the price, terms and conditions of the PSA."[13]

B. THE RATES IN THE PROPOSED PSA ARE UNJUST AND UNREASONABLE TO REORGANIZED PG&E AND ITS RETAIL CUSTOMERS WHO WILL FOOT THE BILL

The heart of the Gen 205 application is PG&E's contention that the rates in the proposed PSA are just and reasonable to Reorganized PG&E on the basis of a

[13] See Exhibit 1 (Kuga Testimony) to PG&E's Gen 205 application, at 11.

"benchmark" analysis conducted by PG&E's witness Meehan. However, as set forth in detail below, PG&E's "benchmark" analysis misses the mark. First, the rates in the proposed PSA must properly be evaluated not against other long-term power transactions, but rather against the rates which PG&E would receive in the absence of the proposed Spin-Off and related transactions. That is, the proposed PSA rates must be compared against the CPUC's rates for Utility Retained Generation. Second, even if it is appropriate to measure the proposed PSA against "comparable" wholesale transactions, PG&E's benchmark analysis fails to establish that the proposed PSA rates are just and reasonable. Third, PG&E fails to provide a cogent analysis of its market power. Consequently, PG&E fails to establish that the price and non-price terms and conditions of the PSA are just and reasonable, and that the PSA is not fatally tainted by self-dealing.

1. The Proposed PSA Rates Must be Evaluated in Comparison with Otherwise Applicable Rates

Under PG&E's proposal, Gen will sell the output of the electric generation facilities currently owned and operated by PG&E to Reorganized PG&E, which would in turn resell the facilities' output to its retail customers. In the absence of the transactions proposed in PG&E's Plan, PG&E would retain the electric generation assets which it proposes to transfer to Gen and to the subsidiaries of Gen, including, in this case, to Diablo Canyon LLC, and would continue selling the output of the generation facilities directly to its retail customers.[14] Under either scenario PG&E's retail customers will receive the same energy and Ancillary Services from the same facilities. Thus, the

[14] As discussed in greater detail in part I above, the CPUC has formulated an Alternative Plan under which PG&E would be able to emerge from bankruptcy without disposing of its electric generation assets.

appropriate comparator against which to measure the PSA is the utility-retained generation ("URG") component of PG&E's retail rates.

Under current California law and CPUC policy, such rates are determined on a traditional cost-of-service basis. *See, e.g., Application of San Diego Gas & Electric Company et al.*, D.01-12-015, 2001 Cal. PUC LEXIS 1072, *7 ("We intend to apply cost-based ratemaking to all of SDG&E's retained generation assets . . . which we believe is consistent with ABX1 6"); *Application of Southern California Edison Company et al.*, D.01-01-061, 2001 Cal. PUC LEXIS 30 ("PG&E, SDG&E and Edison shall establish a cost-based rate for URG"). The CPUC has expressly rejected PG&E's request to set its URG revenue requirement based on market valuation rather than cost-of-service. *Application of Southern California Edison Company et al.*, D.01-10-067, 2001 Cal. PUC LEXIS 959 ("We determine that market valuation does not apply to setting a prospective revenue requirement for PG&E's URG assets").

PG&E's witness Meehan states that the levelized price over the twelve-year period of the PSA is approximately $52.29/MWh.[15] Elsewhere, PG&E asserts that the average price under the contract over the life of the contract is approximately 5.1 cents/kWh ($51/MWh).[16] That the contract costs are unjust and unreasonable as to Reorganized PG&E (and to its retail ratepayers) is confirmed by PG&E's own numbers. In its Plan, PG&E projects revenues under the contract of approximately $1.5 billion annually. For calendar year 2003, PG&E projects revenues under the contract of $1,471,500,000. (*See*

[15] The testimony of Mr. Meehan is set forth in Exhibit 2 to PG&E's Gen 205 application.

[16] See PG&E's Gen 205 application, at 3.

a page from PG&E's Plan, which is attached to Exhibit F hereto as "Exhibit A.") Based solely on the numbers presented by PG&E in its Plan, PG&E's revenue requirement based on traditional cost-of-service principles would be approximately $790.4 million for 2003—about half of PG&E's projected revenues. This translates to an illustrative rate of approximately 2.5 cents/kwh.[17]

This calculation proceeds as follows: PG&E's Plan projects total operating expenses for Gen in 2003, including depreciation, of $759.7 million. From this figure is subtracted "other income" of $88.9 million, leaving net operating expenses of $670.8 million. To this is added a rate of return and taxes of $119.6 million, calculated utilizing PG&E's projected 2003 net plant shown in the Plan of Reorganization for the nuclear and hydro assets of $913.8 million and PG&E's rate of return grossed up for income tax authorized by the CPUC of 13.09%.[18] This results in an illustrative cost-of-service revenue requirement for Gen, using PG&E's own figures, of $790.4 million for 2003.

The illustrative cost-of-service revenue requirement of $790.4 million is 53.7% of the proposed revenues PG&E would receive under the PSA in 2003 of $1,471.5 million. PG&E asserts that rates under the PSA in 2003 would be approximately 4.6 cents/kWh. Since, as PG&E asserts, revenues of $1,471.5 million equates to 4.6 cents/kWh on average, the cost-of-service revenue requirement is approximately 2.5 cents/kWh on

[17] This pleading does not purport to determine the rate which the CPUC would actually set for PG&E's URG for any particular customer or class of customers, but simply utilizes figures provided by PG&E to provide, for illustrative purposes, a rough calculation of a cost-of-service rate based on such figures.

[18] PG&E's Plan shows higher figures for return, interest expense, and taxes, totaling $800.8 million, because the figures reflect and are being used to support the borrowing of over $2 billion to help pay off creditor claims. The $119.6 million in the calculation above includes interest expense on the net plant of $913.6 million, as it is based on a 13.09% weighted average rate of return that includes interest and taxes. *See* PG&E work papers submitted in CPUC Docket No. A.00-11-038, Scenario 1.

average (.537 x 4.6 cents/kWh) for 2003.[19]

While a rate of 2.5 cents/kWh is low compared to recent prices for gas-fired generation, the rate reflects the resource mix utilized for the PSA and PG&E's actual costs—not including the cost of unnecessarily borrowing over $2 billion. PG&E's hydroelectric resources are highly depreciated. PG&E's nuclear and hydro pumped storage resources, including DCPP, have been subject to accelerated depreciation during the transition period established under California's deregulation law. Ratepayers have paid several billion dollars of accelerated depreciation through California's Competitive Transition Charge, and would be losing a good portion of what they paid for under PG&E's Plan of Reorganization. *See also* the proposed decision addressing PG&E's revenue requirement for utility-retained generation ("the URG PD") recently issued by a CPUC Administrative Law Judge.[20]

While these figures may be subject to some refinement, this illustration demonstrates that the PSA is grossly overpriced. If the PSA were approved as proposed, PG&E's ratepayers would make some $700 million in excess payments to Gen over and above the otherwise applicable rate for the same energy from the same facilities in 2003. Over the life of the PSA, the overpayments approximate $8 billion.

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[19] A recent report issued by the consumer group TURN estimates the "Expected Price Under Regulation" at approximately 2.5 cents/kWh in 2003, and 2.9 cents over the term of the PSA. *See* "Highway Robbery: Unmasking the PG&E Bankruptcy Plan's Financial Impact on California Consumers," available at http://www.turn.org/turnarticles/PG&E_report.pdf.

[20] California law generally requires the CPUC's proposed decisions to be released for comment prior to a Commission vote. See Cal. Pub. Util. Code § 311(d), (g). The URG PD is available from the CPUC's web site, at http://www.cpuc.ca.gov/published/comment_decision/12655.htm. An alternate proposed decision of CPUC Commissioner Lynch is available at http://www.cpuc.ca.gov/published/Agenda_decision/12659.htm.

2. PG&E's Benchmark Analysis is Invalid

Assuming, *arguendo*, that the benchmark analysis utilized by FERC in connection with previous affiliate transactions is applicable, PG&E's benchmark analysis, supported by the testimony of witness Meehan, is invalid for a number of reasons, discussed below.

FERC has articulated standards pursuant to which it will accept power sales contracts between affiliates in a series of three orders over the past ten years. *Boston Edison Co. Re: Edgar Electric Energy Co.*, 55 FERC ¶ 61,382 (1991) ("*Edgar*"); *Ocean State Power II*, 59 FERC $61,360 (1992), reh'g denied, 69 FERC ¶ 61,146 (1994) ("*Ocean State*"); *Ameren Energy Mktg. Co.*, 96 FERC ¶ 61,306 (2001) ("*Ameren*"). In *Edgar*, FERC stated that such arrangements will be permitted if two conditions are satisfied. First, FERC requires a showing that there exists no potential abuse of self-dealing or reciprocal dealing. Second, if there has been a showing of no potential abuse of self-dealing or reciprocal dealing, FERC has found that market-based rates may be acceptable if the seller can also demonstrate that it lacks market power (or has adequately mitigated its market power), under familiar principles. *Edgar*, 55 FERC at 62,167.

As PG&E recognizes, the potential for self-dealing is present here, where the seller under the proposed PSA is essentially non-existent, and the terms and conditions of the PSA were developed by a single entity acting on behalf of both the putative seller and buyer. The risk of self-dealing is at its height in this transaction, in which the buyer under the proposed PSA would, if PG&E's Plan is confirmed, be stripped of all of its most valuable assets and the affiliate relationship then terminated.

FERC has articulated three means by which lack of self-dealing or reciprocal dealing may be shown, to ensure that an affiliated "buyer has chosen the lowest cost supplier from among the options presented, taking into account both price and non-price terms (i.e., that it has not preferred its affiliate without justification"). *Edgar*, 55 FERC at 62,168. PG&E has chosen to present "benchmark evidence" of market value, i.e. evidence of other relevant power sales agreements between non-affiliates, which it claims demonstrates that the PSA is not unreasonable.[21] Under the *Edgar* line of cases, the benchmark sales must be: (1) transactions in the relevant market; and (2) should be contemporaneous with; and (3) involve service that is comparable to, the instant transactions. In addition, FERC requires that the benchmark analysis examine non-price as well as price terms, and assumptions used in comparing the various projects should be explained with respect to both price and non-price terms. Finally, the applicant must demonstrate that the benchmark evidence was not distorted by the exercise of market power by the seller or its affiliates. *Ocean State*, 59 FERC at 62,333. FERC has observed that it must "take into account the evolving nature of our analyses of market-based affiliate transactions," including changes to the national generation market. *Ocean State*, 59 FERC at 62,332.

PG&E contends that the relevant market is "the market for firm, long-term baseload and peaking capacity and energy for a duration of approximately 10-15 years with a start date expected near January 2003," and that the relevant region must be limited to suppliers which can deliver energy to PG&E.[22] PG&E contends that the

[21] See PG&E's Gen 205 application, at 14 ff.

[22] See PG&E's Gen 205 application, at 17.

relevant "contemporaneous" period is May 2000 through November 2001.[23] By so attempting to confine the analysis, PG&E contends that the appropriate benchmark sales are nine long-term contracts entered into by the California Department of Water Resources ("DWR") during 2001.

<u>PG&E's Reliance on DWR Contracts</u>

In confining its benchmark comparison to the DWR contracts, PG&E has sought to define as the relevant period precisely the same period in which the California wholesale electricity markets exhibited extreme dysfunction. PG&E has previously characterized this as a period of "massive market failure and upheaval in the regulatory regime that has led to billions of dollars in overcharges since May 2000."[24] Similarly, PG&E has attempted to confine its benchmark comparison to DWR contracts, the negotiation of which PG&E has previously contended were subject to the exercise of market power, and as to which PG&E has contended FERC ought to order refunds.[25] As PG&E stated in its Request for Rehearing of FERC's July 25, 2001 order (*San Diego Gas & Electric Company, et al.*, 97 FERC 61,275 (2001), filed in Docket No. EL00-95 on August 24, 2001, at 12:

> "the DWR bilaterals . . . have drawn the most attention. These transactions are not bilateral purchases in the conventional sense with a willing buyer and a willing seller. Rather, they reflect the state stepping into the shoes of insolvent utilities as the default buyer of power in order to

[23] *See* PG&E's Gen 205 application, at 18.

[24] *See* PG&E's Request for Rehearing of FERC's July 25, 2001 order *(San Diego Gas & Electric Company, et al.*, 97 FERC 61,275 (2001), filed in FERC Docket No. EL00-95 on August 24, 2001, at 19.

[25] FERC has not found any specific DWR contracts to be "just and reasonable." *See, e.g., GWF Energy*, 97 FERC 61,297 (2001), slip op. at pp. 3-4.

> backstop the ISO's efforts at maintaining reliability in a dysfunctional market."

PG&E's reliance on the DWR contracts for its benchmark analysis is fatal. The DWR contracts were negotiated and executed during a period of extreme exercise of market power, as FERC has acknowledged on repeated occasions. FERC has expressly recognized that the exercise of market power in the spot markets extended to the forward markets during the time period to which PG&E seeks to confine the analysis.[26] Thus, the DWR contracts cannot be relied on to be a benchmark of market value in a competitive market, and cannot be relied on to demonstrate that the PSA reflects a competitive market value.[27]

The Relevant Market

In *Ocean State*, FERC indicated that a benchmark analysis should consider as the geographic market suppliers that can supply the relevant product to the buyer. *Ocean State*, 59 FERC at 62,333. However, FERC also expressly stated that its analysis and holding in *Ocean State* were confined to the facts of that proceeding. *Ocean State*, 59 FERC at 62,338 n. 117. With respect to the PG&E reorganization, it is inappropriate to consider only a geographic market centered on PG&E's service territory. First, as discussed above, an analytic limitation to contracts in PG&E's California service territory focuses the analysis on an environment of acknowledged market power.

[26] *San Diego Gas & Electric Company, et al.*, 93 FERC ¶61,121 (2000) at 61,358 ("higher spot prices in turn affect the prices in forward markets"); *San Diego Gas & Electric Company, et al.*, 95 FERC ¶ 61,418 (2001), at 62,556 (expanded spot market mitigation plan "will, over time, impact bilateral and forward markets as well"); *see also AEP Power Marketing, Inc.*, 97 FERC ¶ 61,219 (2001).

[27] Only a competitive market value is relevant to an analysis under section 205 of the Federal Power Act to determine whether a proposed rate is just and reasonable, as "t]he prevailing price in the marketplace cannot be the final measure of 'just and reasonable' rates mandated by the Act." *FPC v. Texaco*, 417 U.S. 380, 397 (1974).

Second, a broader geographic market is appropriate to consider in this case due to the nature of the PSA. The PSA is a long-term agreement with a delayed implementation date. Developed in 2001, it is proposed that the PSA run from January 2003 through 2014. The market for such contracts is decidedly national, not regional. That is, a seller need not be physically located in California in 2001 in order to provide power under a 12-year contract commencing in 2003. Because of the long duration and delayed implementation date, a seller would have sufficient time to build new facilities to satisfy all but the earliest segments of the twelve year period.

That the long-term market for electric generation is essentially national rather than regional is confirmed by an examination of regional pricing for forward electricity contracts. During the height of the recent California energy crisis, western forward prices were substantially higher than forward contracts at other national trading hubs -- as much as an order of magnitude higher. Since FERC's summer 2001 orders restored a measure of stability to western markets, however, forward contract prices at various regional hubs have tended to converge. For instance, as of December 12, 2001 (when the notice was issued in this proceeding) the simple average of reported futures prices for calendar year 2002 were $30.66 for the California-Oregon border ("COB"), $34.25 for PJM, and $30.80 for CINergy.[28] Longer-term prices should show similar convergence. As the relevant market for products similar to the PSA is a national rather than regional market, and PG&E analyzes only a corrupted regional market, PG&E's benchmark analysis fails to satisfy the "relevant market" prong of the benchmark analysis.

[28] See www.enerfax.com. By late January 2002, prices in all three markets had declined.

Contemporaneousness

PG&E's benchmark analysis similarly fails to satisfy the "contemporaneous" prong articulated in the relevant cases. PG&E examined only contracts "entered into between May 2000 and the date of this Application."[29] Meehan's benchmark analysis focuses on nine contracts entered into between February and August 2001 as his "comparison group."[30] As discussed above, this is precisely the period in which all energy transactions in the California markets were tainted with market power. It is patently unreasonable to consider only such contracts. Moreover, this period is not contemporaneous with the period in which the PSA was developed. PG&E filed its Plan with the Bankruptcy Court on September 20, 2001; however, the key event in this scenario is the order issued by FERC on June 19, 2001, which quickly restored a semblance of stability to the California markets. All of the contracts in witness Meehan's "comparison group" were either executed or had an executed letter of intent no later than June 22, 2001.[31] That is to say, the negotiation of all of the comparison group contracts took place in the market power period. By the fall of 2001 when the PSA was developed, forward contract prices in California had already begun to converge with forward prices in regional markets across the country, at prices well below the prices in the PSA. PG&E has thus failed to examine any contemporaneous contracts in its benchmark analysis.

In *Ocean State*, FERC approved a benchmark analysis, which considered as the

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[29] *See* PG&E's Gen 205 application, at 18.

[30] *See* PG&E's Gen 205 application, at 20-21.

[31] *See, California State Auditor*, "California Energy Markets: Pressures Have Eased, But Cost Risks Remain," 193-195, Table 10. The report is available at http://www.bsa.ca.gov/bsa/pdfs/2001009.pdf

relevant period late 1987 into 1989, "reflecting the period during which the purchasers made their decisions to contract with Ocean State II." *Ocean State*, 59 FERC at 62,334. PG&E provides no similar justification for the period it has chosen. Certainly, PG&E makes no claim that that the roughly eighteen month period it has selected for examination represents the only, or even the most relevant, time period in which buyers seeking energy for the 2003-2014 period would have, or did, engage in negotiations.

The CPUC has no principled objection to a "contemporaneous" period of roughly eighteen months. But PG&E has disingenuously selected the precise 18 months in which the California market was at its most dysfunctional. Were there no long-term power contracts entered into in the western United States in the first quarter of 2000? In the last quarter of 1999? Or, for that matter, in the truly contemporaneous period – the third and fourth quarters of 2001? The "contemporaneous" period selected by PG&E is invalid on its face, particularly when coupled with the limited geographical market also selected by PG&E. Any valid benchmark analysis must, if not be limited to, certainly <u>include</u> an examination of contracts executed during a period of relative market stability. Such a period could include, for instance portions of 1999 and 2000, and the latter third of 2001. Evidence as to whether and to what extent buyers sought long-term contracts for period comparable to the PSA during these periods can be presented at hearing.

<u>Comparability</u>

As PG&E observes, FERC has held that benchmark evidence must encompass "similar services when compared to the instant transaction." *Edgar*, 55 FERC at 62,129; *Ocean State*, at 62,333. PG&E's benchmark analysis fails this requirement as well. In the instant case, the PSA provides for capacity and energy from approximately 7,100 MW of hydroelectric and nuclear power plants. The size of the PSA alone disqualifies each of the purported "comparison group" contracts from consideration as comparable. PG&E witness Meehan admits that he must treat each of the comparison group contracts as "infinitely scalable" in order to make a comparison.[32] In *Ocean State*, the applicant provided comparison evidence relating to 33 projects. FERC confined its analysis to the ten projects which were "comparable to Ocean State II with respect to size and technology." *Ocean State*, 59 FERC at 62,334. Similarly, in *Edgar*, FERC rejected a benchmark showing in part due to the applicant's failure to evaluate the proposed rates against truly comparable projects. *Edgar*, 55 FERC at 62,169 ("Boston Edison's comparison of projects [against a 306 MW combined-cycle generating unit] includes projects as small as 0.7 MW and powered by wind, wood, waste, peat and hydropower"). Here, of course, the facilities proposed to support the PSA are exclusively hydroelectric and nuclear generating plants. The "comparison group" contracts, to the extent that they have any specific source of generation attached to them, are exclusively natural gas-fired units. The PSA is for some 7,100 MW. Only one of the comparison group contracts is within the same order of magnitude. The comparison group contracts are comparable in neither size nor technology to the PSA.[33]

[32] See PG&E's Gen 205 application, at 27, and Exhibit 2 to the Gen 205 application, at 25.

[33] PG&E declines to provide benchmark evidence regarding "buy-back" agreements executed in recent years in connection with sales of nuclear facilities in New York, or with fairly large hydroelectric portfolios elsewhere in the U.S.

Price

The foregoing establishes that PG&E's benchmark analysis fails to establish the absence of self-dealing in the development of the PSA. As such, the PSA may not be accepted. *Edgar*, 55 FERC at 62,170. Moreover, the proposed rates in the PSA are simply too high to be considered just and reasonable. For instance, the capacity charges in the first year of the PSA amount to $170.75/kW-year.[34] Specifically, the capacity charges are $20.50/kW-mo for the peak months of July and August, $15.25/kW-mo for June, September, and October, and $12/kW-mo for November through May. The capacity payment is paid on a portfolio of 7,100 MW of capacity.[35] Thus the capacity payments alone under the PSA, in the first year, amount to over $1.2 billion, and escalate to nearly $1.5 billion in year eleven.

FERC recently addressed another power sales agreement between affiliates in *Ameren*. The contract is for a minimum of 350 MW of capacity and energy per hour from June 2001 through May 2002. In the affiliate contract at issue in *Ameren*, the maximum capacity charge is $4/kW-mo. The minimum capacity charge in PG&E's PSA exceeds that by 300 per cent.

At this juncture, one point should be clear: the value of PG&E's Plan to Gen exceeds the revenues that Gen would receive under the PSA. Under the Plan, Gen will receive not only $52.29/MWh for twelve years, but in addition, Gen will receive virtually all of PG&E's electric generation assets for a fraction of their value. Gen will effectively

[34] See Exhibit 1 (Kuga testimony) to PG&E's Gen 205 application, at 6.

[35] See Exhibit 1 (Kuga testimony) to PG&E's Gen 205 application, at 5.

pay reorganized PG&E $2.4 billion for PG&E's hydroelectric assets and DCPP.[36] Gen thus proposes to acquire the hydro and nuclear assets for less than PG&E has previously proposed as the market value for the hydro facilities alone.[37]

The foregoing facts demonstrate that the PSA cannot appropriately be considered in isolation. However, any substantive evaluation of the PSA must consider related issues including the value to Gen of obtaining the PG&E generating facilities for a fraction of their PG&E-proposed market value.

3. PG&E's Market Power Analysis is Woefully Insufficient

The *Edgar* line of cases requires an applicant in an affiliate sales case to make two separate market power showings. First, PG&E must demonstrate that "the benchmark evidence was not distorted by exercise of market power by the seller or its affiliates." *Ocean State*, 59 FERC at 62,333. In this regard, FERC is concerned that, "If the seller or any of its affiliates has exercised market power and thus kept prices high in the relevant market, the benchmark evidence would be skewed in favor of the seller and thereby allow the affiliated buyers to give an undue preference to the sellers." *Ocean State*, 59 FERC at 62,337. In the Gen 205 proceeding, FERC must address not only whether PG&E has exercised market power and thus skewed the benchmark evidence, but rather whether any party exercised market power in connection with the benchmark evidence. That is, a

[36] See PG&E's Gen 205 application, at 2. Upon receiving the generating facilities from PG&E, "Gen will then transfer cash and notes to PG&E amounting to $2.4 billion".

[37] See Exhibit D, at 17-33. The market value of the hydro facilities was set at $2.8 billion in a settlement agreement proposed by PG&E, TURN, and other parties in CPUC Docket No. A.99-09-053, but which was not approved by the CPUC. PG&E subsequently proposed a market value of $4.1 billion for the hydroelectric facilities alone in CPUC Docket No. A.00-11-056.

proper market analysis in this proceeding must consider whether the benchmark evidence was skewed by the exercise of market power. As discussed above, there is no doubt that it was. Accordingly, the benchmark evidence is invalid, and cannot be used to support the PSA.

Second, if there has been a showing of no potential abuse of self-dealing or reciprocal dealing, FERC has found that market-based rates may be acceptable if the seller can also demonstrate that it lacks market power (or has adequately mitigated its market power), under familiar principles. *Edgar*, 55 FERC at 62,167. As PG&E requests acceptance of the PSA as market-based rate,[38] PG&E must satisfy this standard (although, as is noted above, PG&E has not demonstrated the lack of abuse of self-dealing).

PG&E currently possesses in excess of, and Gen proposes to acquire, 7,100 MW of generation. PG&E's contention that a supplier of such magnitude in frequently constrained Northern California does not have market power fails the straight face test. Indeed, PG&E has been among the loudest voices arguing that suppliers with much smaller portfolios have both possessed and abused market power.[39]

Whether measured by the now-disregarded hub-and-spoke methodology or the

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[38] *See* PG&E's Gen 205 application, at 14 n. 13.

[39] *See, e.g.,* "Late Motion to Intervene and Protest of Pacific Gas & Electric Company and Southern California Edison Co." in FERC Docket No. ER99-1722-004, filed April 3, 2001, at 7 ("because the premises on which Williams based its market power analysis are no longer valid, and because of the clear evidence that Williams can exercise market power in the WSCC, the Commission's review should lead to a suspension of Williams' market-based rate authority") (emphasis added) and "Testimony of James Wilson for PG&E" in FERC Docket No. EL00-95-000 at 10-16 and Figures 1, 2 and 5 (unrebutted testimony demonstrating that conditions in the California marketplace have permitted the exercise of market power, bidding without adequate competition by pivotal suppliers, and existence of Cournot pricing conditions during potentially 4000 hours in 2001).

Supply Margin Assessment ("SMA") screen established in *AEP Power Marketing, Inc.*, 97 FERC ¶ 61,219 (2001) ("AEP"), PG&E indisputably possesses market power. At best, PG&E's showing -- i.e. that it is a net purchaser rather than a net seller of electricity, and that its generation resources are currently required both by state and federal regulation to be devoted to native load -- demonstrates that under current circumstances it has little incentive to exercise the market power it possesses.[40] All this, of course, will change should PG&E's Plan be implemented. Gen would become a stand-alone merchant seller with the largest single generation portfolio in California, and one of the largest generation portfolios in the country. Moreover, although the Gen 205 application is a new market-based rate application submitted after the announcement of the SMA screen in AEP, PG&E has failed to perform an SMA analysis. Nor has PG&E submitted a hub-and-spoke analysis.

In sum, there can be no question that a supplier with a generation portfolio of the magnitude at issue here in Northern California possesses market power.

4. In Light of the Inadequacies of PG&E's Showing, and the Unique Aspects of the Proposed PSA, Only Cost-based Rates May be Accepted as Just and Reasonable

PG&E's Gen application to the FERC wholly fails to satisfy the applicable standards necessary to support the rates in the proposed PSA, or any market-based rates. Due to the unique nature of both the proposed transaction and the magnitude of the generation portfolio supporting it, it is unlikely that PG&E could make a showing that satisfies the benchmark standards and effectively rebuts the presumption of self-dealing

[40] See PG&E's Gen 205 application, at 34-35.

which must be drawn from the facts at issue here.

PG&E has asserted that other suppliers in California should be subject to cost-based ratemaking. For instance, in PG&E's Request for Rehearing of FERC's July 25, 2001 order (filed August 24, 2001), PG&E asserted that "cost of service rates [are] the only legally appropriate baseline given the fact that the California wholesale markets have been found to be unable to yield just and reasonable rates in all hours." *Id.*, at 2. In that Rehearing Request, PG&E similarly states that, "As PG&E has previously stated in these dockets, absent a properly functioning market sellers should be permitted to collect no more than their cost of service, which would include a reasonable return on equity."

PG&E is entitled to no more. As the example set out above illustrates, a lawful cost-of-service rate for the portfolio supporting the PSA is on the order of 2.5 cents/kWh for 2003—roughly half of the rate proposed by PG&E.

C. PG&E ACKNOWLEDGES THAT THE TRUE JUSTIFICATION FOR THE RATES PROPOSED IN THE PSA IS TO SERVICE THE DEBT TO BE INCURRED BY GEN UNDER THE PLAN

Further evidence that the rates proposed in the PSA are justified neither by truly comparable benchmark sales in a competitive environment, nor by any other measure of just and reasonable pricing, is provided in various statements of PG&E's, which reveal the true justification for the proposed rates. For instance, at 41-42 of its Gen 205 application, PG&E states that "it would not be possible for Gen to assume this substantial portion of Exit Financing Debt without the PSA." That is, the rates in the PSA were determined by reference solely to the amount of financing which PG&E anticipates that Gen will incur after taking possession of the generating assets, including DCPP, and by the cash flow necessary to support that debt. If PG&E thought it could raise additional debt, the rates in the PSA would have been higher. If it had to finance the true market value of the facilities, the rates under the PSA would have to be substantially higher.

In fact, neither the income stream under the PSA nor the PSA itself are necessary for PG&E to emerge from bankruptcy. Nor will PG&E's Plan provide, as PG&E asserts, a quick route out of bankruptcy. The legal infirmities of PG&E's Plan are so extensive (and PG&E apparently so determined to press on with its Plan despite its legal infirmities) that years of litigation over the plan are almost inevitable. Rather, as discussed in part I above, the CPUC has formulated an Alternative Plan, to be outlined in greater detail to the Bankruptcy Court on February 13, 2002, which would enable PG&E to promptly emerge from bankruptcy with a minimum of litigation, without dismantling the company, and without the need to charge PG&E ratepayers the egregious rates proposed in the PSA.

* * * * *

As noted in part I above, the legal infirmities of the PG&E Plan, and their attendant regulatory uncertainties, raise serious doubt about the ultimate approval of that Plan. However, these infirmities and uncertainties also demonstrate that there is no reasonable assurance that Gen will be able to cover the estimated operating costs of DCPP. Thus, Gen cannot by any stretch of the imagination be deemed to satisfy the financial responsibility requirement of the Commission's regulation, at 10 CFR 50.33(f)(2). Moreover, there is a reasonable Alternative Plan, sponsored by the CPUC, under which PG&E will continue to operate DCPP under cost-of-service rates, that <u>does</u>

provide reasonable assurance of more than adequate funding for all of DCPP's plant operational and maintenance-related needs, thereby assuring protection of public health and safety. For all these reasons relating to the lack of financial responsibility of the proposed transferee of DCPP, the Commission should reject PG&E's request for a license transfer.

IV. THE TRANSFER OF DIABLO CANYON OWNERSHIP AND OPERATING LICENSES FROM PG&E TO GEN AND DIABLO WOULD REDUCE CALIFORNIA'S REGULATORY RESPONSIBILITIES OVER NUCLEAR POWER TO THE DETRIMENT OF THE PUBLIC HEALTH, SAFETY AND WELFARE OF THE CITIZENS OF CALIFORNIA.

A. THROUGH ITS REORGANIZATION AND LICENSE TRANSFER SCHEME, PG&E IS SEEKING TO TRUMP THE STATE'S VITAL INTERESTS IN REGULATING UTILITIES

1. California's Basic Interest in Regulating Public Utilities

Approval of PG&E's application to transfer DCPP, as well as other generation facilities, from a state regulated utility to a newly created, largely unregulated LLC would undermine the longstanding relationship between the utility and the ratepayers of California. The contours of this relationship are established in a number of California Public Utilities Code sections that PG&E would like to unilaterally nullify through its reorganization and license transfer scheme.

Under its reorganization scheme, PG&E seeks to evade Public Utilities Code §§ 701, 702, 728, and 761. *See* PG&E's Amended Disclosure Statement ("Amend. Disc. Stmt.") dated December 19, 2001. These sections establish the fundamental relationship between the State of California and its regulated public utilities. Section 701 is the basic enabling provision that establishes the Commission's power to regulate public utilities. It provides that "[t]he Commission may supervise and regulate every public utility in the State and may do all things, whether designated in this part or in addition thereto, which are necessary and convenient in that exercise of such power and jurisdiction." Cal. Pub. Util. Code §701. Section 702 requires that every public utility obey and comply with every order, decision or rule of the CPUC. Cal. Pub. Util. Code §702. Section 728 provides that whenever, after a hearing, the CPUC finds that rates or classifications set by a public utility are unjust and unlawful, the CPUC shall determine and fix reasonable rates to be observed by the utility. Cal Pub. Util. Code §728. Section 761 provides that whenever, after a hearing, the CPUC finds that any other aspect of a public utility's business is unjust, unreasonable, or otherwise contrary to the public interest, the CPUC shall determine the proper course of conduct for the utility, and order the utility to perform accordingly. Cal. Pub. Util. Code §761.

These four statutes establish the core powers of the CPUC as a regulator. The State of California's interest in enforcing them is, thus, synonymous with its interest in the regulation of public utilities itself. PG&E is using the Bankruptcy Court, the NRC and FERC to dodge its responsibilities under these code provisions. The attempt to transfer its substantial generation assets, particularly DCPP, from this regulated utility to an unregulated LLC is a direct attack on the authority of the State of California, in its sovereign capacity as a government and a regulator, to regulate electrical utilities in the interest of the health and safety of the citizens of California.

2. California's Interest in Ensuring Universal Service and Fair and Just Utility Rates

Through its reorganization and license transfer scheme, PG&E also seeks to escape from its responsibilities under Public Utilities Code Sections 451 and 453. (Amend. Disc. Stmt., at 129). Section 451 establishes the fundamental "duty to serve" obligation on the part of a public utility to serve all of the needs of its customers within its designated area of operation. Cal. Pub. Util. Code §451. Section 451 also establishes the rule that all rates or charges demanded by a public utility for any service rendered or commodity furnished shall be just and reasonable. *Id.* Section 453 provides that all such rates and charges must be set on a non-discriminatory basis, without any unreasonable difference in rates between customers, localities, or classes of service. Cal. Pub. Util. Code § 453.

If Sections 701, 702, 728, and 761 set forth the basic powers of the CPUC and the relationship between the State and its regulated public utilities, Sections 451 and 453 represent the basic purpose of public utility regulation. Without its ability to enforce the utilities' basic obligation to provide electric service to every California customer on a fair and non-discriminatory basis, the State's ability to guarantee this essential right would be eviscerated. *See* Cal. Pub. Util. Code §739.

3. California's Interest in Protecting Financial Integrity and Dedication of Service

PG&E also seeks to shirk its duties under California Public Utilities Code Sections 701.5, 816-830, 845, 851, 852, and 854 by transferring the Diablo Canyon ownership and operating licenses. (Amend. Disc. Stmt., at 130.) These laws provide that a public utility may not enter into certain transactions that affect its ownership and control, financial integrity, or ability to carry out its functions without prior review and approval by the CPUC. Cal. Pub. Util. Code §§ 701.5, 816-830, 845, 851, 852, 854. The purpose of these sections is to ensure that regulated public utilities do not enter into transactions that undermine their ability to serve their customers. Section 851, for example, prevents a utility from disposing of property useful in the performance of its duty to serve the public without the prior approval of the CPUC, to ensure that a public utility does not jeopardize the public health and welfare by rendering itself unable to serve. Cal. Pub. Util. Code § 851.

As a regulated public monopoly, PG&E does not have the same freedom with its property and operations as a purely private company. In exchange, PG&E enjoys the considerable advantages of being a public monopoly. The State of California has a strong interest in ensuring that its public utilities remain financially sound and in the position to satisfy their obligations to serve their designated service areas. The Legislature determined that the above kinds of transactions have the potential to affect a utility's ability to perform its duties. Thus, the Legislature directed the CPUC to review all such transactions to ensure that they do not have a detrimental impact upon a utility's ability to serve.

Furthermore, California has a strong interest in conditioning any public utility transaction with the potential to affect the environment upon the performance of a CEQA environmental review. *See* Cal. Pub. Res. Code § 21000, *et. seq*. Only by weighing the environmental impacts of a proposed action before it is taken can the State protect its environment and inhabitants from unnecessary harm.

In attempting to bypass the CPUC's review obligation through a bankruptcy reorganization and license transfer, PG&E attacks the State's basic power to protect the public against the danger that a utility will fail to carry out its duties, or the danger that a proposed utility transaction will have adverse impacts upon the environment.

4. California's Interest in Preventing the Loss of In-State Generation Facilities

PG&E also seeks to dodge the mandates of Public Utilities Code Section 377. (Amend. Disc. Stmt., at 129.) Prior to January 2001, that section provided that, after market valuation, an electrical utility's generation assets would become eligible for deregulation. In the midst of the State's energy crisis, however, the government feared that California electrical utilities might sell or dispose of generation assets to third parties not obligated to serve California ratepayers and not subject to regulation by the Commission.

In January 2001, the California Legislature passed AB1X 6, amending Section 377 to prohibit any public utility from disposing of any generation facilities before January 1, 2006. *See,* California Statutes of 2001, chapter 2. As the Legislature explained in adopting AB1X 6 to take effect immediately as an urgency statute, it amended Section 377 "to ensure that public utility generation assets remain dedicated to service for the benefit of California ratepayers, and are not deregulated as a consequence of market valuation, without appropriate review and authorization of the Public Utilities Commission pursuant to Section 851 of the Public Utilities Code." *Id.*, Sec. 5.

In seeking to thwart Section 377's moratorium, PG&E is using the Bankruptcy Court, the NRC and FERC in an attempt to reverse the California Legislature's recent sovereign determination, during a time of crisis, that it is essential to public health and safety that all electrical generation assets located in California remain dedicated to service for the benefit of the people of California. Following the proposed license transfer, Diablo would have no such obligation to the citizens of California.

5. California's Interest in Preventing Improper Inter-Company Transactions

Under the reorganization and license transfer scheme, PG&E also seeks to avoid the application of California Public Utility Code Sections 797 and 798 and the CPUC's Affiliate Transaction Rules. (Amend. Disc. Stmt., at 130-31.) Section 797 provides that the Commission shall periodically audit all significant transactions between a public utility and its subsidiaries or affiliates. *See* Cal. Pub. Util. Code § 797. Section 798 provides for civil penalties where the Commission determines that a utility has willfully made an imprudent payment to, or received a less than reasonable payment from, a subsidiary or affiliate. *See* Cal. Pub. Util. Code § 798. The Affiliate Transaction Rules provide a comprehensive code governing the relationship between California's energy utilities and certain of their affiliates. These Rules set forth rules of nondiscrimination and disclosure and separation standards. They also address to what extent a utility should be required to have its non-regulated or potentially competitive activities conducted by its affiliate. *See* CPUC Decision No. 98-08-035, 1998 Cal. PUC LEXIS 594, *2 (August 8, 1998).

The State has an obvious and strong interest in limiting the scope of the monopolies it grants to public utilities in exchange for the utilities' undertaking to serve. These provisions and rules prevent a public utility from abusing its non-arm's length relationship with subsidiaries and affiliates in competition, and otherwise acting to the detriment of the public. In short, these rules ensure that the considerable benefits that flow from being a regulated public monopoly are properly concentrated in that "regulated" monopoly, and not inappropriately transferred to or otherwise enjoyed by private, unregulated affiliates of that monopoly, which would not be subject to the same regulatory restrictions.

6. California's Interest in Preventing the Misuse of the Holding Company Structure

In Decisions Nos. 96-11-017 and 99-04-068, the CPUC first approved a transaction in which PG&E became a wholly owned subsidiary of a utility holding company. *See* CPUC Decision No. 96-11-017, 1996 Cal. PUC LEXIS 1141 (November 6, 1996). The CPUC later approved a second transaction in which a major subsidiary of the regulated utility, through which it conducted most of its business, became a subsidiary of the parent. *See* CPUC Decision No. 99-04-068, 1999 Cal. PUC LEXIS 242 (April 22, 1999).

In approving these transactions, the CPUC ordered PG&E to continue to comply with its obligations under the Public Utilities Code, including providing appropriate reports to the CPUC, providing the CPUC with access to the corporate books and records, paying dividends only on the basis of a ratepayer interest standard, rather than when it might be in the interest of an affiliate, and properly reporting transactions with affiliates. *See* Decision No. 99-04-068, 1999 Cal. PUC LEXIS at *140-141. As a condition of this approval, PG&E agreed not to abuse the holding company structure as a means to evade its obligations under the Public Utilities Code, and agreed not to abuse the structure to enter into improper self-dealing transactions and cross-subsidize unregulated lines of business. *Id.*

The CPUC imposed these conditions to prevent PG&E from defeating regulation through a purely formal change in corporate organization. In claiming that these conditions imposed by the CPUC are invalidated due to its bankruptcy filing, PG&E signals its intent to employ the holding company structure as a means to escape its obligations under the California Public Utilities Code. As was amply discussed in Section III above, the new holding company structure created by this reorganization is ripe for abuse.

7. California's Interest in Requiring Utilities to Share Gains On Sale with Ratepayers

PG&E has claimed that the CPUC's "gain-on-sale" rules would be preempted by a Confirmation Order of the Bankruptcy Court. (Amend. Disc. Stmt., at 130.) Generally, these rules establish that gain on the sale of utility properties must be allocated between the shareholders of the utility and the ratepayers, in the form of an offset to the rate base.

Because public utilities operate with ratepayer funds, for the benefit of the ratepayers, the CPUC has determined that ratepayers are entitled to share the benefit of the sale of utility property. The CPUC adopted these rules to encourage utilities to maximize the value of utility assets, while at the same time giving ratepayers the greatest possible reduction in the rate base. California ratepayers have an obvious economic stake in an asset as valuable as the DCPP. Thus, the CPUC's gain-on-sale rules assure that the ratepayers receive an adequate return on the long-term investment they have paid for through rates, and that the property's value is not distributed to holding companies and private shareholders only.

B. STATE REGULATION HAS SIGNIFICANT ADVANTAGES OVER FEDERAL REGULATION

With its reorganization and license transfer scheme, PG&E seeks to transfer its crown jewels from the utility, permanently removing major generating assets from CPUC regulation. Removing state oversight of DCPP is not in best interest of Californians. Under PG&E's proposed scheme, oversight over the rates charged for power generated by the plant would pass from the CPUC to FERC, which oversees wholesale transactions. However, FERC's oversight over the proposed 12-year wholesale power purchase agreement between the proposed Gen and PG&E is insufficient to protect the interests of California ratepayers. State oversight is additionally necessary to handle the many other responsibilities relating to energy generation by a facility such as DCPP.

Ultimately, any regulatory regime exists for the benefit of the public. Here, the residents of California can best be served by local regulations by the CPUC. In a state with such a large population and economy, the regulatory oversight of energy matters necessarily involves considering the rights and interests of many diverse individuals, consumer groups, commercial entities, municipalities, regional districts, other public utilities, and a host of marketing and shipper interests. For one thing, unlike FERC, the CPUC provides for local public hearings, not just in large cities around the State, but also in smaller suburban and rural communities. These hearings allow the average customers of public utilities to communicate their recommendations and objections, based on real-life experiences with their public utilities. Many of the parties and stakeholder groups who appear before the CPUC would almost certainly be unable to participate at FERC, which holds its hearings in Washington, D.C. and does not address the type of local regulatory concerns, and the health and safety of California citizens, that the CPUC routinely deals with.

Furthermore, in formal proceedings before the CPUC, many cities, consumer groups, irrigation districts, and individuals have the realistic opportunity to participate as active parties. By statute, interveners who contribute to the outcome of the proceeding can receive compensation. *See* Cal Pub. Util. Code §§ 1801, *et seq*. In this way, customers or customer groups can afford, for example, to hire expert witnesses and generally have the means to advocate their views and protect their interests. This important element of the CPUC's regulation of PG&E, as well as the other public utilities of the state, would be lost with respect to an extremely large part of the costs that are calculated into rates, and with respect to the administration of safety and reliability standards that directly involve the public welfare. Under FERC regulations and procedures, only those who can afford to travel to Washington, D.C. (where the FERC exclusively resides) and only those who pay for their own time and expert witnesses would be able to participate in setting rates and in adopting the rules for services that affect their personal lives as well as the economies of their communities. In such cases, these hearing may be without the voices of individuals and consumer groups that directly represent the public interest.

V. PUBLIC SAFETY AND WELFARE ARE THREATENED BY THE PROPOSED LICENSE TRANSFER

Such local concerns are particularly relevant in a post September 11th country where citizens are anxious about state infrastructure reliability and safety, particularly regarding potential terrorist targets such as nuclear power plants. Just this past Friday, a front-page headline in the local Oakland Tribune newspaper read:

> **New Terror Attacks on U.S. Predicted**
> **Nuclear reactor seen as possible target**

See Exhibit H, which is a copy of the newspaper article under this headline clipped from Oakland Tribune of February 1, 2002.

The attached article speaks for itself. According to Secretary of Defense Donald Rumsfeld, nuclear power plant safety is now a fundamental matter of national security, and the lives of millions of Americans are at stake. In the vicinity of DCPP, the lives of over a hundred thousand Californians are at stake.

Given its mission to protect public health and safety, the NRC most certainly should not approve a license transfer, such as the one at issue in this proceeding, in which important safeguards to public health and safety will be lost as a result of the deprivation of concurrent state jurisdiction over an NRC-regulated facility. The task of protecting public safety and national security does not fall to the federal government alone. Since DCPP was licensed in the 1980's, the CPUC the NRC have worked in tandem to assure the safety and reliability of that facility.

In the wake of September 11th, it would be a dereliction of its public duty for the

NRC to dissolve the fruitful and beneficial collaboration of state and federal agencies in overseeing the safety and reliability of DCPP. And yet, as astonishing and unacceptable as its implications are, in this Application, PG&E asks the NRC to dismiss the State of California from any further responsibility to help the NRC oversee the public safety related aspects of the operation of DCPP. Such a dismissal would unquestionably harm public health and safety and would certainly constitute a dereliction by the NRC of its duty to the public and, more broadly, to help assure national security in connection with the operation of nuclear power plants.

A. FINANCIAL ASPECTS

Several critical financial-related public safety and security issues arise in connection with the proposed transfer of the DCPP license from PG&E to Diablo. These issues arise from the transition from a cost-of-service to a market-driven rate base. In the past, nuclear power has required massive public subsidy. Now, however, previously subsidized assets are being transferred out from under public control. This phenomenon poses two major sets of problems:

1. How can nuclear power plants be guaranteed to be run properly at market-based rates? No subsidy plus lower profits equals a recipe for cutting corners. In order to be as competitive as possible in the free market, Diablo will certainly attempt to reduce operating expenses, which, in turn, could very conceivably affect plant safety and reliability, and lead to disaster.

2. The relatively distant relationship between Diablo and its ultimate Parent, PG&E Corporation, seems structured to flow profits from Diablo to Parent while isolating Parent from responsibility for plant operations and safety. Diablo will be held by Gen, which in turn will be held by Newco, which in

> turn will be held by Parent, PG&E Corporation, three levels of limited liability away. In a worst-case scenario, Parent could loot Diablo, blow it out into bankruptcy and then leave the public holding the bag.

A huge safety risk is imposed upon the public by allowing nuclear plants to be run on a profit maximization basis. As is discussed in great detail in part III above, the NRC must accordingly determine whether or not this new entity can properly run DCPP. In this regard, it must be noted that Parent and its subsidiaries have no experience operating nuclear power plants in a deregulated environment. Diablo will operate under a new set of incentives, *i.e.* market ones, and will strive to be unprecedentedly "lean and mean." As a matter of sound public policy, especially in the wake of September 11, should we as a society give control over a nuclear power plant to an entity which may be feeling its way along, and compromising safety and reliability in the process? Public safety and national security dictate that this is too important a matter to allow for unsupervised experimentation.

We can safely presume that, in response to newly relevant market constraints, DCPP will try to downsize its workforce. Even though DCPP will be locked into a 12-year contract to provide power above market rates, the profits realized will not necessarily be applied towards plant maintenance and safety. It will most likely follow the industry trend and not hire the full complement of staff from DCPP's current owner, PG&E. Similarly, DCPP will probably increase its use of overtime. Safety and reliability can only be negatively affected by the likely implementation of such policies.

Moreover, in light of this and other license transfers, the NRC's Revised Reactor

Oversight Process and shift towards "risk based" regulations come at a particularly inopportune moment. They reduce the number of resident inspectors and lessen NRC oversight and on-site support at time of change in ownership and operational priority (*i.e.* merchant rather than regulated cost-of-service based). Not only is the risk to public health and safety evidently increased, but also the failure of any nuclear power plant at this juncture, for operational or financial reasons, could lower market confidence and adversely affect the entire nuclear power industry. Once again, unsupervised experimentation poses unreasonable risks.

Unlike the previous owner, DCPP will have no rate base to support it in time of financial need. The proposed license transfer lacks any adequate assurances of Diablo's ability and financial wherewithal to assure safe operation. A dip in the profitability of the plant could therefore compromise public safety.

Furthermore, as Californians have seen during the recent energy crisis, Diablo's profits will flow to the Parent along a one-way pipeline. The manner in which Diablo's limited liability corporation is structured could well inhibit its flexibility to react quickly to unanticipated problems. Diablo, as a nested LLC, will provide a source of profit to Parent in good times, but will be forced to stand on its own when profits go negative. Accordingly, if Diablo is to acquire the license for DCPP, we must be sure that it is capable of anticipating and meeting maintenance and decommissioning costs. Otherwise, in the event of a crisis or prolonged period of unstable or negative profits, the LLC structure will allow the holding company to bankrupt Diablo and avoid financial responsibility. We have already seen such a scenario realized in the current PG&E

bankruptcy case.

B. PUBLIC SAFETY ASPECTS

Finally, the proposed license transfer would remove a significant level of public safety oversight from DCPP simply by taking ownership out of the hands of PG&E. If PG&E is successful in persuading the Bankruptcy Court to accept its proposed bankruptcy reorganization Plan, DCPP will no longer fall under California regulation. This would not only remove the CPUC from its oversight role, but would also spell the death knell of the Diablo Canyon Independent Safety Committee ("DCISC"). The DCISC was established as a part of a settlement agreement arising out of the CPUC's proceedings in connection with its approval of DCPP. This agreement set up the DCISC as an independent safety committee for the purposes of reviewing DCPP's operations with respect to safety, and for recommending changes to improve safety. The agreement further provided that: (1) the DCISC shall have the right to receive certain operating reports and records of Diablo Canyon; (2) the DCISC shall have the right to conduct an annual examination of the Diablo Canyon site and such other supplementary visits to the plant site as it may deem appropriate; and (3) the DCISC is to prepare an annual report, and such interim reports as may be appropriate, which shall include any recommendations of the Committee.

The detailed nature of the review that the DCISC conducts, and the great value of that review both for public health and safety, for national security, and as a crucial adjunct to the NRC's own oversight responsibility, can best be demonstrated by a review of the thorough and detailed nature of the DCISC's Annual Reports. Accordingly, a copy of the most recent such Annual Report, covering July 1, 2000 through June 30, 2001, and approved on October 17, 2001, is attached hereto as Exhibit I. Although this Report is voluminous, it evidences a high seriousness of purpose and a profound depth of technical expertise. Indeed, one of the current members of the DCISC, Dr. E. Gail DePlanque, is a former NRC Commissioner.

It would be a shame and, again, a dereliction of the NRC's public responsibilities, to approve a proposed license transfer that would have the effect of eliminating a public oversight body that has done such a commendable job in dovetailing with, and supplementing, the Commission's own nuclear power plant safety oversight jurisdiction. Given the urgent need since September 11th for nuclear power plant safety to be a major national priority, groups like the DCISC should be encouraged and supported, not overlooked and dismissed. For this important public policy and national security reason alone, the NRC should reject PG&E's application in this matter.

VI. CONCLUSION

For the foregoing reasons, the CPUC respectfully requests that the NRC grant its petition for leave to intervene in this matter, and grant its motion to dismiss the Application on file in this matter as premature. In the alternative, CPUC requests that the NRC issue an order holding any proceedings in this matter in abeyance until the all legal issues relating to the possible preemption of state authority raised in the Bankruptcy Court proceeding have been fully addressed and resolved. Finally, if and when the NRC does moves forward on this matter, the CPUC requests the Commission to hold a substantive subpart G hearing pursuant to 10 C.F.R. §2.1329(b), due to the special circumstances concerning the subject of the hearing.

February 5, 2002

Respectfully submitted,

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EXHIBIT A

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FILED
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UNITED STATES BANKRUPTCY COURT
SAN FRANCISCO, CA

UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION

In re PACIFIC GAS AND ELECTRIC COMPANY, a California corporation, Debtor. Federal I.D. No. 94-0742640	Case No. 01-30923 DM Chapter 11 Case **CALIFORNIA PUBLIC UTILITIES COMMISSION'S OBJECTION TO PROPOSED DISCLOSURE STATEMENT FOR PLAN OF REORGANIZATION UNDER CHAPTER 11 OF THE BANKRUPTCY CODE FOR PACIFIC GAS AND ELECTRIC COMPANY PROPOSED BY PACIFIC GAS AND ELECTRIC COMPANY AND PG&E CORPORATION** Date: December 19, 2001 Time: 9:30 a.m. Place: 235 Pine Street, 22nd Floor, San Francisco, California

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MISCELLANEOUS

The California Public Utilities Commission (the "CPUC"), a creditor and party in interest in this chapter 11 case, by and through its undersigned counsel, submits this objection (the "Objection") to the proposed Disclosure Statement For Plan of Reorganization Under Chapter 11 of the Bankruptcy Code For Pacific Gas and Electric Company Proposed by Pacific Gas and Electric Company and PG&E Corporation, dated September 20, 2001 (the "Disclosure Statement" or "D.S."). In support of its Objection, the CPUC respectfully represents as follows:

BACKGROUND

On September 20, 2001, Pacific Gas and Electric Company ("PG&E") filed its proposed Plan of Reorganization Under Chapter 11 of the Bankruptcy Code for Pacific Gas and Electric Company (the "Plan") together with its Disclosure Statement.

On October 9, 2001, this Court held a status conference concerning the Disclosure Statement (the "October 9th Status Conference"). At that Status Conference, it was made clear that the Plan and Disclosure Statement were prepared and filed without any negotiation or discussion with many of the key players involved in this case and in the regulation of PG&E's operations, including the CPUC and representatives of the State of California. The CPUC and the State Attorney General's Office also expressed their concern that the myriad requests for declaratory and injunctive relief dispersed throughout the Plan and Disclosure Statement, most of which are aimed at displacing the CPUC's and the State's existing regulatory oversight over PG&E, must be the subject of one or more adversary proceedings.

By Order dated October 10, 2001 (the "October 10th Order"), this Court required that any party in interest that contends that an adversary proceeding is required for the Proponents[1] to obtain any of the relief requested in the Plan must file an objection (the "Adversary Proceeding Objection") by November 6, 2001 setting forth the specific relief sought in the Plan that such party contends can only be obtained by adversary proceeding. This Court further set November 27, 2001 as the last day for filing and serving written objections to the Disclosure Statement and

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1 Capitalized terms used and not defined herein shall have the meanings ascribed to them in the Plan and Disclosure Statement.

established December 19, 2001 as a "place holder" for a hearing to consider approval of the Disclosure Statement.

Pursuant to the October 10th Order, on November 6, 2001, the CPUC timely filed and served its Adversary Proceeding Objection, which is incorporated herein. The CPUC now submits this Objection to PG&E's Disclosure Statement.

PRELIMINARY STATEMENT

Through its Plan and Disclosure Statement PG&E seeks to affect a regulatory jailbreak unprecedented in scope in bankruptcy annals. Under the guise of section 1123(a)(5) of the Bankruptcy Code and through a misapplication of the debtor protection provisions of chapter 11, PG&E seeks sweeping preemptive relief primarily in the form of no fewer than fifteen affirmative declaratory and injunctive rulings, each designed to permanently dislocate various state and local laws and regulations affecting PG&E's operation of its public utility.[2] PG&E's Plan is concerned only secondarily with adjusting debtor-creditor relations and restoring its utility operations to financial health. To be sure, if those were PG&E's primary concerns, then would have proposed a much more straightforward reorganization strategy.

PG&E has as its own agenda an escape from CPUC and State regulation. From the outset of this case it has been clear that PG&E seeks to employ this Court as a super-legislature. It first tried in its adversary proceeding against the CPUC where it attempted (unsuccessfully) to overturn portions of the CPUC's March 27th Order.[3] Its Plan and Disclosure Statement constitute more of the same. As with its earlier case against the CPUC, its current scheme is deeply flawed on many levels – constitutional and bankruptcy alike. Such flaws make approval of PG&E's Disclosure Statement at this stage imprudent.

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2 *See* CPUC's Adversary Proceeding Objection (Docket No. 3104), at 4-5, for a brief description of such requests for declaratory and injunctive relief.

3 *Southern Cal. Edison Co.*, 2001 WL 327151 (Cal. P.U.C.) 207 P.U.R. 4th 261 (Mar. 27, 2001) (int. opinion re: proposed rate increases) (the "March 27th Order).

The fundamental problem in approving PG&E's Disclosure Statement is that it describes a Plan that is unconfirmable. As demonstrated below, the Plan fails to satisfy certain plan confirmation standards, including those contained in sections 1129(a)(1), (3), (6) and (11) of title 11 of the United States Code, 11 U.S.C. §§ 101 et seq. (the "Bankruptcy Code"), for the following reasons:

- The Plan may not comply with the Bankruptcy Code, as required by section 1129(a)(1), because it fails to contain adequate means for its implementation, a requirement under section 1123(a)(5) of the Bankruptcy Code. The CPUC recognizes that a conclusive determination of this issue necessarily must await the outcome of the adversary proceeding(s) PG&E must commence to obtain the declaratory and injunctive relief it seeks. But approval of the Disclosure Statement at this stage is, at best, premature.

- The Plan has not been proposed in good faith, as required by section 1129(a)(3), because it is inconsistent with the purposes and objectives of the Bankruptcy Code.

- The Plan may provide for hidden rate increases without CPUC approval, in violation of section 1129(a)(6) of the Bankruptcy Code.

- The Plan may not be feasible, as required by section 1129(a)(11). The Plan is predicated entirely upon PG&E's receipt of favorable rulings on many of its requests for declaratory and injunctive relief, as well as favorable outcomes at the FERC, SEC and NRC. Until PG&E obtains such rulings, including by way of one or more adversary proceeding(s), a feasibility determination is impossible.

Where, as here, a disclosure statement describes a Plan that is unconfirmable, the law is clear – such disclosure statement should not be approved.

Approval of PG&E's Disclosure Statement now would place the proverbial confirmation cart before the horse. The Court should first determine whether the relief PG&E seeks is lawful. There is sufficient uncertainty surrounding the lawfulness of PG&E's Plan to warrant such an approach. To proceed otherwise may result in the waste of huge amounts of estate and judicial resources.

Yet, even if this Court disagrees that approval now is premature, the Disclosure Statement still should not be approved. Styled as a complaint against the CPUC and the State of California, the Disclosure Statement lacks the objectivity required for its dissemination to creditors. The Disclosure Statement is riddled with half-truths, misstatements and omissions.

Also, in many instances it leaves unanswered more questions than it answers. Thus, at a minimum, the Disclosure Statement must be substantially amended prior to its approval by this Court.

For these reasons approval of the Disclosure Statement is unwarranted and inappropriate.

ARGUMENT

I.

PG&E'S DISCLOSURE STATEMENT DESCRIBES A PLAN THAT IS UNCONFIRMABLE AS A MATTER OF LAW[4]

This Court should not approve PG&E's Disclosure Statement because it describes a nonconfirmable Plan. The law is well settled in this Circuit and elsewhere that a disclosure statement that describes a nonconfirmable plan is incapable of being approved. *In re Silberkraus*, 253 B.R. 890, 899 (Bankr. C.D. Cal. 2000) ("There are numerous decisions which hold that where a plan is on its face nonconfirmable, as a matter of law, it is appropriate for the court to deny approval of the disclosure statement describing the nonconfirmable plan.") (citi. *In re United States Brass Corp.*, 194 B.R. 420 (Bankr. E.D. Tex. 1996); *In re Spanish Lake Assoc.*, 92 B.R. 875, 877 (Bankr. E.D. Mo. 1988); *In re Pecht*, 57 B.R. 137, 139 (Bankr. E.D. Va. 1986); *In re Century Investment Fund VIII Ltd. Partnership*, 114 B.R. 1003 (Bankr. E.D. Wis. 1990)); *In re Main Street AC, Inc.*, 234 B.R. 771, 776 (Bankr. N.D. Cal. 1999) (denying approval of disclosure statement where plan whose principal purpose was avoidance of application of securities laws was unconfirmable); *In re 266 Washington Assoc's.*, 141 B.R. 275, 288 (Bankr. E.D.N.Y. 1992), *aff'd* 147 B.R. 827 (E.D.N.Y. 1992) (same).[5] To hold otherwise,

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[4] At the outset, the CPUC reserves the right to make these and other objections to the Plan's confirmability in connection with any confirmation hearing that may be scheduled by this Court.

[5] This Court has acknowledged as much. *See* Transcript of October 9th Status Conference at 37 (responding to the U.S. Trustee's position that the Court should not send out a disclosure statement that describes a flawed plan; "If it's – on its face it's unconfirmable, I agree with you of course. The law is clear on that . . . .").

would result in a waste of time and resources and burden the estate with unnecessary expense. *In re Eastern Maine Elec. Coop., Inc.*, 125 B.R. 329, 333 (Bankr. D. Me. 1991) ("[U]ndertaking the burden and expense of plan distribution and vote solicitation is unwise and inappropriate if the proposed plan could never legally be confirmed."); *In re Valrico Square Ltd. P'ship*, 113 B.R. 794, 796 (Bankr. S.D. Fla. 1990) ("Soliciting votes and seeking court approval on a clearly fruitless venture is a waste of the time of the Court and the parties.").

As described more fully below, PG&E's Plan is unconfirmable because it fails to satisfy the confirmation standards set forth in sections 1129(a)(1), (3), (6) and (11) of the Bankruptcy Code. These Plan infirmities render PG&E's Disclosure Statement incapable of being approved.

A. PG&E's Plan Violates Section 1129(a)(1) of the Bankruptcy Code.

Section 1129(a)(1) of the Bankruptcy Code requires a plan of reorganization to comply "with the applicable provisions of [title 11]." 11 U.S.C. § 1129(a)(1); *Resorts Int'l* v. *Lowenschuss (In re Lowenschuss)*, 67 F.3d 1394, 1401 (9th Cir. 1995). ("The bankruptcy court lacks the power to confirm plans of reorganization which do not comply with applicable provisions of the Bankruptcy Code."). "An examination of the Legislative History of [section 1129(a)(1)] reveals that although its scope is certainly broad, the provisions it was most directly aimed at were Sections 1122 and 1123." *In re S&W Enter.*, 37 B.R. 153, 158 (Bankr. N.D. Ill. 1984).

PG&E's Plan violates section 1123(a)(5) of the Bankruptcy Code by failing to provide adequate means for its implementation. *See* 11 U.S.C. § 1123(a)(5).[6] As noted above and in the

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[6] Section 1123(a)(5) provides that

> (a) [n]otwithstanding any otherwise applicable nonbankruptcy law, a plan shall — (5) provide adequate means for the plan's implementation such as—
>
> (A) retention by the debtor of all or any part of the property of the estate;
>
> (B) transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;

CPUC's Adversary Proceeding Objection, PG&E's Plan is predicated upon its obtaining no fewer than fifteen favorable declaratory and injunctive rulings, each designed to displace portions of the CPUC's and the State of California's century-old regulatory authority over PG&E's operations.[7] Where, as here, a plan is largely predicated on one or more favorable judicial rulings, courts have held that the plan fails to satisfy section 1123(a)(5). *See In re Yates Dev., Inc.*, 258 B.R. 36, 43 (Bankr. M.D. Fla. 2000) (holding that plan predicated on favorable appellate court ruling impermissibly shifted the risk of delay in plan effectiveness from the debtor to creditors); *In re Sunflower Racing, Inc.*, 219 B.R. 587, 604-05 (Bankr. D. Kan. 1998) *aff'd.* 226 B.R. 673 (D. Kan. 1998) (holding that plan that is predicated on the occurrence of multiple events whose outcome is uncertain is infeasible).

> (C) merger or consolidation of the debtor with one or more persons;
>
> (D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate;
>
> (E) satisfaction or modification of any lien;
>
> (F) cancellation or modification of any indenture or similar instrument;
>
> (G) curing or waiving of any default;
>
> (H) extension of a maturity date or a change in an interest rate or other term of outstanding securities;
>
> (I) amendment of the debtor's charter; or
>
> (J) issuance of securities of the debtor, or of any entity referred to in subparagraph (B) or (C) of this paragraph, for cash, for property, for existing securities, or in exchange for claims or interests, or for any other appropriate purpose.

11 U.S.C. § 1123(a)(5).

[7] *See* Plan Art. 8.1 (listing many of the declaratory and injunctive requests as conditions precedent to confirmation); D.S. at 147-48 (noting that the Bankruptcy Court's refusal to approve the Reorganized Debtor's conditions for its assumption of the net short position would jeopardize PG&E's financial viability rendering it "unable to consummate the Plan").

That same result is particularly warranted here given that the relief PG&E seeks is unlawful. PG&E bases its claim for such relief on its unprecedented and incredibly sweeping interpretation of section 1123 of the Bankruptcy Code.[8] However, the preemptive relief PG&E seeks is not available under section 1123, nor under any other provision of the Bankruptcy Code for that matter. In addition, PG&E is barred from obtaining the relief it seeks against the CPUC or the State under the Eleventh Amendment to the U.S. Constitution and related principles of sovereign immunity. These legal infirmities render the Plan incapable of being implemented, as required under section 1123(a)(5), which, in turn, renders the Plan unconfirmable.[9]

However, this Court need not, and indeed should not, rule on the Plan's confirmability under sections 1129(a)(1) or (11) in the context of a Disclosure Statement hearing. Rather, such rulings must await the Court's separate determination of the lawfulness of the declaratory, injunctive and other preemptive relief PG&E seeks – relief that is the linchpin of PG&E's Plan and which the CPUC submits may only be sought through PG&E's commencement of one or more adversary proceeding(s) against the CPUC and others whose rights PG&E seeks to affect. *See generally*, CPUC's Adversary Proceeding Objection (Docket No. 3104).[10] Only at that point can interested parties be relatively certain whether PG&E's Plan complies with section

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8 *See, e.g.*, D.S. at 3 ("Pursuant to section 1123(a) of the Bankruptcy Code, the Bankruptcy Code preempts any otherwise applicable non-bankruptcy law that may be contrary to its provisions.").

9 The Plan is likewise infeasible and, thus, violates section 1129(a)(11) as well. Section 1129(a)(11) requires that a plan may only be confirmed if "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan." 11 U.S.C. § 1129(a)(11). By its own admission, certain of the declaratory and injunctive relief PG&E seeks "is a critical component of the overall feasibility of the Plan." D.S. at 147-48 (discussing PG&E's need for this Court to declare that PG&E need not resume procurement of its net open position until certain PG&E-imposed criteria have been satisfied). *See* Objection, *infra* at pp. 14-15, for a further discussion of the CPUC's feasibility concerns.

10 That the Plan itself purports to provide for such declaratory and injunctive relief is violative of section 1129(a)(1) of the Bankruptcy Code. Rule 7001 of the Bankruptcy Rules requires that such relief must be obtained by adversary proceeding. *See* Fed. R. Bankr. P. 7001(7), (9); CPUC's Adversary Proceeding Objection at 8-12. By failing to comply with Bankruptcy Rule 7001 PG&E's Plan cannot comply with section 1129(a)(1).

1129(a)(1) or (11) of the Bankruptcy Code and is otherwise confirmable. Until then, however, approval and dissemination of PG&E's Disclosure Statement would be premature and could result in a waste of estate and judicial resources.

Accordingly, because the adversary proceeding(s) likely will resolve a number of critical issues directed at the Plan's confirmability, approval and dissemination of the Disclosure Statement should await their outcome.[11]

B. PG&E's Plan Violates Section 1129(a)(3) of the Bankruptcy Code.

PG&E's Plan has not been submitted in good faith as required by section 1129(a)(3) of the Bankruptcy Code. Under that section, a prerequisite to confirmation is that "[t]he plan has been proposed in good faith and not by any means forbidden by law." 11 U.S.C. § 1129(a)(3). To satisfy section 1129(a)(3)'s "good faith" requirement, "a Plan must be intended to achieve a result consistent with the objectives of the Bankruptcy Code." *Ryan* v. *Loui* (*In re Corey*), 892 F.2d 829, 835 (9th Cir. 1989); *Pac. First Bank* v. *Boulders on the River* (*In re Boulders on the River*), 164 B.R. 99, 103 (B.A.P. 9th Cir. 1994). Whether a plan is proposed in "good faith" depends upon "the totality of the circumstances" surrounding the debtor's chapter 11 case. *See Stolrow v. Stolrow's, Inc. (In re Stolrow's Inc.)*, 84 B.R. 167, 172 (9th Cir. B.A.P. 1988).

In addition to being consistent with the Bankruptcy Code's purposes and objectives, to satisfy the "good faith" requirement the Plan and Disclosure Statement must not be intentionally

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[11] PG&E's legal entitlement to the declaratory, injunctive and other preemptive relief it seeks is ripe for determination right now. The doctrine of ripeness "prevents courts from deciding theoretical or abstract questions that do not yet have a concrete impact on the parties." *Shell Oil Co.* v. *City of Santa Monica*, 830 F.2d 1052, 1061 (9th Cir. 1987), *cert. denied*, 487 U.S. 1235 (1988). Ripeness requires that a court "'look at the facts as they exist today in evaluating whether the controversy . . . is sufficiently concrete to warrant [judicial] intervention.'" *Id.* at 1062 (quoting *Assiniboine & Sioux Tribes* v. *Bd. of Oil & Gas Conservation*, 792 F.2d 782, 788 (9th Cir. 1986)).

PG&E's filing of its Plan clearly raises the preemption issue and puts squarely before this Court each of its approximately fifteen requests for declaratory and injunctive relief. The CPUC and others have made no secret of our (and their) opposition to the relief PG&E seeks and our (and their) belief that such relief is unlawful. The issues have been joined and it is appropriate to litigate them now, prior to approval of the Disclosure Statement. No purpose is served by delay.

misleading or incomplete. *Big Shanty Land Corp.* v. *Comer Prop., Inc.*, 61 B.R. 272, 281 (N.D. Ga. 1985) (noting that where disclosure is intentionally misleading or incomplete "there is sufficient precedent for resting a finding of bad faith") (citing *American United Mutual Insurance Co.* v. *City of Avon Park*, 311 U.S. 138 (1940); *Barnes* v. *Whelan*, 689 F.2d 193 (D.C. Cir. 1982); *In re Goeb*, 675 F.2d 1386, 1390 n.9 (9th Cir. 1982)).

PG&E's Plan and Disclosure Statement are both inconsistent with the Bankruptcy Code's purposes and objectives and are intentionally misleading.

(a) <u>PG&E's Scheme to Escape from State Regulation is Inconsistent with the Bankruptcy Code's Purposes and Objectives</u>

Though masked in debtor-creditor garb, the focus of PG&E's Plan is its desired escape from state regulation, an unattainable objective long sought by PG&E. Indeed, it may well be the primary motivation for PG&E's decision to walk away from the negotiating table and go its own way in bankruptcy. Surely, a less draconian approach exists for PG&E to satisfy its debts and repay creditors. But PG&E apparently will not consider alternatives that keep it under CPUC and State regulatory control.

There exists no basis under the Bankruptcy Code for PG&E's attempted use of chapter 11 as a legislative device to displace entire regulatory schemes. To the contrary, numerous Bankruptcy Code provisions evince Congressional respect for state and local laws and regulations. *See e.g.*, 11 U.S.C. § 362(b)(4) ("police and regulatory power" exception to the automatic stay); § 541 (property rights determined by reference to state law); 28 U.S.C. § 959(b) (requiring debtors in possession to operate their businesses in accordance with state laws). If PG&E desires to "FERC itself" by transferring vast amounts of property from state to federal control, it must seek the approval of appropriate state and federal legislators and regulators. Such relief is not available to it under chapter 11.

PG&E is not acting in good faith by attempting to use the plan process to deregulate itself by shifting significant estate assets beyond state regulation. As a result, its Plan is incapable of satisfying section 1129(a)(3)'s "good faith" requirement and is thus, unconfirmable.

(b) **The Disclosure Statement is Misleading**

In PG&E's effort to excoriate (unfairly) the CPUC and the State of California and in the process turn creditors against the CPUC and the State and in favor of PG&E's deregulation scheme, PG&E ends up grossly mischaracterizing many of the CPUC's and the State's actions taken prior to and during this case. The result is that the Disclosure Statement is riddled with half-truths and hyperbole and is plainly misleading.

For instance, in Section IV of the Disclosure Statement, captioned "Events Preceding the Commencement of the Chapter 11 Case and Filing of the Plan," PG&E paints an extremely distorted and one-sided picture of the regulatory events preceding its chapter 11 filing. Without responding to each and every misstatement, mischaracterization, distortion or omission (which would take great length), the CPUC will nonetheless, through a few key illustrations, attempt to debunk certain of PG&E's myths:

- **MYTH:** The CPUC and representatives of the State of California failed to address promptly PG&E's financial situation. *See, e.g.*, D.S. at 41-43.

- **FACT:** On the contrary, the CPUC moved quickly. As a regulatory body, the CPUC is required, among other things, to provide due process to the various parties in its proceedings and to comport with various statutory and procedural requirements. In many instances, the CPUC accelerated the emergency rate relief proceedings, waived or reduced parties' comment periods and removed procedural barriers that otherwise would have delayed CPUC decisions. The CPUC also aided PG&E in other respects, such as by implementing the State's emergency energy legislation and challenging at the FERC the unjust and unreasonable wholesale electric prices charged to PG&E and seeking refunds therefor.

- **MYTH:** The CPUC hindered PG&E's ability to enter into block forward contracts for the purchase of power to hedge against spikes in market prices. D.S. at 32-34.

- **FACT:** During the first 18 months after the CPUC approved PG&E's participation in the California Power Exchange Corporation's block forward market ("BFM") (July 1999 through December 2000), PG&E utilized only about 35% of its BFM procurement allotment. Though PG&E faults the CPUC for not authorizing its use of hedging instruments earlier, PG&E failed to fully utilize the authority it was given. PG&E claims that the BFM proved to be thinly traded and of limited use for hedging purposes. D.S. at 26. While that may be true, it was due, in large part, to PG&E's and California's other investor-owned utilities' reluctance to commit their demand to the BFM. PG&E would have been afforded significant price protection against the run up of wholesale electric prices that began in May 2000 had it utilized the BFM to a greater extent.

- **MYTH:** The CPUC, consumer groups and policymakers thrust deregulation upon PG&E and California's other investor-owned utilities. D.S. at 28-30.

- **FACT:** PG&E not only supported passage of AB 1890 in 1996, but claimed credit for its development. For example, in its 1997 annual report, the Parent stated that "our Utility in conjunction with other California electric utilities, the CPUC, state legislators, consumer advocates, and others, developed a transition plan, in the form of state legislation [AB 1890], to position California for the new market environment." *See* 1997 PG&E Corp. Annual Report, at 20-21. It is not surprising that PG&E and its Parent took credit for deregulation in 1997. During the first few years of deregulation PG&E profited handsomely as a result of the artificially high rate freeze and was able to upstream billions of dollars to its Parent. Now, unhappy with the way things turned out, PG&E and its Parent seek only to attribute blame. PG&E cannot have it both ways.

- **MYTH:** The CPUC's audits revealed that PG&E "had accurately portrayed the accounting on which the Debtor had calculated that the rate freeze had ended." D.S. at 48-49.

- **FACT:** The CPUC's audit report contained no such finding. Such a finding would have required the auditors to market value PG&E's assets, which the auditors did not do.

- **MYTH:** "The Debtor was forced to seek relief under Chapter 11 of the Bankruptcy Code in part because of the *unlawful* actions of the State and the CPUC relating to the recovery of transition costs and the filings to timely conclude that the conditions for ending the rate freeze had been satisfied." D.S. at 91 (emphasis added).

- **FACT:** This is an expression of PG&E's opinion; it is not a fact. Neither the State's nor the CPUC's actions have been held to be unlawful. To the contrary, in the only challenge to have been decided, this Court held that the accounting true-up portion of the CPUC's March 27th Order did not violate the Bankruptcy Code's automatic stay.

The Disclosure Statement is misleading in other key respects as well. For example, PG&E represents that Gen's, ETrans' and GTrans' assets will "continue to be regulated to protect the public interest," D.S. at 7, but fails to take account of the vast range of environmental and public interest issues imperiled by PG&E's proposed wholesale transfer of such assets, particularly the hydroelectric and land assets to be transferred to Gen.[12] In addition, PG&E asserts that "[t]he Plan . . . is, in the Proponents' reasoned opinion, the *only* reasonable solution . . . ." D.S. at 54 (emphasis added). The CPUC submits that this is a gross overstatement for at

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[12] For example, the Disclosure Statement fails to address the impact upon California's environment and the public of PG&E's planned swith to the FERC's environmental standards which, in many respects, are less strict than those of the CPUC and the State. The CPUC is concerned that the wholesale transfer of PG&E's transmission and generation assets beyond CPUC and State control could, among other things, negatively impact the State's water flows and water and air quality and result in significant losses of forest, habitat and recreation in PG&E's watershed lands. These and other environmental issues are the subject of an extensive report prepared in connection with PG&E's proceeding before the CPUC to sell its hydroelectric assets. These issues are important and deserve greater mention in the Disclosure Statement.

least two reasons: *first*, PG&E never once approached the CPUC or the State to see if an alternative existed; and *second*, the drastic decline in wholesale power prices during the last four months has left PG&E with "headroom" again, which may provide PG&E and its creditors with viable alternatives.[13] In short, PG&E's Plan is not the "only solution," it merely is PG&E's preferred outcome.

PG&E's intent in unfairly slanting the factual background and other aspects of its Disclosure Statement is clear – it seeks to portray the CPUC and the State as incompetent so that it can curry favor with creditors in support of its deregulation scheme. Essentially, PG&E is telling those voting on the Plan that their only chance to be paid in full is for PG&E to embark upon a regulatory sea change that transfers valuable assets beyond CPUC and State control. That is ludicrous. And, more importantly, it constitutes an abuse of the disclosure process, which is intended to ensure that creditors/voters are presented with objective information that hopefully will inform their decision to accept or reject a plan of reorganization. PG&E's exaggerations and misrepresentations alone merit denial of the Disclosure Statement.[14]

C. <u>PG&E's Plan Violates Section 1129(a)(6) of the Bankruptcy Code</u>.

Despite representations to the contrary in its Disclosure Statement,[15] the CPUC suspects that PG&E's Plan is premised upon a disguised rate increase.[16] Section 1129(a)(6) of the Bankruptcy Code requires as a condition to confirmation that "[a]ny governmental regulatory commission with jurisdiction, after confirmation of the plan, over the rates of the debtor has

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[13] PG&E's Disclosure Statement nowhere mentions "headroom" in electric rates or its record profits in the latest quarter, both of which have been widely reported in the press and PG&E's own SEC filings. Surely, such information is relevant.

[14] In the event that this Court disagrees, then the CPUC requests that, at a minimum, PG&E be required to amend its Disclosure Statement to correct the various misrepresentations contained therein. The CPUC is available to meet and confer with PG&E to craft acceptable alternative language.

[15] *See* D.S. at 6, 69 ("Without raising retail electricity rates above current levels, the Plan provides . . . .).

[16] If the CPUC is wrong, then PG&E should demonstrate why through added disclosure.

approved any rate change provided for in the plan, or such rate change is expressly conditioned on such approval." 11 U.S.C. § 1129(a)(6).[17] PG&E's failure to provide for CPUC approval of any rate increase in its Plan violates section 1129(a)(6) and, as a result, renders PG&E's Plan unconfirmable.

At least two factors inform the CPUC's rate suspicion. The first is that the Plan and Disclosure Statement may be premised upon the assumption that the entire three-cent rate increase ordered by the CPUC on March 27, 2001 belongs to PG&E. Pursuant to the express terms of the March 27th Order, however, a portion of that three-cent rate increase is to be allocated to DWR. March 27th Order at 19 n.4, 27, 56, 64, 67. Thus, if PG&E hopes to keep it all (or any portion that would otherwise belong to DWR), then its electric rates must necessarily increase.[18]

Second, the rates Gen proposes to charge the Reorganized Debtor under the Power Sales Agreement to be entered into between the two exceeds Gen's cost-based rate. Currently, CPUC regulations and State law permit PG&E to charge only cost-based rates. The mark-up above cost provided for in PG&E's Plan is without CPUC consent.

For these reasons, PG&E's Plan is unconfirmable under section 1129(a)(6) of the Bankruptcy Code.

D. <u>PG&E's Plan Violates Section 1129(a)(11)'s Feasibility Requirement</u>.

As noted above, section 1129(a)(11) requires that before a Plan may be confirmed, its proponent must demonstrate that,

> "[c]onfirmation of the plan is not likely to be followed by the liquidation, or the need for further financial reorganization, of the debtor or any successor to the debtor under the plan."

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17 In its Disclosure Statement, PG&E admits that "[t]he CPUC will continue to have jurisdiction over the Debtor's retail electric and gas distribution assets, rates and services . . . ." D.S. at 7. Accordingly, pursuant to section 1129(a)(6) of the Bankruptcy Code, any rate increase provided for by the Plan requires CPUC approval.

18 Because the CPUC has not yet allocated the three-cent rate increase among DWR and PG&E it is unclear how PG&E can keep any portion of such increase without CPUC approval.

11 U.S.C. § 1129(a)(11).

Clearly, if PG&E is unable to obtain at least certain of the various declaratory and injunctive rulings and other preemptive relief it seeks, then its Plan will not be feasible. This much PG&E admits in its Disclosure Statement. *See* n. 9, *supra*.

Other feasibility concerns persist as well. For one thing, PG&E's projections for the Reorganized Debtor's operating revenues assume that "[e]lectric annual load growth approximates 2% per year." Exhibit C to D.S. at 3. This assumption, however, is unsupported by historical evidence, which instead shows that electric load growth has been flat, if not declining. If PG&E is wrong, and history is a more accurate barometer of future load growth, then the Reorganized Debtor may experience unanticipated financial pressures.

The CPUC is skeptical of the Reorganized Debtor's survival for another reason as well. Assuming PG&E's Plan is confirmed, the Reorganized Debtor would be stripped of many crown jewels, such as its hydroelectric and transmission assets and any recovery in its Rate Recovery Litigation (all of which would be transferred to its Parent), yet it would remain burdened with many of the liabilities with which it entered bankruptcy (*i.e.*, those that according to PG&E's Plan will survive chapter 11). The CPUC fears that this imbalance in the Reorganized Debtor's remaining assets and liabilities could seriously jeopardize its ability to weather future financial storms. This fear is underscored by PG&E's own financial projections which show that the Reorganized Debtor's current liabilities will exceed its current assets by between approximately $750 – 800 million per year between the years 2002 through 2005. *See* Exhibit C to D.S., Reorganized Debtor Balance Sheet.

For these reasons, the CPUC believes that PG&E's Plan may not satisfy section 1129(a)(11)'s "feasibility" requirement.

II.

PG&E's DISCLOSURE STATEMENT CONTAINS INADEQUATE INFORMATION

Despite its length, PG&E's Disclosure Statement is riddled with inadequacies. Meaningful and accurate disclosure is at the heart of the reorganization process. *Oneida Motor Freight, Inc.* v. *United Jersey Bank*, 848 F.2d 414, 417 (3d Cir. 1988), *cert. denied*, 488 U.S. 967 (1988); *H & L Dev., Inc.* v. *Arvida/JMB Partners (In re H & L Dev., Inc.)*, 178 B.R. 71, 74 (Bankr. E.D. Pa. 1994). Effective disclosure requires the dissemination of "adequate information," *Knupfer* v. *Wolfberg (In re Wolfberg)*, 255 B.R. 879, 883 (B.A.P. 9th Cir. 2000), defined under the Bankruptcy Code to include:

> information of a kind, and in sufficient detail, as far as is reasonably practicable in light of the nature and history of the debtor and the condition of the debtor's books and records, that would enable a hypothetical reasonable investor typical of holders of claims or interests of the relevant class to make an informed judgment about the plan . . . .

11 U.S.C. § 1125(a)(1).

What constitutes adequate information varies from case to case. *Texas Extrusion Corp.* v. *Lockheed Corp. (In re Texas Extrusion Corp.)*, 844 F.2d 1142, 1157 (5th Cir. 1988), *cert. denied*, 488 U.S. 926 (1988); *In re Diversified Investors Fund XVII*, 91 B.R. 559, 560 (Bankr. C.D. Cal. 1988); *In re Reilly*, 71 B.R. 132, 134-35 (Bankr. D. Mont. 1987). As a general rule, however, "[t]he [plan] proponent should be biased towards more disclosure than less." *Official Comm. of Unsecured Creditors* v. *Michelson (In re Michelson)*, 141 B.R. 715, 720 (Bankr. E.D. Cal. 1992). In that vein, courts have established certain minimum disclosure requirements — information that must be contained in every disclosure statement — including the following:

(a) the events leading to the filing of the bankruptcy petition;

(b) a summary of the proposed plan of reorganization;

(c) a description of the available assets and their values;

(d) the condition and performance of the debtor while in chapter 11;

(e) information regarding claims against the estate;

(f) a liquidation analysis setting forth the estimated return that creditors would receive under chapter 7;

(g) the accounting and valuation methods used to produce the financial information in the disclosure statement;

(h) the collectability of any accounts receivable;

(i) any financial information, valuations or pro forma projections that would be relevant to determinations of whether to accept or reject the plan;

(j) information relevant to the risks being taken by the creditors and interest holders;

(k) the actual or projected value that can be obtained from avoidable transfers;

(l) the existence, likelihood and possible success of nonbankruptcy litigation;

(m) the debtor's relationship with its affiliates;

(n) the future management of the debtor;

(o) the source(s) of information stated in the disclosure statement;

(p) the scheduled claims;

(q) the estimated administrative expenses, including attorneys' and accountants' fees;

(r) the debtor's tax attributes; and

(s) the anticipated future of the company.

See, e.g., In re Dakota Rail, Inc., 104 B.R. 138, 142 (Bankr. D. Minn. 1989); *In re Microwave Prod. of Am., Inc.*, 100 B.R. 376, 378 (Bankr. W.D. Tenn. 1989); *Diversified Investors Fund XVII*, 91 B.R. at 560; *Reilly*, 71 B.R. at 134; *In re Jeppson*, 66 B.R. 269, 292. (Bankr. D. Utah 1986).

In this case, PG&E's Disclosure Statement clearly fails to satisfy at least items (c), (g), (j), (k), (l), (m) (n), (o), (q) and (r) of the foregoing list. PG&E's Disclosure Statement is deficient in numerous other respects as well, as described below.

A. <u>The Disclosure Statement Fails to Disclose Claims Against Third Parties.</u>

PG&E's Disclosure Statement fails to identify significant claims PG&E's bankruptcy estate may have against third-parties. The most glaring omissions are claims against the Parent and against generators and others who sold power to PG&E.

(i) **Claims against the Parent**

PG&E's estate holds certain claims against its Parent which could prove to be a valuable source of recovery for its creditors. The CPUC is aware of at least two types of such claims:[19] (i) claims that the Parent violated the "first priority" rule ordered by the CPUC when it approved PG&E's holding company structure;[20] and (ii) avoidance actions for dividend and other payments made by PG&E to its Parent while PG&E may have been insolvent.[21] Disclosure of these (and other) claims not only is required under the case law cited above, but is essential, for instance, for creditors and others to value the release to be provided to the Parent under Article 11.5(b) of the Plan.[22] Accordingly, PG&E's Disclosure Statement must be amended to include a discussion of the nature and potential value of the claims PG&E's bankruptcy estate may have against the Parent.

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19 These claims are the subject of a pending CPUC investigation. To the extent other claims exist their disclosure is similarly required.

20 The "first priority" rule addresses the Parent's obligation to give "first priority" to PG&E's capital requirements to meet its obligations to serve. *Re: Pacific Gas and Elec. Co.*, 1999 WL 589171 (Cal. P.U.C.) 194 P.U.R. 4th 1 (Apr. 22, 1999) (decision approving formation of holding company) at § 6.4. According to the report (the "Audit Report") issued by the auditors retained by the CPUC in December of 2000 to audit PG&E, "[s]ince 1997 [when the holding company was formed, Parent] has not provided cash, credit or other financial assistance or support to PG&E . . . . Historically, cash has flowed in only one direction, from PG&E to [Parent] and then to [PG&E's] unregulated affiliates." *Review of Pacific Gas and Elec. Co. Financial Condition for Cal. Public Utilities Comm'n*, Barrington-Wellesley Group, Inc. (Jan. 30, 2001) at I-5 *available at* www.cpuc.ca.gov/word_pdf/audit/pge_report.pdf. By failing to downstream funds to PG&E during times of need, the Parent violated the "first priority" rule.

21 The Audit Report further disclosed that "[f]rom 1997 to 1999 PG&E provided [Parent] $4.0 billion in the form of dividends paid and repurchases of stock." *Id.*

22 Article 11.5(b) of the Plan provides that:

> [a]s of the Effective Date, the Debtor releases the Parent from any and all Causes of Action held by, assertable on behalf of, or derivative from, the Debtor, in any way relating to the Debtor, the Debtor-in-Possession, the Chapter 11 Case, the Plan, negotiations regarding or concerning the Plan, the ownership, management and operation of the Debtor, and any transactions or transfers between the Parent and the Debtor, including but not limited to, any Cause of Action arising under Chapter 5 of the Bankruptcy Code or any state fraudulent conveyance statute.

Plan Art. 11.5(b).

(ii) **Generator claims**

PG&E must similarly disclose claims, including refund claims pending before the FERC that PG&E may have against generators and others that sold it power at unjust and unreasonable prices.[23] As the Disclosure Statement correctly points out, the FERC has determined that certain electric sales in California since October 2, 2000 are subject to refund. D.S. at 55. The potential total recovery to the State and its three investor-owned public utilities could range from $1 to $9 billion. Despite their significance, PG&E pays these claims mere lip service in its Disclosure Statement. *See* D.S. 54-55. Greater disclosure is required. Specifically, PG&E should, at a minimum, disclose the estimated value of these claims as well as the likelihood and timing of recovering on them and the potential impact of such recoveries on its reorganization.[24] PG&E should be compelled to do the same with respect to any and all other claims it may have against the generators and other power sellers.

B. The Disclosure Statement Insufficiently Discloses the Risks Associated with PG&E's Scheme to Escape State Regulation.

On its face, PG&E's Plan seems like a panacea for PG&E's creditors – recovery in full with interest. However, it is far from certain that PG&E will obtain the various declaratory and injunctive rulings and other preemptive relief necessary for it to confirm its Plan. Indeed, the CPUC believes that such relief is unlawful. Surely, those voting on the Plan are entitled to know just how bumpy a confirmation road lies ahead. Presently, they are offered no clue.

For starters, the Disclosure Statement should inform those voting on the Plan that the preemptive relief PG&E seeks is unprecedented in scope.[25] The CPUC is unaware of any case in

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[23] The CPUC is aware that this may be a sensitive issue for PG&E given the generators' significant representation on the Creditors' Committee and the Creditors' Committee's support of its Plan. Nevertheless, such disclosure is required because claims against the generators constitute significant assets of PG&E's chapter 11 estate.

[24] PG&E's estate has retained outside counsel to investigate and prosecute claims against the generators and PG&E is active in the FERC refund proceedings. As a result, PG&E could easily supply these added disclosures.

[25] Undoubtedly, PG&E and those familiar with bankruptcy lore will quickly point to the *Public Service of New Hampshire* case as precedential value for the relief PG&E seeks. However, the scope of the preemptive relief sought in that case was much narrower than the relief

which a regulated utility succeeded in deregulating itself under a plan of reorganization. Creditors voting on PG&E's Plan should be made aware of this. In addition, creditors should be apprised of the procedural and timing issues associated with the requested relief. Nowhere does the Disclosure Statement mention that to obtain such relief PG&E likely will have to litigate with the CPUC, the State and others every step of the way, including by way of one or more adversary proceedings against multiple defendants. Nor does the Disclosure Statement contain any reference as to how long it may take PG&E to prevail (including appellate proceedings) or how much it may cost. This information is critical to those evaluating whether to accept or reject the Plan. It is one thing for creditors to expect to receive distributions by January 2002; it is quite another to caution that litigation may delay distributions for years.

Finally, PG&E should provide creditors with some insight into the likelihood that it will obtain the various declaratory and injunctive rulings and other preemptive relief it seeks. It is not enough for PG&E simply to state that such relief is available under section 1123(a)(5) of the Bankruptcy Code. That is a legal determination to be left to this Court. Creditors should be apprised (objectively) of the strengths and weaknesses of PG&E's position, particularly given this Court's stated reluctance to solve "PG&E's, or California's or the country's energy crisis." *Pacific Gas & Elec. Co.* v. *California Public Utilities Comm'n, et al. (In re Pacific Gas & Elec. Co.)*, 263 B.R. 306, 309 (Bankr. N.D. Cal. 2001) (noting that "[t]hat is for others to attempt.").

In a similar vein, PG&E should be required to disclose the obstacles, risks and costs involved in obtaining the various regulatory approvals needed to effectuate its Plan. PG&E should expect that the regulatory approvals and certificates it seeks from the FERC, SEC, NRC and others will be challenged by the CPUC and others whose rights it seeks to affect before those regulatory bodies. All of this should be disclosed.

PG&E seeks here and, ultimately, the chapter 11 plan approved in *PSNH* was a consensual one, rather than a litigation result. Moreover, *PSNH* has no precedential value in this Circuit.

C. PG&E Should Disclose the Laws it Seeks to Preempt.

PG&E should not be allowed to claim preemption of various state and local laws and regulations without first specifically identifying them. Preemption inquiries require precise statutory analyses of both the federal and state statutes in question and an examination of the legislative history of each. 1 Lawrence Tribe, *American Constitutional Law* § 6-28 p. 1177 (3d ed. 2000) ("[T]he most fundamental point to remember is that preemption analysis is, or at least should be, a matter of precise statutory construction rather than an exercise in free-form judicial policymaking."); 2 Ronald Rotunda & John E. Nowak, *Treatise on Constitutional Law*, § 12.1 (3d ed. 1999) ("Before a judicial determination occurs, therefore, the Court must consider the federal law and its operation compared with the state statute and its operation.").

PG&E's assertions that it will seek an affirmative ruling of this Court that section 1123 of the Bankruptcy Code preempts various "state and local laws," are insufficient under any preemption analysis.[26] Instead, PG&E should identify each and every state and local law and regulation it seeks to preempt. Because preemption forms the undergirding of PG&E's Plan, such disclosure is necessary so that interested parties will be on notice of the laws PG&E seeks to preempt. In addition, if this Court overrules the CPUC's and others' Adversary Proceeding Objections, then the Disclosure Statement may serve as the only notice of the Plan's preemptive sweep.[27]

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26 *See, e.g.*, D.S. at 74, 76-77, 80-81; *see also* D.S. at 84 (noting that PG&E will seek a ruling that section 1123 preempts "*certain provisions* of the California Corporations Code in connection with the Internal Restructurings and the Reorganized Debtor Spin-Off") (emphasis added).

27 The CPUC has tried on its own to identify the myriad laws and regulations PG&E seeks to preempt, and the list is long. However, the CPUC and others should not be required to engage in a guessing game. As the party seeking the relief, PG&E should be required to clearly identify each law it hopes to preempt.

D. The Disclosure Statement Fails to Disclose Adequately (a) the Values of the Assets it Seeks to Transfer, (b) the Consideration to be Received in Exchange, and (c) the Identities of the Transferees.[28]

PG&E should disclose the (a) market values of the assets it seeks to transfer to each of ETrans, GTrans and Gen (and their respective subsidiaries and affiliates), (b) the precise consideration to be received by the Reorganized Debtor in exchange therefor, and (c) the identities of the transferees. Presently the Plan and Disclosure Statement provide only as follows:

> (a) PG&E's electric transmission assets will be transferred to ETrans (or one or more subsidiaries or affiliates of ETrans) in partial consideration of $770 million in cash (subject to adjustment), $380 million in long-term notes and the assumption of certain (unspecified) liabilities;
>
> (b) PG&E's gas transmission and storage assets will be transferred to GTrans (or one or more subsidiaries or affiliates of GTrans) in partial consideration of $390 million in cash (subject to adjustment), $420 million in long-term notes and the assumption of certain (unspecified) liabilities; and
>
> (c) PG&E's generation assets will be transferred to Gen (or one or more subsidiaries or affiliates of Gen) in partial consideration of $200 million in cash (subject to adjustment), $1.9 billion in long-term notes and the assumption of certain (unspecified) liabilities.

D.S. at 71, 75, 78.

PG&E's disclosure in this area is woefully inadequate. First, PG&E fails to disclose the market values of the assets to be transferred. A comparison of the market values and the consideration to be paid for such assets is necessary so that PG&E's creditors can make informed decisions about whether such transfers are fair and reasonable or, alternatively, whether they reflect sweetheart deals between PG&E and its Parent. For example, how can PG&E justify the transfer of its generation assets to Gen for only $2.1 billion in cash, notes and the assumption of certain (unspecified) liabilities when PG&E itself recently valued its hydroelectric assets alone at approximately $4.1 billion in proceedings before the CPUC to determine whether the rate freeze has ended? In other words, if PG&E believes that its generation assets are worth in excess of

[28] Schedules identifying the precise assets to be transferred should be annexed to the Disclosure Statement.

$4.1 billion, then why is it willing to transfer them to its Parent for only $2.1 billion? PG&E should be required to explain this and any other discrepancies in the values of the assets to be transferred and the consideration to be received in exchange therefor.

In addition, PG&E should have to disclose the precise consideration to be paid for such assets. It cannot suffice for PG&E to disclose only the "partial consideration" to be received or that the cash portion of the consideration remains "subject to adjustment" or the assumed liabilities unspecified. Rather, PG&E must disclose all of the consideration to be received and specify, at a minimum, the reasons for any adjustments to the cash portion of the consideration. As for the assumed liabilities, PG&E knows what they are and should be forced to disclose them. *See, e.g.*, D.S. at 73, 79 (noting that the FERC must approve ETrans' and Gen's assumption of liabilities; PG&E anticipates making its FERC filings on or before November 30, 2001).

Finally, PG&E should disclose the identities of the entities to whom such assets will be transferred. PG&E recently filed notices with the CPUC of its intent to form a number of Parent subsidiaries and affiliates in anticipation of implementing its Plan. The names of these entities along with descriptions of the assets to be transferred to each should be included in the Disclosure Statement. It is not sufficient for the Disclosure Statement merely to recite that "[t]he Debtor *may* also create indirect subsidiaries or affiliates to hold other assets." *See* D.S. at 5 (emphasis added).

E. <u>Litigation.</u>

Section VI(H) of the Disclosure Statement, captioned "Litigation," describes certain claims PG&E's estate has against third parties,[29] as well as certain claims asserted against PG&E. D.S. at 87-91. Lacking, however, are any objective assessments of such claims, including (i) PG&E's claims in the Rate Recovery Litigation[30], the BFM Contract Seizure

[29] Excluding, notably, potential claims against the Parent and generators and other power sellers. *See* pp. 17-19, *supra*.

[30] At a minimum, PG&E should disclose that the CPUC has moved to dismiss PG&E's complaint in that case.

Litigation, and the appeal of this Court's Order dismissing PG&E's complaint in its adversary proceeding against the CPUC and its Commissioners, all of which PG&E believes are significant estate assets, and (ii) the claims asserted against PG&E in the Compressor Station Chromium Litigation. Also lacking is any explanation of why PG&E's Plan provides for the assignment of virtually the entire recovery (if any) in each such case, as well as its claims against the State, to Newco or its subsidiary.[31] These assignments are particularly troubling given that it is PG&E or the Reorganized Debtor, not the Parent or Newco, that will continue funding such lawsuits. PG&E needs to explain these transfers and to justify them, if possible.

A further issue is PG&E's description of its adversary proceeding against the CPUC and its Commissioners. *See* D.S. at 52, 62. In its description, PG&E never discloses that its adversary complaint was dismissed *with prejudice*. Nor does it disclose this Court's reluctance to solve California's or PG&E's energy crisis (a disclosure that is particularly relevant in light of the sweeping relief PG&E seeks under its Plan). *See* p. 20, *supra*. Further, on page 62 of the Disclosure Statement, PG&E mistakenly represents that its adversary complaint was filed "in accordance with the automatic stay provision of the Bankruptcy Code . . . ." Clearly, this Court decided otherwise. PG&E should be compelled to clarify and correct each of these items.

F. <u>Corporate Governance</u>.

The Disclosure Statement fails to identify the members of the boards of directors or control (as applicable) or the senior management of each of ETrans, Gtrans, Gen and the Reorganized Debtor. D.S. at 72, 75, 78, 83. These disclosures are required by law and, in any event, are a prerequisite to plan confirmation.[32] Their importance is particularly significant

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[31] *See, e.g.*, D.S. at 88 (noting that PG&E will assign to Newco or its subsidiary "the rights to 95% of the of the net after-tax proceeds from any successful resolution of the Rate Recovery Litigation and resulting CPUC rate order requiring collection in rates."); D.S. at 91 (noting similar assignments of recoveries from the BFM Contract Seizure Litigation and from claims against the CPUC and the State regarding PG&E's transition cost recovery).

[32] *See* 11 U.S.C. § 1129(a)(5), providing that:

> (a) The court shall confirm a plan only if all of the following requirements are met:

where, as here, there is the potential for interlocking directorates and sharing of management roles and responsibilities, which give rise to obvious conflict-of-interest concerns. Therefore, PG&E should be required to include this information in its Disclosure Statement.

G. **Executory Contracts and Unexpired Leases.**

PG&E's Disclosure Statement should list and briefly describe each significant executory contract and unexpired lease that it anticipates assuming, assuming and assigning to a third party (including such third party's identity), or rejecting. The cure amount for each such contract or lease to be assumed, or assumed and assigned, should similarly be disclosed. Finally, PG&E should update Section V(14) of the Disclosure Statement to reflect this Court's grant or denial, as the case may be, of any further requested extensions of the time within which PG&E may assume or reject its unexpired real property leases. D.S. at 63 (reflects extension only through October 5, 2001).

H. **Asset Sales.**

PG&E's Disclosure Statement provides that "[c]ertain other assets of the Debtor deemed not essential to operations will be sold under the Plan." D.S. at 65 (providing that PG&E expects to yield approximately $75 million from the sale of certain land parcels and property rights it deems nonessential). PG&E should specifically identify the assets to be sold and their approximate values.

> (5)(A)(i) The proponent of the plan has disclosed the identity and affiliations of any individual proposed to serve, after confirmation of the plan, as a director, officer, or voting trustee of the debtor, an affiliate of the debtor participating in a joint plan with the debtor, or a successor to the debtor under the plan; and (ii) the appointment to, or continuance in, such office of such individual, is consistent with the interests of creditors and equity security holders and with public policy; and
>
> (B) the proponent of the plan has disclosed the identity of any insider that will be employed or retained by the reorganized debtor, and the nature of any compensation for such insider.

11 U.S.C. § 1129(a)(5).

I. **Other items.**

(i) **Certain allocations among ETrans, GTrans, Gen and the Reorganized Debtor**

No basis exists, nor is one offered, for the following allocations among ETrans, GTrans, Gen and the Reorganized Debtor:

- The long-term notes to be issued under the Plan by each of ETrans (12%), GTrans (15%) and Gen (73%). D.S. at 14 n.1.

- The long-term subordinated notes to be issued to holders of QUIDS Claims (Class 11) by each of ETrans (27.5%), GTrans (19.8%) and Gen (52.7%). D.S. at 22.

- The Reorganized Debtor remaining solely liable on the Mortgage Backed PC Bond Claims (Class 4a), the MBIA Insured PC Bond Claims (Class 4b), the MBIA Claims (Class 4c), the Prior Bond Claims (Class 4f), and the Treasury PC Bond Claims (Class 4g). D.S. at 15-19. This is especially puzzling given that many of the assets securing such claims are to be transferred to ETrans, GTrans and Gen.

- Liability for the Letter of Credit Backed PC Bond Claims (Class 4d) and the Letter of Credit Bank Claims (Class 4e) being shared among the Reorganized Debtor (26%), ETrans (17%), GTrans (14%) and Gen (43%), respectively. D.S. at 16-18.

- Liability for the Allowed Chromium Litigation Claims for Actual Damages (Class 9a) and Punitive Damages (Class 9b) being shared among the Reorganized Debtor (50%), ETrans (12.5%), GTrans (12.5%) and Gen 25%. D.S. at 20-21.

PG&E should be required to explain and to justify each such allocation, if possible.

(ii) **Estimate of PX, ISO and Generator Claims (Class 6)**

PG&E fails to substantiate its $1.060 billion estimate of the PX, ISO and Generator Claims (Class 6)[33] despite its admission that the filed claim amounts are substantially higher. PG&E should explain the variance between the filed and estimated claim amounts and disclose whether its Plan can be consummated if the actual claim amounts exceed PG&E's estimate.

[33] PG&E represents that this amount also includes an estimate of the allowable ESP Claims. D.S. at 19 n. 4. This is perplexing given that the ESP Claims are separately classified in Class 7 and are estimated to equal $4.204 billion. *Id.*

(iii) **The Plan Supplement**

PG&E's Plan Supplement should be on file with the Court and made available to interested parties at or prior to the time that its Disclosure Statement is disseminated.[34] According to the Disclosure Statement, the Plan Supplement will contain, among others things, material agreements to be entered into between the Reorganized Debtor and each of ETrans, GTrans and Gen.[35] Inasmuch as these agreements will largely govern the relations among these entities subsequent to PG&E's reorganization, their terms should be disclosed up front so they may inform decisions to accept or reject the Plan.

(iv) **Employee Issues**

PG&E should be required to identify the individuals to be employed by each of the Reorganized Debtor, ETrans, GTrans and Gen. In addition, PG&E should disclose each entity's additional employee-related costs resulting from, among other things, (i) the renegotiation of various collective bargaining agreements with PG&E's employees, D.S. at 95, (ii) the need for new hires as a result of the Internal Restructurings (*e.g.*, whereas one person could operate and maintain certain transmission and distribution assets, two may become necessary if ownershi those assets no longer is shared), and (iii) the increased cost of the Reorganized Debtor's workers' compensation insurance given that the Parent will no longer guarantee payment of such claims.[36] D.S. at 96. Finally, PG&E should quantify the cost to ETrans, GTrans and Gen and

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[34] Presently, the Disclosure Statement provides only that the Plan Supplement will be filed at least ten days prior to the voting deadline. D.S. at 129.

[35] These include, without limitation, the Power Sales Agreement to be entered into between the Reorganized Debtor and Gen, the gas transmission and storage agreement to be entered into between the Reorganized Debtor and GTrans, and the master separation and distribution agreement to be entered into among the Reorganized Debtor, ETrans, GTrans and Gen. D.S. at 85-86, 92-93.

[36] On a related issue, PG&E should explain the statement on page 120 of the Disclosure Statement that all workers' compensation programs are to be treated as executory contracts and assumed under the Plan. PG&E's Plan provides for drastic changes to its workers' compensation program as a result of the Internal Restructurings. It is unclear just how PG&E can assume such programs *cum onore,* as it is required to under section 365 of the Bankruptcy Code, in light of such expected changes.

the impact upon its reorganization if this Court holds that the CPUC's affiliate transaction rules apply.[37]

(v) **Claims Resolution**

PG&E should disclose where it is in the claims allowance process and, assuming it obtains all of the preemptive and other relief it seeks in connection with its Plan, when creditors might expect distributions on their allowed claims.

(vi) **$40 million "Placement Fee"**

PG&E's Plan provides that, in addition to being paid in full with interest, holders of allowed claims in Classes 5 (Unsecured Claims), 6 (ISO, PX and Generator Claims), 7 (ESP Claims) and 9 (Chromium Litigation Claims for Actual Damages) will each receive its *pro rata* share of a $40 million "placement fee." D.S. at 19-21. It is unclear from the Plan what that placement fee represents and whether it is part of the consideration to be paid to holders of allowed claims in those classes on account of such claims. If the placement fee constitutes an additional distribution on such allowed claims, then PG&E's Plan may be unconfirmable in that it unfairly discriminates in favor of creditors in those classes and provides them with greater than a full recovery on their allowed claims. Alternatively, if the placement fee is something else, PG&E should state what it is and under what circumstances and why it is to be paid.

(vii) **DWR's Revenue Requirement**

The Disclosure Statement's discussion of DWR's revenue requirement and the CPUC's proceedings and PG&E's and others' challenges relating thereto is inaccurate, stale and in need of updating. PG&E's description has been superseded in many key respects by intervening events since the filing of its Disclosure Statement.

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[37] The CPUC's affiliate transaction rules require that a utility be compensated whenever a utility-employee is transferred to an affiliate. In the past, the CPUC has determined that a utility should be paid 25% of the worker's annual compensation.

(viii) **Gen as a "Public Utility"**

At page 151 of its Disclosure Statement, PG&E states that it will seek an affirmative ruling of this Court that Gen's facilities will not be dedicated to the public and, thus, that Gen is not a "public utility" within the meaning of the California Public Utilities Code. Elsewhere in its Disclosure Statement, however, PG&E freely admits that Gen is indeed a "public utility." D.S. at 73, 80 (noting that the Parent will own two public utilities – ETrans and Gen). Which is it?

(ix) **Hunters Point and Humboldt Bay Power Plants**

PG&E fails to explain why the Hunters Point and Humboldt Bay Power Plants will remain with the Reorganized Debtor and not be transferred along with PG&E's other generation assets to Gen. Is the Parent seeking to saddle the Reorganized Debtor with the decommissioning responsibilities associated with these power plants?

(x) **Mortgage Backed PC Bond Claims, MBIA Insured PC Bond Claims and Treasury PC Bond Claims**

As noted above, the Plan provides that the Reorganized Debtor will remain solely liable for payment of PG&E's Mortgage Backed PC Bond Claims, MBIA Insured PC Bond Claims and Treasury PC Bond Claims (Classes 4a, 4b and 4g, respectively). Yet, certain of the obligations under the loan documents covering such claims contain covenants that require ETrans', GTrans' and Gen's compliance (as applicable). *See e.g.*, D.S. at 102-103, 110-111.[38] If ETrans, GTrans

[38] Those portions of the Disclosure Statement provide as follows:

> With respect to any property transferred by the Debtor to ETrans, GTrans or Gen pursuant to the terms of the Plan, the acquisition or construction of which was financed or refinaned with the proceeds of a series of Mortgage Backed PC Bonds [, MBIA Insured PC Bonds or Treasury PC Bonds, as the case may be], the transferee shall assume the obligation to perform, satisfy and/or comply with those terms, covenants, conditions or obligations under the related PC Bond Documents arising from and after the Effective Date which are to be observed, performed, satisfied or complied with by the owner or operator of the "Project" (as described therein) or any portion thereof which is then owned or controlled by such party, including, without limitation, (a) any obligation to maintain such Project or portion thereof and its other assets and to timely pay any taxes, governmental charges, assessments, insurance premiums or other costs or expenses related thereto, (b) the obligation to comply

and/or Gen fail to comply with these covenants, then any resulting liability will be borne solely by the Reorganized Debtor, despite the fact that the Reorganized Debtor cannot compel their compliance. This risk should be disclosed.

(xi) <u>Resumption of the Net Short</u>

PG&E's self-imposed criteria for the Reorganized Debtor's resumption of the net short are at best unclear and confusing. *See, e.g.*, D.S. at 66 (setting forth the criteria). For example, PG&E fails to disclose the party responsible for establishing the objective retail rate recovery mechanism or the objective procurement standards. Will it be this Court, the CPUC, the Reorganized Debtor or some other body or entity? Equally unclear, is what PG&E means when it says that the Reorganized Debtor will assume the net open position "not already provided through the DWR's contracts . . . ." *Id.* Currently, DWR covers the entire net short, much of it through contracts it has with power suppliers. Under PG&E's formulation, what does PG&E forecast would remain for the Reorganized Debtor to cover? The Disclosure Statement needs to provide answers to these questions.

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with all restrictions on the use of such Project or portion thereof set forth in the related PC Bond Documents, and (c) the obligation to refrain from taking any action or permitting any action to be taken with respect to such Project or portion thereof that could cause interest on the related series of PC Bonds to become includable in the gross income of the holders thereof for federal income tax purposes.

(xii) **Separate Classification of the Environmental and Tort Claims for Actual and Punitive Damages (Classes 8a and 8b, respectively) and the Chromium Litigation Claims <u>for Actual and Punitive Damages (Classes 9a and 9b, respectively)</u>**

PG&E offers no justification for the separate classification and treatment of the Environmental and Tort Claims for Actual and Punitive Damages (Classes 8a and 8b, respectively), on the one hand, and the Chromium Litigation Claims for Actual and Punitive Damages (Classes 9a and 9b, respectively), on the other.

(xiii) **<u>Tax Consequences</u>**

According to PG&E's Disclosure Statement, the Proponents will seek a private letter ruling from the IRS or, alternatively, a legal opinion from their tax advisors, stating that the Internal Restructurings and the Reorganized Debtors Spin-Off will not be taxable events. D.S. at 163-64. PG&E admits, however, that any resulting tax liability could be substantial. *Id.* at 164. PG&E should estimate the amount of such potential tax liability and describe its potential impact on PG&E's proposed reorganization.

CONCLUSION

For the reasons set forth herein, the CPUC respectfully requests that this Court refuse to approve PG&E's Disclosure Statement.

DATED: November 27, 2001

Respectfully submitted,

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-and-

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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA
SAN FRANCISCO DIVISION

In re PACIFIC GAS AND ELECTRIC COMPANY, a California corporation, Debtor. Federal I.D. No. 94-0742640	Case No. 01-30923 DM Chapter 11 Case **OBJECTION TO PACIFIC GAS & ELECTRIC COMPANY'S SECOND MOTION FOR ORDER FURTHER EXTENDING EXCLUSIVITY PERIOD FOR FILING PLAN OF REORGANIZATION TO PERMIT THE CALIFORNIA PUBLIC UTILITIES COMMISSION TO FILE AN ALTERNATE PLAN OF REORGANIZATION** Date: January 16, 2002 Time: 9:30 a.m. Place: 235 Pine Street, 22nd Floor, San Francisco, California Judge: Hon. Dennis Montali

[SUPPORTING DECLARATION OF GARY M. COHEN FILED SEPARATELY]

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LEGISLATIVE HISTORY

The California Public Utilities Commission (the "Commission"), a creditor and party in interest in this chapter 11 case, by and through its undersigned counsel, submits this objection (the "Objection") to Pacific Gas & Electric Company's Second Motion for Order Further Extending Exclusivity Period for Filing Plan of Reorganization (the "Second Extension Motion") to permit the Commission to file its alternative plan of reorganization (the "Alternate Plan"). In support of its Objection, the Commission respectfully represents as follows:

I.

PRELIMINARY STATEMENT

Plan exclusivity extensions must be earned by hard bargaining. That is the clear purpose and intent of section 1121(d) of the Bankruptcy Code, which balances the estate's interest in promoting a consensual reorganization plan with the debtor's urge to use its exclusive right tactically to compel creditors and other interested parties to accede to its view of the world. It is that very tension that is at issue in the Second Extension Motion filed by Pacific Gas & Electric Company ("PG&E").

PG&E has enjoyed the exclusive right to file a plan of reorganization for more than nine months, since April 6, 2001. During that period, PG&E has not even attempted to negotiate with the Commission, its chief regulator. Instead, PG&E has initiated a frontal assault on the Commission's and the State's regulatory authority. From the first days of this case, when PG&E filed an adversary proceeding to strike a portion of a Commission order, to its plan filing some five months later, PG&E's strategy has been obvious – it prefers to fight, rather than reach agreement, with the Commission.

Its confirmation efforts complicated by its own belligerence, PG&E seeks an additional four month extension of its exclusive period, until June 30, 2002, to seek confirmation of its plan. PG&E has not earned such an extension. PG&E has enjoyed nine months of exclusivity and the time has now come to level the playing field. PG&E's creditors and other interested parties no longer should be held hostage to PG&E's battle plans against the Commission. In addition, a further extension of exclusivity would unjustifiably reward PG&E for pursuing precisely the type of "take-it-or-leave-it" attitude section 1121(d) of the Bankruptcy Code is designed to prevent.

As described more fully in the Declaration of Gary M. Cohen filed in support hereof (the "Cohen Declaration"), the Commission has developed an alternate approach, and this Court should deny PG&E's Second Extension Motion to the extent necessary to permit the Commission to file and solicit acceptances to its Alternate Plan. Such an approach is fully justified. To begin with, PG&E has failed to meet its burden of establishing "cause" for its second exclusivity extension, as it is required to do under section 1121(d) of the Bankruptcy Code. In fact, PG&E's Second Extension Motion does not contain *any* evidence of "cause." Rather, the Motion contains only unsupported allegations of alleged progress toward confirmation of a plan and the size and complexity of this case. PG&E's Sec. Ext. Mot. at 7-9. That, without more, is insufficient to satisfy the "cause" requirement.

The truth is, PG&E has made little, if any, progress toward confirmation of a *consensual* plan. As is obvious from the roughly 70 Disclosure Statement objections filed to date, the Plan does not enjoy the support of key constituencies in this case, including the Commission and the State of California, and PG&E has done nothing to gain their support. Moreover, as those objections point out, the Plan is infirm in a number of respects, leaving its confirmability in doubt. Allowing PG&E to proceed with its current Plan to the exclusion of all others may result in nothing more than wasted time and delay at the expense of PG&E's creditors who, in PG&E's own words, are footing the bill for "literally millions of dollars per week in fees, costs and interest accruals with respect to creditor claims." PG&E's Sec. Ext. Mot. at 4.

Similarly, the size and alleged complexity of this case do not support PG&E's second requested extension. While this case is no doubt large, its size is largely irrelevant to PG&E's need to maintain plan exclusivity. Size is important, where, unlike here, the existence of multiple creditor constituencies with varying rights and priorities magnify the difficulty of negotiating a consensual plan. Here, PG&E purportedly is offering to pay creditors in full.

Regardless of the number of constituencies involved, it should not be difficult for PG&E to convince creditors to take 100 cents-on-the-dollar. In short, size really does not matter.

PG&E's assertions of complexity are similarly unavailing. Much of the complexity surrounding this case has been engineered by PG&E. If PG&E were concerned only with debtor-creditor issues and emerging quickly from bankruptcy, more mundane alternatives exist for it to do so. In fact, the Commission has developed one such alternative, which is described below and in the Cohen Declaration. But, PG&E obviously is more interested in walking a legal minefield in an effort to remove itself from Commission and State regulation. Thus, PG&E itself has unnecessarily complicated matters by foisting upon creditors and this Court its complicated preemption battle. PG&E should not be allowed to create complexity where none needs to exist and then use it as a basis to monopolize the plan process.

"Cause" lacking, PG&E should not be granted a further extension of its exclusive period. Rather, this Court should deny PG&E's requested extension to allow the Commission to file and solicit acceptances to its own Alternate Plan. The Commission is keenly interested in PG&E's reorganization and has worked diligently to construct its Alternate Plan. The Commission is now poised, with this Court's permission, to present creditors and this Court with an alternative that, among other things, pays creditors in full in cash in a manner that is consistent with the broader interests of the State of California and PG&E's ratepayers, allows PG&E to emerge promptly from chapter 11 as a viable, creditworthy utility and avoids the costly preemption litigation at the heart of PG&E's Plan. Whereas creditors currently are stranded by PG&E's "take-it-or-leave-it" approach, they would now have a choice.

Accordingly, as discussed more fully below, the Commission requests that PG&E's Second Extension Motion be denied to permit the Commission to file its Alternate Plan.

II.

BACKGROUND

1. On April 6, 2001 (the "Petition Date"), PG&E filed a voluntary petition under chapter 11 of title 11 of the United States Code, 11 U.S.C. §§ 101 *et seq.* (the "Bankruptcy

Code"). PG&E continues to manage and operate its business and property as a debtor in possession pursuant to sections 1107 and 1108 of the Bankruptcy Code. No trustee has been appointed in this case.

2. The Commission is an independent, Constitutional agency of the State of California charged with, among other things, regulating California's public utilities. Cohen Decl. ¶ 2. PG&E is a public utility subject to the Commission's jurisdiction. *Id.* The Commission is also a creditor of PG&E and a party in interest in this case with standing to file a plan of reorganization.[1]

3. On July 3, 2001, PG&E made its first request to extend exclusivity, which was granted by an order (the "Extension Order") of the Court dated July 20, 2001. Order Extending Exclusivity Period, *In re Pacific Gas & Elec. Co.*, No. 01-30923 DM (Bankr. N.D. Cal., July 20, 2001). PG&E's first request was premised principally upon the size and alleged complexity of its chapter 11 case and its need for additional time to develop a plan of reorganization. Debtor's Motion for Order Extending Exclusivity Period For Filing Plan of Reorganization at 7-8. The Extension Order granted PG&E an additional four months within which to file a plan, until December 6, 2001, and in the event that PG&E did file a plan by December 6, 2001, the Extension Order extended the period during which plan exclusivity was maintained under section 1121(c)(3) until February 4, 2002. Extension Order at 1.

4. On September 20, 2001, PG&E, together with its parent company, PG&E Corporation (the "Parent"), as co-proponent, filed a Plan of Reorganization under Chapter 11 of the Bankruptcy Code for Pacific Gas and Electric Company (as amended, the "Plan") together with a proposed disclosure statement (as amended, the "Disclosure Statement").

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1 On October 2, 2001, the Commission filed a proof of claim for approximately $12 million representing amounts due from PG&E for, among other things, unpaid fees and expenses under the California Environmental Quality Act and unpaid user fees and other amounts due under the Women/Minority/Disabled/Veteran Business Enterprise Program.

5. The Plan and Disclosure Statement were prepared and filed without any negotiation or substantive discussion with many of the key players involved in this case and in the regulation of PG&E's operations, including the Commission. Cohen Decl. ¶ 8.

6. As this Court is keenly aware, the Plan is premised, in large part, upon PG&E's wholesale transfer of its generation and its electric and gas transmission assets to newly formed entities that would be beyond the purview of Commission regulation. First Am. Plan, Art. 7. In addition, the Plan hinges on PG&E's receipt of no fewer than fifteen affirmative declaratory and injunctive rulings against the Commission and various other State and local agencies, and approvals from the Federal Energy Regulatory Commission ("FERC"), the Securities and Exchange Commission ("SEC") and the Nuclear Regulatory Commission ("NRC"), all of which will be the subject of significant litigation before this Court and elsewhere. First Am. Plan, Art. 7, 8; First Am. D.S. at 123, 200-01. Assuming PG&E is successful on all of these fronts, the Plan allegedly provides for creditor claims to be satisfied in full, with interest, in the form of either cash or a combination of cash and debt securities. First Am. Plan, Art. 4.

7. As set forth more fully in the Commission's Objection to PG&E's Disclosure Statement, filed on November 27, 2001 (the "Disclosure Statement Objection"), the Commission submits that PG&E's Plan, which attempts to preempt myriad Commission, State and local laws and regulations, is unlawful and incapable of being confirmed.

8. Specifically, the Commission and other parties have identified the following critical confirmation infirmities:

- The Plan may not comply with the Bankruptcy Code, as required by section 1129(a)(1), because it fails to contain adequate means for its implementation, a requirement under section 1123(a)(5) of the Bankruptcy Code. Discl. Stmt. Obj. 6-9.
- The Plan has not been proposed in good faith, as required by section 1129(a)(3), because it is inconsistent with the purposes and objectives of the Bankruptcy Code. *Id.* at 9-13.
- The Plan may provide for hidden rate increases without Commission approval, in violation of section 1129(a)(6) of the Bankruptcy Code. *Id.* at 14.
- The Plan may not be feasible, as required by section 1129(a)(11). The Plan is predicated entirely upon PG&E's receipt of favorable rulings on many of its

requests for declaratory and injunctive relief relating to preemption, as well as favorable outcomes at the FERC, SEC and NRC. Until PG&E obtains such rulings, a feasibility determination is impossible. *Id.* at 14-15.

- The Plan fails the "best interests" test of section 1129(a)(7) of the Bankruptcy Code because it seeks to transfer proceeds of the Rate Recovery Litigation (as defined in the Plan) and other litigation to the Parent. *See* Objection of Certain Debtholders to Approval of the Disclosure Statement for Plan of Reorganization of Pacific Gas and Electric Company and PG&E Corp. at 10-14.
- The Plan improperly grants third party releases to the Parent and other creditors. *Id.* at 14-15.
- The Plan fails to comply with the "absolute priority rule" under section 1129(b)(2) of the Bankruptcy Code because it (a) allows equity holders to retain their ownership interest in PG&E when senior creditors are not paid in full, and (b) provides that QUIDS claimants will receive property of PG&E when senior creditors have not been paid in full. *Id.* at 15-19.

9. Pursuant to this Court's Order dated December 5, 2001, PG&E filed its amended Plan and Disclosure Statement on December 19, 2001. Hearings to consider approval of the amended Disclosure Statement are scheduled for January 14, 2002, to address the adequacy of disclosure only, and January 25, 2002, to address whether PG&E's Plan is unconfirmable as a matter of law based upon sovereign immunity or preemption grounds.

10. Pursuant to this Court's December 5th Order, on December 18, 2001, the Commission and its counsel met with PG&E and its counsel and counsel to the Parent to discuss the Commission's objections to the Disclosure Statement. Cohen Decl. ¶ 8. As of the date of this Objection, many of the Commission's objections to the Disclosure Statement remain unaddressed by the amended Disclosure Statement, although the Commission and PG&E have scheduled a further "meet and confer" for January 9, 2001. *Id.* at ¶ 6.

11. On December 19, 2001, PG&E filed its Second Extension Motion.

III.

COMMISSION'S ALTERNATE PLAN[2]

Faced with PG&E's refusal to negotiate, the Commission has developed its Alternate Plan. Now, with PG&E's exclusive right about to expire (absent an extension), the Commission

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[2] The following description of the Alternate Plan is for informational purposes and is included only as support for this Objection. By this Objection, the Commission is not proposing an alternative plan nor is it soliciting acceptances to any such alternative or rejections of PG&E's Plan.

is prepared to describe the salient features of its Alternate Plan and, with this Court's permission, to file a plan and disclosure statement in short order.

The following are certain of the significant provisions of the Commission's Alternate Plan:

- PG&E's short-term borrowings incurred during the energy crisis would be paid in full in cash (including accrued and unpaid interest through the effective date) by the first quarter of 2003 through a combination of PG&E's cash on hand (approximately $4.9 billion as of November 30, 2001 according to PG&E's most recent 8-K filing with the SEC)[3] and PG&E's residual revenues after deducting authorized revenue requirements from billed revenues ("residual revenues");
- all of PG&E's remaining indebtedness would be reinstated or refinanced;
- PG&E's creditworthiness and financial viability would be restored – the Commission would adopt a post-bankruptcy rate structure consistent with state law that would provide PG&E with an opportunity to earn a reasonable return that would allow it to maintain an investment-grade credit rating;
- valuable claims against the Parent (which under PG&E's Plan are to be released)[4] and other assets such as PG&E's refund claims pending before FERC would be preserved and transferred to a litigation trust or similar entity and prosecuted for the benefit of PG&E's ratepayers;
- costly and time-consuming preemption litigation would be avoided;
- PG&E would emerge promptly from chapter 11;
- the Commission and State of California would continue to regulate PG&E's operations;
- PG&E's integrated operations would not be disaggregated;
- rates would not increase, and may be reduced in 2003 (or earlier);
- utility assets would not be diverted to pay the Parent's expenses; and
- costly litigation at the FERC, NRC and SEC would be avoided.

Cohen Decl. ¶ 9.

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3 The Commission expects this number to increase over time. Cohen Decl. ¶ 10.

4 These claims include, among others, claims that the Parent has violated the "first priority" condition imposed upon the Parent by a Commission order approving PG&E's holding company structure and claims that PG&E declared and paid dividends to its Parent while it was insolvent.

Mindful of the chaos that could ensue if PG&E's plan exclusivity were terminated generally to allow any party in interest to file a plan, the Commission's Objection is more limited. The Commission objects to PG&E's Second Extension solely to allow it to file and solicit acceptances to the Commission's Alternate Plan. For the reasons that follow, the Commission submits that such relief is required under section 1121(d) of the Bankruptcy Code and is in the best interests of PG&E's estate, its creditors and other parties in interests.

IV.

ARGUMENT

PG&E'S SECOND EXTENSION MOTION SHOULD BE DENIED FOR FAILURE TO SHOW "CAUSE" UNDER SECTION 1121(d) OF THE BANKRUPTCY CODE

The Court should deny PG&E's Second Extension Motion to the extent necessary to permit the Commission to file its Alternate Plan because PG&E has failed to meet its burden of establishing "cause" for an extension as required under section 1121(d) of the Bankruptcy Code. 11 U.S.C. § 1121(d)[5]; *In re Dow Corning Corp.*, 208 B.R. 661, 663 (Bankr. E.D. Mich. 1997) ("a debtor bears the burden of proof when it requests an extension of its period of exclusivity"); *In re Express One Int'l, Inc.*, 194 B.R. 98, 100 (Bankr. E.D. Tex. 1996) ("The debtor-in-possession bears the burden of establishing 'cause' for an extension of its exclusivity period."). Though the Bankruptcy Code does not define "cause," it is well established that "cause" is a flexible concept that provides courts with broad discretion in determining when it exists based upon the particular facts and circumstances of each case. *See In re Sharon Steel Corp.*, 78 B.R. 762, 763-64 (Bankr. W.D. Pa. 1987) ("In essence, Congress has left the meaning of the phrase 'for cause' to be determined by the facts and circumstances in each individual case."); *In re Public Serv. Co. of New Hampshire* ("*PSNH*"), 99 B.R. 155, 173 n.10 (Bankr. D.N.H. 1989) ("[I]f a debtor-in-possession is to retain exclusive control of the formulation of a plan of

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[5] Section 1121(d) provides that "[o]n request of a party in interest made within the respective periods specified in subsections (b) and (c) of this section and after notice and a hearing, the court may *for cause* reduce or increase the 120-day period or the 180-day period referred to in this section." 11 U.S.C. § 1121(d) (emphasis added).

reorganization under an exclusivity period it must demonstrate that it uses its position to effectively foster consensual agreement by all entities involved").

Critical to the determination of whether "cause" exists is consideration of the balance Congress intended to strike in section 1121 between the relative negotiating positions of the debtor and its creditors and other key constituents. Section 1121 is the product of Congress' attempt to remedy the imbalance between debtors and creditors found under chapter XI of the former Bankruptcy Act. Under chapter XI, debtors maintained the exclusive right to propose a plan <u>indefinitely</u>, thereby giving debtors undue leverage over creditors whose only recourse was to move for conversion of the case to chapter X, an unattractive alternative. In contrast, under section 1121 of the Bankruptcy Code, debtors enjoy exclusivity only for a limited period of time -- 120 days to file a plan and no more than 180 days from the inception of the case to seek its acceptance -- which may only be extended or reduced upon a showing of "cause." As the legislative history of section 1121(d) makes clear, extensions should not be used to upset the delicate balance Congress sought: "Since the debtor has an exclusive privilege for 6 months during which others may not file a plan, *the granted extension should be based on a showing of some promise of probable success. An extension should not be employed as a tactical device to put pressure on parties in interest to yield to a plan they consider unsatisfactory*." S. Rep. No. 95-989, at 118 (1978), *reprinted in* 1978 U.S.C.C.A.N. 5787, 5904. *See also In re Pine Run Trust, Inc.*, 67 B.R. 432, 434 (Bankr. E.D. Pa. 1986) ("By granting the debtor a limited period of exclusivity in plan filing, the Code seeks to balance the relative negotiating positions of the debtor and creditors."); *In re Washington –St. Tammany Elec. Coop., Inc.*, 97 B.R. 852, 855 (E.D. La. 1989) ("Congress enacted . . . 1121 in order to limit the debtor's exclusive rights to file a plan to clearly defined periods."); *United Savings Assoc. of Tx.* v. *Timbers of Inwood Forest Assocs., Ltd. (In re Timbers of Inwood Forest Assocs., Ltd.)*, 808 F.2d 363, 372 (5th Cir. 1987) ("[T]he bankruptcy court must avoid reinstituting the imbalance between the debtor and its creditors that characterized proceedings under the old Chapter XI.") (*en banc*), *aff'd*, 484 U.S. 365 (1988).

In balancing the relative positions of various constituencies, courts examine a variety of factors to determine whether "cause" for an extension exists. In one of the leading decisions in this area, the court in *PSNH* considered whether an extension was paid for with "hard bargaining," whether a further extension would promote a consensual plan of reorganization within a reasonable timeframe and whether chaos would ensue following the expiration of exclusivity. *PSNH,* 99 B.R. at 173-77. Other courts have considered multiple factors, many of which amount to variations on the same theme. *See, e.g., Express One Int'l,* 194 B.R. at 100; *Dow Corning*, 208 B.R. at 64-65.[6]

PG&E has not submitted any evidence that "cause" for an extension exists. Instead, its Second Extension Motion is premised solely upon boilerplate suggestions of "cause," including PG&E's alleged progress towards reorganization and the size and complexity of this case. The cited reasons are unsupportable. Even if true, though, they do not add up to "cause." Under such circumstances it is appropriate for the Court to deny PG&E's Second Extension Motion to the extent necessary to allow the Commission to file its Alternate Plan.

A. PG&E Has Not Made Substantial Progress Towards A Successful *Consensual* Reorganization Sufficient To Justify An Extension of Exclusivity.

The purpose of the exclusive period is to enable the debtor to negotiate a *consensual* plan of reorganization with its creditors. *See In re PSNH*, 99 B.R. at 173 n.10 ("if a debtor-in-possession is to retain exclusive control of the formulation of the plan of reorganization under an exclusivity period it must demonstrate that it uses its position to effectively foster consensual

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6 The *Express One* court considered the following factors: (1) size and complexity of the case; (2) necessity of sufficient time to permit the debtor to negotiate a plan of reorganization and prepare adequate information; (3) the existence of good faith progress toward reorganization; (4) the fact that the debtor is paying its bills as they become due; (5) whether the debtor has demonstrated reasonable prospects for filing a viable plan; (6) whether the debtor has made progress in negotiations with its creditors; (7) the amount of time which has elapsed in the case; (8) whether the debtor is seeking an extension of exclusivity to pressure creditors to submit to the debtor's reorganization demands; and (9) whether an unresolved contingency exists. *Express One Int'l,* 194 B.R. at 100. Courts that employ the factors analysis do not merely tally the factors for and against an extension but rather view them holistically. *See Dow Corning*, 208 B.R. at 659 ("Sometimes one or more factors strongly point to a particular result while others point the other way only weakly. And sometimes certain factors are just more relevant or important than others.").

agreement by *all entities involved*") (emphasis added). Accordingly, in evaluating whether cause exists for an extension, courts examine whether there is a "reasonable probability that . . . [the debtor] will be able to propose a plan that will result in a successful reorganization within a reasonable time." *In re Southwest Oil Co. of Jourdanton, Inc.*, 84 B.R. 448, 451 (Bankr. W.D. Tex. 1987); *see In re Pine Run Trust, Inc.*, 67 B.R. 432, 435 (Bankr. E.D. Pa. 1986) (justifying exclusivity extension on, among other things, a finding that "substantial progress has been made in negotiations that, all concede, are critical to a successful reorganization"). Even after a plan is filed, courts evaluate the status of negotiations between the debtor and key parties in interest towards achieving a consensual reorganization. *See generally PSNH*, 99 B.R. at 175-76 (denying debtor utility's second extension request where status of negotiations indicate that a further extension of exclusivity will not promote a consensual plan of reorganization within a reasonable time frame).

PG&E claims that it has made "substantial efforts towards a successful reorganization," citing that (i) it has already filed a Disclosure Statement and Plan which it claims enjoy broad creditor support, (ii) it is in the process of obtaining approval of its Disclosure Statement, and (iii) it has amended the Plan and Disclosure Statement to address concerns raised by interested parties. PG&E's Sec. Ext. Mot. at 9-10. PG&E's submissions in this respect are insufficient to establish cause. First, PG&E has failed to engage in the "hard bargaining" (indeed *any* bargaining) with several key constituencies, which is a necessary prerequisite to a grant of an extension of exclusivity. *PSNH*, 99 B.R. at 173. Second, until critical determinations are made regarding, among other things, the lawfulness of the preemption PG&E seeks under its Plan, its confirmability remains very much in doubt. Therefore, whatever progress PG&E has made to date may prove to be illusory and of no consequence to creditor recoveries and its eventual emergence from chapter 11.

(i) <u>PG&E Has Failed to Negotiate with the Commission and Other Key Parties in Interest.</u>

Extensions of exclusivity must be paid for by "hard bargaining." *Id.* (citing *In re Manville Forest Prods. Corp.*, 31 B.R. 991, 993 (S.D.N.Y. 1983)). As the government body charged with regulating most of PG&E's operations, the Commission is a critical player in this case. Yet, PG&E has not negotiated any terms of a plan with the Commission, preferring instead to embroil this chapter 11 estate in a risk-laden attack on the Commission's regulatory authority. Such failure to negotiate is fatal to PG&E's Second Extension Motion.

Faced with a similar circumstance of a regulated utility failing to negotiate the terms of its reorganization plan with its regulators, the court in *PSNH* refused to grant the debtor utility a further extension of exclusivity. In that case, the court denied the debtor's second request for an extension of exclusivity because instead of continuing to bargain with state representatives, the debtor filed a non-consensual "FERC plan" similar in some respects to PG&E's Plan. Specifically, in *PSNH* the court found that although representatives of the debtor, the state and key creditor and equity security holder constituencies met on more than one occasion and discussed and exchanged proposals, the debtor was uninterested in making real progress in its negotiations with the state toward a consensual plan of reorganization. *PSNH*, 99 B.R. at 174. Instead, the court found that much like PG&E here, the debtor utility preferred to "stiff arm" th state and go it alone in furtherance of its own agenda. *Id.* at 175. The court there was left only to conclude that after the debtor utility's "FERC plan" was filed, unless exclusivity was terminated and parties were permitted to file alternative plans, there was little likelihood that the debtor and the state would negotiate a consensual plan of reorganization. *Id.* at 176. As a result, the court denied the debtor utility's requested extension of plan exclusivity. *Id.* at 177.

Here, PG&E's behavior is even more egregious than that of *PSNH*. PG&E flat out has not negotiated at all with the Commission. Cohen Decl. ¶ 8. During the approximately nine months in which PG&E has enjoyed exclusivity it has not met with or phoned representatives of the Commission to discuss substantively its Plan. *Id.* The most PG&E has done is to provide one informational "briefing" to Commission staff on November 30, 2001, at which it described its filings with the FERC, SEC and NRC in furtherance of its Plan. There was no negotiation over the terms of the Plan at this briefing. *Id.* In addition, the Commission's counsel attended a court-ordered "meet and confer" session on December 18, 2001 to discuss the Commission's

Disclosure Statement Objection. *Id.* Another "meet and confer" is scheduled for January 9, 2002. *Id.* at ¶ 6.

PG&E's deliberate decision to exclude its chief regulator from the Plan process reflects PG&E's poor judgment and belligerence toward a significant constituency in this case. It also flies directly in the face of section 1121 and its accompanying legislative history, which evince a clear Congressional intent that favors a negotiated, consensual resolution of chapter 11 cases. PG&E's failure to negotiate with the Commission and the State constitutes conduct undeserving of a further extension of exclusivity. Given PG&E's recalcitrance, this Court, like the court in *PSNH*, should promote a consensual plan of reorganization by terminating exclusivity to allow the Commission to file its Alternate Plan. A contrary result would allow PG&E to reap the benefits afforded by plan exclusivity without paying the toll of hard bargaining. It would also allow PG&E to continue to kidnap the plan process to pursue its own deregulation goal, holding the Commission, the State and creditors hostage in the meantime.[7]

(ii) <u>It is Too Early to Determine Whether PG&E's Plan Can Result in a Successful Reorganization</u>.

PG&E claims that an extension of exclusivity is warranted because it has "made substantial efforts towards a successful reorganization." PG&E's Sec. Ext. Mot. at 9. PG&E then pins its requested extension on a line of cases as well as section 1121's legislative history which, as PG&E concedes, establish "that exclusivity period extensions are appropriate where the debtor displays some likelihood of a successful, *consensual* reorganization." *Id.* at 8 (emphasis added). PG&E's factual averments are misleading and the cases upon which it relies are factually inapposite.

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[7] PG&E's creditors are hostage to PG&E's "willful blindness" to plan alternatives. PG&E would have those voting on its Plan and this Court believe that its drastic "FERC plan" involving massive dislocations of Commission, state and local laws and regulations is the only plan capable of being confirmed, *i.e.*, that there are no alternatives. First Am. D.S. at 64-65. PG&E is wrong. If allowed to file its Alternate Plan, the Commission intends to show that a very simple alternative exists, one that pays creditors in full in cash by the first quarter of next year without the need for years of litigation. Creditors and other parties in interest should be given the chance to choose the alternative most attractive to them.

First, as detailed above, PG&E has made no effort during this case to build consensus with the Commission on a plan of reorganization. It strains credulity for PG&E to imply otherwise.

Second, despite having filed its Plan more than three months ago, PG&E has been unable to move it out of the starting blocks. As PG&E admits, "70 parties have filed objections to the Disclosure Statement, many of which also reflect opposition to the Plan." PG&E's Sec. Ext. Mot. at 3-4. PG&E further freely concedes that "in view of the sheer number and complexity of the issues involved, it may take months to fully resolve these matters and obtain confirmation of the Plan." *Id.* at 4. PG&E also recognizes that there are likely to be "dozens of contested issues with respect to confirmation of the Plan, many of which are likely to be quite time-consuming to resolve or adjudicate." *Id.* Much of the same can be said of PG&E's various proceedings at the FERC, NRC and SEC. In view of the foregoing, it is premature at best for PG&E to trumpet its efforts at making substantial progress towards a successful reorganization (certainly not a *consensual* reorganization). It may very likely be the case that PG&E's Plan has failed to advance the confirmation ball at all.

Finally, the cases cited by PG&E where courts have granted an extension based in part on a showing of progress towards reorganization are factually inapposite and do not support PG&E's Second Extension Motion. In many, no plan of reorganization had yet been filed, and it still appeared that extra time would afford the parties the opportunity to negotiate a consensual plan.[8] Others involved unique circumstances not present here.[9]

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[8] *See, e.g.*, *In re Pine Run Trust, Inc.*, 67 B.R. 432, 435 (Bankr. E.D. Pa. 1986) (no plan filed; granting first extension to allow debtors who run retirement community to continue negotiations with residents' committee where creditor-objector asked *not* to be included in such negotiations, and there was no evidence that debtor sought additional extension in order to pressure creditors to accede to reorganization demands); *In re Swatara Coal Co.*, 49 B.R. 898, 899-900 (Bankr. E.D. Pa. 1985) (no plan filed; justifying first extension on fact that debtor's owners did not acquire ownership and control of the debtor until nearly three months after case was filed and that pursuant to stipulation and order agreed to by debtor and objector-committee, debtor is required to negotiate with certain parties for a set period yet to expire); *In re McLean Indus., Inc.*, 87 B.R. 830, 833, 835 (Bankr. S.D.N.Y. 1987) (no plan filed; objector *agrees* with course of direction debtor is taking and complex issues relating to liquidation and estimation of certain claims and asset valuation need to be resolved or close to resolution before debtor can negotiate terms of plan, meaningful disclosure can be made t

In short, PG&E's mere filing of a Plan and Disclosure Statement that lacks the support of key constituencies and is legally infirm does not, without more, constitute the type of progress toward a successful reorganization that justifies a further extension of PG&E's exclusive period.

(iii) PG&E's Use of Exclusivity As a Tactical Device to Bully the Commission, the State and its Creditors to Accept its Plan Undermines its Requested Extension.

PG&E further argues that its "progress" towards reorganization justifies "cause" for an extension because "there is nothing to suggest that PG&E seeks the requested extensions in order to pressure its creditors to accede to its reorganization demands." PG&E's Sec. Ext. Mot. at 9. The Commission disagrees. As demonstrated below, PG&E's strategy for seeking a further extension of its exclusive period has at least two objectives: first, it allows PG&E to continue to prevent the Commission from having a meaningful, affirmative voice in its reorganization; and second, by silencing other voices, PG&E can pressure creditors into believing its own rhetoric that "[t]he Plan . . . is, in the Proponents' reasoned opinion, the *only* reasonable solution . . . ." First Am. D.S. at 64-65 (emphasis added). However, where, as here, a debtor seeks to employ exclusivity as a tactical device to force parties in interest to accede to its reorganization demands,

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creditors and creditors will be able to determine their distributions); *In re Gibson & Cushman Dredging Corp.*, 101 B.R. 405, 409-10 (E.D.N.Y. 1989) (no plan filed; debtor's attempts to negotiate with creditors' committee ongoing); *In re Trainer's, Inc.*, 17 B.R. 246, 247 (Bankr. E.D. Pa. 1982) (no plan filed; debtor making substantial efforts to sell main asset, a restaurant).

9 *In re Homestead Partners, Ltd.*, 197 B.R. 706, 719-20 (Bankr. N.D. Ga. 1996) ("new value" plan filed; court denies motion to terminate by undersecured lienholder on debtor's principal asset because need for competition can be satisfied by requirement that a competitive auction for new equity interest be held at confirmation and grants motion to extend because of lienholder's high degree of recalcitrance and presence of complex legal issues); *In re United Press Int'l, Inc.*, 60 B.R. 265, 271 n.12 (Bankr. D.C. 1986) (granting debtor's motion to extend exclusivity to allow debtor to *file* a plan where the court had previously modified exclusivity to allow creditors' committee and another creditor to file plans); *Gaines* v. *Perkins (In re Perkins)*, 71 B.R. 294, 295, 298 (W.D. Tenn. 1987) (affirming bankruptcy court's decision allowing extension to continue soliciting acceptances where lower court had found, among other things, that the debtor's plan had already received acceptances from all but a few creditors, the two bankruptcy judges in the district had to contend with approximately 14,000 pending cases between them and progress had been made with respect to creditors who had objected to plan); *In re Nicolet, Inc.*, 80 B.R. 733, 744 (Bankr. E.D. Pa. 1988) (decision on exclusivity scheduled for a later date).

courts uniformly hold that such a factor weighs heavily against a finding of "cause" to extend a debtor's plan exclusivity. *See, e.g., PSNH*, 88 B.R. 521, 537 (Bankr. D. N.H. 1988) (courts consider general balancing analysis "to avoid allowing the debtor to hold the creditors and other parties in interest 'hostage' so that the debtor can force its view of an appropriate plan upon the other parties"); *Teachers Ins. & Annuity Assoc. of Am.* v. *Lake in the Woods* (*In re Lake in the Woods*), 10 B.R. 338, 345-46 (E.D. Mich. 1981) (holding that "extensions are impermissible if they are for the purpose of allowing the debtor to prolong reorganization while pressuring a creditor to accede to its point of view on an issue in dispute").

Thus far, PG&E's actions amount to the very "take-it-or-leave-it" attitude Congress sought to prevent by replacing the Bankruptcy Act. *See In re Lake in the Woods*, 10 B.R. at 344 ("'The take-it-or-leave-it attitude on the part of debtors as permitted by Chapter XI is fraught with potential abuse. The granting of authority to creditors to propose plans of reorganization and rehabilitation serves to eliminate the potential harm and disadvantages to creditors [and] democratizes the reorganization process.'") (quoting Bankruptcy Act Revision, Serial No. 27, Part 3, Hearings on H.R. 31 and H.R. 32 before the Subcomm. on Civil and Constitutional Rights of the Comm. on the Judiciary, 94th Cong., 2d Sess. (March 29, 1976) (prepared statement of Harvey R. Miller, William J. Rochelle and J. Ronald Trost) 1875-76 (footnotes omitted)). PG&E's own words evidence that it has foreclosed consideration of all alternatives. *See* First Am. D.S. at 64-65. In so doing, it is forcing creditors to accept its own view of the world and, in the process, using exclusivity to freeze out the Commission and the State while it embarks upon a massive regulatory sea change. Terminating exclusivity now to allow the Commission to file its own Plan would free creditors from the vise PG&E currently has them in and allow the Commission to continue with its State-mandated mission to regulate California's public utilities.

B. <u>The Size and Complexity of PG&E's Chapter 11 Case Do Not Justify an Extension.</u>

Aside from its alleged "progress" toward a successful reorganization, PG&E's only other proffered justification for its requested extension is the often-cited (and overused) "size-and-complexity" excuse. Specifically, PG&E argues that because this case involves "tens of billions of dollars of assets, and claims of more than 13,000 creditors" its sheer size together with its exceeding complexity justify its requested extension. PG&E's Sec. Ext. Mot. 7-8. PG&E's argument in this regard elevates form over substance and ignores the fact that PG&E itself has engineered much of the cited complexity.

This is a very large case — of course it is. However, size and complexity do not necessarily go hand in hand. Here, for instance, where creditors likely will be paid in full, much of the complexity associated with having to negotiate with multiple creditor constituencies with different rights and priorities is nonexistent. After all, it should not be difficult to convince creditors to take 100 cents-on-the-dollar with interest. So while the sheer size of this case may present administrative difficulties, it does not support an extension of time ostensibly needed for the debtor to negotiate with its creditors.

Nor can PG&E hide behind the alleged "complexities" of this case in seeking to extend plan exclusivity. PG&E contends that this case "is exceedingly complex, based on, *inter alia*, PG&E's status as a utility company subject to a myriad of state and federal statutes, rules and regulations," many of which PG&E seeks to preempt through confirmation of its Plan. PG&E's Sec. Ext. Mot. at 2, 8.[10] Elsewhere in its Motion PG&E contends that "in view of the sheer number and complexity of the issues [raised in the objections to PG&E's Plan and Disclosure Statement] . . . it may take months to fully resolve these matters and obtain confirmation of the Plan." *Id.* at 4. Nowhere, however, does PG&E mention that it is responsible for much of the complained-of complexity. As evidenced by the Commission's Alternate Plan, alternatives exist to repay creditors in full and to have PG&E emerge from chapter 11. Indeed, the elegance of the Commission's Alternate Plan lies in its simplicity. But PG&E is not interested in simplicity, or primarily in creditor recoveries. Its interests lie elsewhere — in the massive dislocation of the

[10] PG&E further premises the complexity of this case on "the fact that PG&E continues to grapple with an unprecedented energy crisis." PG&E's Sec. Ext. Mo. at 8. PG&E's statement is an exaggeration. As the CPUC's Alternate Plan would very clearly show, PG&E's retail electric rates exceed its wholesale costs, and have since at least around June 2001, leaving PG&E with substantial "residual revenues." Cohen Decl. ¶ 10.

Commission and the State of California's laws and regulations governing its operations. The preemption fight PG&E has started is the cause of much of the complexity surrounding this case, and PG&E should not be permitted to exploit problems it creates.

Finally, size and complexity cannot, without more, constitute "cause" for an extension of exclusivity where other bases for cause are lacking. *See, e.g., In re Sharon Steel Corp.*, 78 B.R. 762, 766 (Bankr. W.D. Pa. 1987) (denying extension of exclusivity despite size and complexity of debtor); *PSNH,* 88 B.R. at 537 (size and complexity alone do not justify extension for cause); *In re Express One Int'l*, 194 B.R. at 100-01 (same). The *PSNH* court thoroughly addressed the circumstances under which size and complexity would justify an extension for "cause" in its decision on the debtor's first extension request:

> It seems clear from a review of the relevant authorities that size and complexity alone cannot suffice as "cause" for a continuation of a debtor's plan exclusivity right in a chapter 11 reorganization. If that were so, a debtor in a case such as the present would automatically have a right to plan exclusivity throughout the proceedings – contrary to the "balancing" and "tension" rationale underlying § 1121 as detailed above. It does stand to reason that a debtor in a large and complex case may make a showing of cause on those facts for exclusivity extension in the *initial stages* of the reorganization by virtue of that factor . . . . If size and complexity *alone* were sufficient cause, that interpretation of the statutory standard would in effect eat up the rule.
>
> The court concludes that an appropriate interpretation of the "for cause" language of § 1121(d) would provide that the size and complexity must be accompanied by other factors pertinent to the particular debtor and its reorganization to justify extension of plan exclusivity, except perhaps in the very early, initial stages of the chapter 11 proceeding. Such factors include those developed in the cases, *i.e.*, <u>the likelihood of an imminent consensual plan if the debtor retains control, no alternate substantial plan being held off by debtor exclusivity, and the general balancing analysis to avoid allowing the debtor to hold the creditors and other parties in interest "hostage" so that the debtor can force its view of an appropriate plan upon the other parties</u>.[11]

[11] In this first *PSNH* decision on exclusivity, an extension was granted principally because the court saw a seven-month "window of opportunity" within which the parties could negotiate towards a consensual plan. 88 B.R. at 538.

PSNH, 88 B.R. at 537 (citations omitted) (underlined emphasis supplied).

Applying this rationale here, size and complexity alone simply do not justify a further extension for PG&E. First, PG&E has already enjoyed one extension, premised at least in part on the size and complexity of its case; granting PG&E another would lead to the very rule-swallowing cautioned against by the court in *PSNH*. Second, confirmation of PG&E's Plan is neither imminent, nor likely to be consensual. Third, here, exclusivity *would* prevent the filing of an "alternate substantial plan," the Commission's Alternate Plan. Finally, as argued above, it appears that the only benefit an extension would offer PG&E would be an opportunity to further cram its views of an appropriate Plan down the throats of creditors, the Commission and other parties in interest that are currently held hostage by PG&E's exclusivity. Under these circumstances, an extension should not rest on "size and complexity."[12]

C. Denying PG&E's Motion to Allow the Commission to File its Alternate Plan Would Benefit Interested Parties Without Prejudicing PG&E.

Terminating PG&E's Plan exclusivity to allow the Commission to file and solicit acceptances to its Alternate Plan is in the best interests of PG&E's creditors and its estate and would not prejudice PG&E. Presently, creditors have only one choice — PG&E's Plan. Their options are to either accept PG&E's Plan and endure years of litigation and uncertainty while they continue to finance, in PG&E's words "literally millions of dollars per week in fees, costs and interest accruals" (PG&E's Sec. Ext. Mot. 4), or to reject PG&E's Plan in the face of no known alternatives. Neither option may be particularly appealing. Fortunately, a third option exists — the Commission's Alternate Plan. As detailed elsewhere, it provides for creditors to be

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12 The cases relied upon by PG&E do not suggest otherwise; in each there existed some independent basis for cause other than size and complexity. *See, e.g.*, *In re Dow Corning*, 80 B.R. at 668 (debtor willing to discuss other means of reorganizing); *In re Express One*, 194 B.R. 100-01 (size and complexity only appropriate consideration where, among other things, no alternative plan); *PSNH*, 88 B.R. at 538 (extension premised principally on "window of opportunity" to negotiate, not size and complexity of debtor); *In re Texaco*, 76 B.R. 322 (plan product of settlement between primary adversaries; plan proposed by party seeking termination is substantially similar, the only changes affecting corporate governance); *In re Perkins*, 71 B.R. at 295 (plan had "overwhelming" creditor support; most acceptances already solicited); *In re Pine Run Trust*, 67 B.R. at 435 (court found that "traditional ground" of large size not established); *In re United Press Int'l*, 60 B.R. at 271 n.12 (modifications of exclusivity already granted to certain parties).

paid in full in cash by no later than the first quarter of 2003 and avoids the unnecessary and costly legal battle to preempt a century of state laws and regulations. In addition, it gives the Commission a voice in PG&E's restructuring, which to date it has been denied by PG&E. Creditors that are not interested in joining PG&E's preemption bandwagon should be given the option not to. Denying PG&E's Second Extension Motion to allow the Commission to file its Alternate Plan gives them that option.

Moreover, modifying PG&E's plan exclusivity to permit the Commission to file its Alternate Plan comes without cost to PG&E. PG&E may still pursue confirmation of its Plan should it choose to do so. In addition, notwithstanding PG&E's unsupported rhetoric to the contrary, the requested modification of PG&E's exclusive period would not "create needless confusion and conflicts that will presumably prejudice all parties." PG&E's Sec. Ext. Mot. at 4. This Objection is limited in that it seeks only to open up the plan process to the Commission's Alternate Plan — the Commission is not advocating that it be opened up generally to all parties in interest. Courts in similar situations have recognized that allowing competing plans may be efficient and can be used as an appropriate means of facilitating reorganization. *See In re Interco, Inc.*, 137 B.R. 999, 1001 (Bankr. E.D. Mo. 1992) (noting that "simultaneous consideration of competing plans may be an efficient procedure"); *PSNH,* 88 B.R. at 539 n.16 (rejecting an argument similar to PG&E's; "If taken literally, the debtor's position would mean that the debtor must have the sole power to present a plan, because multiple plans will bring chaos; therefore, the debtor's exclusivity period must be continued indefinitely."); *In re United Press Int'l*, 60 B.R. at 271 n.12 (justifying the "middle course" taken in an earlier decision to modify exclusivity to allow parties the opportunity to present plans and at the same time prevent the disturbance to the process that may result from terminating exclusivity entirely);[13] *In re*

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[13] Specifically, the *United Press* court offered the following rationale for its approach: "Thus, this Court adopted a middle approach, initially suggested by the parties themselves – opening up the right to file a plan on a limited basis to those two entities (besides the Debtor itself) that have the most at stake in this case and have shown themselves to be responsible parties, while refraining from opening the floodgates completely. The statute does not expressly prohibit this eminently sensible middle course, and I can perceive no reason to find any such prohibition by implication." *United Press*, 60 B.R. at 271 n.12.

Texaco, 81 B.R. at 808 (Bankr. S.D.N.Y. 1988) (referring to earlier ruling from bench that "it would be willing to terminate the exclusivity periods on motion if the statutory committees and . . . [the debtor's principal adversary] could agree unconditionally to a base/cap plan, provided that Texaco was given an opportunity to have input with respect to the negotiations").

Finally, if PG&E's concerns about ensuing chaos have merit, then this Court can construct adequate procedural safeguards to address such concerns. *See PSNH*, 99 B.R. at 177.

In sum, PG&E's threats of "chaos" are sufficiently remote and capable of being addressed so as not to warrant exclusion of the Commission's Alternate Plan.

V.

CONCLUSION

For the reasons set forth herein and in the Cohen Declaration, the Commission respectfully requests that this Court deny PG&E's Second Extension Motion to the extent necessary to permit the Commission to file its Alternate Plan and solicit acceptances thereto.

DATED: January 8, 2002

Respectfully submitted,

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UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

SAN FRANCISCO DIVISION

In re PACIFIC GAS AND ELECTRIC COMPANY, a California corporation, Debtor. Federal I.D. No. 94-0742640	Case No. 01-30923 DM Chapter 11 Case **THE COMMISSION'S MEMORANDUM IN FURTHER SUPPORT OF ITS OBJECTION TO PROPOSED DISCLOSURE STATEMENT FOR PLAN OF REORGANIZATION UNDER CHAPTER 11 OF THE BANKRUPTCY CODE FOR PACIFIC GAS AND ELECTRIC COMPANY** Date: January 25, 2002 Time: 9:30 a.m. Place: 235 Pine Street, 22nd Floor, San Francisco, California

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PRELIMINARY STATEMENT

PG&E's proposed Plan and Disclosure Statement have little to do with the traditional bankruptcy goal of adjusting debtor-creditor relationships and other interests in property of the debtor. Instead, the centerpiece of PG&E's proposed plan is its attempt to obtain unprecedented and sweeping relief against the Commission and the State of California enjoining them from exercising their sovereign regulatory authority. PG&E has not proposed a normal plan of reorganization; it has proposed a plan of preemption and deregulation. PG&E asks the Court to order that PG&E, unlike all other integrated public utilities in this country, need not comply with applicable state statutes, state regulations, and state regulatory authority.

The Court should not approve PG&E's Disclosure Statement because it describes a Plan that is unconfirmable on its face, for at least two independent reasons:

1. No Preemption. According to PG&E, section 1123(a)(5) of the Bankruptcy Code evinces Congressional intent to sweep aside virtually all state regulatory authority over public utilities that file for bankruptcy. But Congress intended nothing of the kind. Section 1123(a)(5) provides that "[n]otwithstanding any otherwise applicable nonbankruptcy law, a plan shall . . . provide adequate means for the plan's implementation . . . ." On its face, this language refers to the contents of a plan, and preempts nonbankruptcy laws that might otherwise regulate the content of the plan, such as securities-related laws that might otherwise require more disclosure in the plan than is mandated by the Bankruptcy Code. Section 1123(a), read naturally, does *not* provide for express preemption of nonbankruptcy laws regulating transactions contemplated by the provisions of a proposed plan. Nor could Congress reasonably have intended that the phrase "notwithstanding any otherwise applicable nonbankruptcy law" would confer upon the bankruptcy court the discretion or authority to authorize violations of state or federal nonbankruptcy law, civil or criminal, merely because the debtor has indicated its intention to violate those laws in its plan.

The legislative history of section 1123(a)(5) shows that the "notwithstanding" phrase was added in 1984 as a technical amendment that was *not* intended to alter the prior scope of the law. Furthermore, the "notwithstanding" phrase derives from a provision in a 1980 bill that was described in a Report of the House Judiciary Committee in a way that squarely supports the Commission's reading of the text, and is completely irreconcilable with PG&E's. Under applicable case law, which was left unaffected by enactment of the "notwithstanding" phrase, the extent to which provisions of a proposed plan may displace otherwise applicable state law is governed by principles of *implied* preemption. The backdrop for those principles includes presumptions that militate strongly against preempting state regulatory law. *See Medtronic, Inc. v. Lohr*, 518 U.S. 470, 485 (1996).

In keeping with these principles, the Ninth Circuit ruled in *Baker & Drake Inc. v. Public Service Commission of Nevada*, 35 F.3d 1348 (9th Cir. 1994), that the Bankruptcy Code does not preempt state statutes or regulations intended to protect the public safety and welfare. According to the Ninth Circuit, state statutes may be preempted by the Bankruptcy Code only if, at a minimum, they are directed solely at economic regulation, narrowly understood, and if certain other factors apply. The provisions of the Public Utilities Code that PG&E seeks to preempt protect the public safety and welfare, and accordingly preemption cannot occur. That would be true even if enforcement of the challenged provisions of state law would make a bankruptcy reorganization more difficult, or even impossible.

Here, however, that is not the case. As the Commission states in its objection to PG&E's second request for an extension of its plan exclusivity, which the Commission is also filing today, the Commission has formulated an alternative plan. With the Court's permission, the Commission intends to propose that plan. The Commission's plan does not require preemption of state regulatory law, maintains adequate safeguards for the safety and welfare of California citizens, and provides PG&E's creditors with payment in full in cash (including accrued interest through the plan's effective date). Preemption is not even necessary here, and that is an additional reason why it is impermissible.

2. <u>Sovereign Immunity</u>. The Eleventh Amendment and related principles of sovereign immunity will bar requests for relief against a state or state agency, whether sought in an adversary proceeding or by way of a chapter 11 plan, that have the practical effect of constituting "the prosecution, or pursuit, of some claim, demand, or request . . . in a court of justice." *Cohens v. Virginia*, 19 U.S. (6 Wheat) 264, 407 (1821) (Marshall, C.J.). Here, the

relief PG&E demands in its proposed plan is just such a "claim, demand, or request" against the State of California. PG&E demands sweeping declaratory, injunctive, and the functional equivalent of monetary relief against the Commission and the State of California. These demands for relief are doubly offensive to the sovereignty of the State. First, the demands are aimed specifically and purposefully at the Commission and the State in their capacities as sovereign regulator; PG&E is not requesting relief against the Commission or the State as ordinary creditors. Second, PG&E's demands for relief seek to bar the Commission and the State from exercising sovereign powers that are absolutely fundamental to the State's regulatory authority over PG&E, a public utility, and consequently to the safety and welfare of the citizens of California.

STATEMENT OF FACTS

In its proposed plan, PG&E demands sweeping declaratory and injunctive relief against the Commission and its sovereign regulatory authority. PG&E's proposed plan seeks to dislodge the Commission's regulatory jurisdiction to review, for compliance with California law, the four main transactions through which PG&E will separate its current business into ETrans, GTrans, Gen, and the Reorganized Debtor.[1] In this way, PG&E hopes to push through a series of transactions that, in their current form, could not reasonably be expected to survive the scrutiny of the Commission and its experts. PG&E also demands that the Bankruptcy Court retain jurisdiction over several critical aspects of the operations of the proposed Reorganized Entities, even after PG&E emerges from bankruptcy. In essence, PG&E would have this Court remain on as a "super-regulator" to review and manage the relationship between PG&E, the Commission, and ratepayers in California.

As set forth at greater length in the accompanying declaration of Loretta M. Lynch, President of the Commission, the state statutes and regulations that PG&E seeks to preempt constitute the heart of the Commission's regulatory authority over public utilities like

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[1] Capitalized terms not defined herein shall have the meanings ascribed thereto in PG&E's First Amended Disclosure Statement ("Am. Discl. Stmt.").

PG&E, and reflect sovereign determinations of the State of California that balance the competing interests of regulated public monopolies and those of the citizens of the State.

The statutes and regulations that PG&E seeks to preempt are not merely "economic" in the sense that they primarily generate revenue or taxes for the State, or are primarily concerned with other economic or debtor-creditor matters. Rather, these statutes and regulations directly further the State's police power and sovereign obligation to provide for the safety and welfare of its residents. For example, PG&E demands that section 451 of the Public Utilities Code be preempted. That section, together with other provisions of California law, establishes PG&E's fundamental "obligation to serve," which requires PG&E to provide electricity at all times to every ratepayer within its service area.[2] PG&E demands that the Bankruptcy Court preempt PG&E's obligation to serve and replace it with a new regulatory regime of PG&E's own making, under which the Bankruptcy Court would retain jurisdiction indefinitely to regulate and oversee the relationship between PG&E and its customers. *See* Am. Discl. St. at 112.

Similarly, public safety and welfare would be compromised if the Court preempted, as PG&E demands, state laws that require Commission review and approval before a public utility may enter into certain transactions that affect its ownership and control, financial integrity, or ability to carry out its functions. (Lynch Decl. ¶¶ 34-37.)

As a regulated public monopoly, of course, PG&E does not have the same freedom concerning its property and operations that a purely private company does. In exchange, PG&E enjoys the considerable advantages of being a public monopoly. The purpose

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[2] *See* Cal. Pub. Util. Code §§ 451, 761, 762, 768, 770 (2002); *see also Interim Order Affirming the Obligation to Serve and Issuing Temporary Restraining Order*, PUC Dec. 01-01-046 dated Jan. 19, 2001, at 1-2 ("We affirm that regulated California utilities must serve their customers. This requirement, known as the 'obligation to serve,' is mandated by state law. A utility's obligation to serve is part and parcel of the entire regulatory scheme under which the Commission regulates and controls utilities under the Public Utilities Act."); *id.* at 7, 16 ("State law clearly requires utilities to serve their customers"; "[u]nder Public Utilities Code sections 451, 761, 762, 768 and 770, PG&E . . . [has] an obligation to provide full and adequate service to all of [its] customers . . . ."; opinion discusses basis in California statutes and regulatory decisions for PG&E's duty to serve).

of requiring Commission review of transaction involving regulated public monopolies is to ensure that the monopolies do not enter into transactions, such as many of the transactions that PG&E proposes here, that threaten their ability to serve their customers, have an adverse environmental impact, or that have the potential to harm the public interest. (*Id.* ¶¶ 34-35.)

For example, PG&E demands that the Commission's Affiliate Transaction Rules be preempted. (*See* Am. Discl. St. at 112.) These rules establish certain limits and Commission oversight of the transactions and relationship between public utilities and their affiliates. The State has an obvious and strong interest in limiting the scope of the monopoly it grants to public utilities in exchange for the utilities' undertaking to serve. These provisions and rules prevent a public utility from abusing its self-dealing relationship with subsidiaries and affiliates in competition, and otherwise acting to the detriment of the public. (Lynch Decl. ¶¶ 47-48.)

To make matters worse, several of the critical transactions that PG&E now seeks to accomplish were in substance considered by the Commission prior to PG&E's bankruptcy, and were rejected because the proposed transactions would have been detrimental to public safety and welfare. For example, in 1994 PG&E indicated an intention to change the jurisdictional status of its California natural gas transmission and storage systems into "interstate" facilities, subject to regulation by FERC rather than by the Commission. The Commission determined, however, that the transactions contemplated would have potential adverse impacts and were not in the public interest. (*Id.* ¶¶ 7-8, 44-46.) Such adverse impacts included "the possibility that the Commission will be unable to ensure the provision of base service to homes, schools and hospitals in the case of a supply or capacity crisis; the possibility that the pricing of gas service for captive customers will undermine the universal availability of affordable gas service for California citizens; the possibility that pricing of gas service for captive customers will necessitate the widespread use of alternative fuels, thereby creating adverse impacts on the environment." (*Id.* ¶ 8.)

Similarly, in 1999 PG&E asked the Commission to approve a proposal to break its massive hydroelectric system into a number of lots, or "bundles," and auction those bundles off in the market to the highest bidder. But a draft Environmental Impact Report prepared for the Commission by independent consultants showed that the proposal would have significant adverse environmental consequences. (*Id.* ¶¶ 9-11 & Ex. A.)

The laws and rules that PG&E would have this Court preempt are vital to public safety and welfare in the State of California and constitute the heart of the Commission's sovereign regulatory authority. They should not be preempted.

ARGUMENT

The Court should not approve PG&E's Disclosure Statement because it describes a Plan that is unconfirmable on its face. *See In re Silberkraus*, 253 B.R. 890, 899 (Bankr. C.D. Cal. 2000) ("There are numerous decisions which hold that where a plan is on its face nonconfirmable, as a matter of law, it is appropriate for the court to deny approval of the disclosure statement describing the nonconfirmable plan.").[3]

I.

PG&E'S PROPOSED PLAN IS UNCONFIRMABLE BECAUSE IT DEMANDS DECLARATORY AND INJUNCTIVE RELIEF THAT THE BANKRUPTCY COURT CANNOT GRANT

It appears that PG&E seeks to avoid the effect of a multitude of state statutes and regulations on the grounds that those statutes and regulations are preempted by section 1123(a)(5) of the Bankruptcy Code. That section, which is contained in the section of the Bankruptcy Code governing the description of plan contents, provides in relevant part:

> (a) Notwithstanding any otherwise applicable nonbankruptcy law, a plan shall
> . . .
> (5) provide adequate means for the plan's implementation such as—

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[3] Pursuant to the Court's Order of December 5, 2001, this Memorandum sets forth only the Commission's arguments that the Proposed Amended Plan cannot be confirmed as a matter of law (and that the Proposed Amended Disclosure Statement therefore cannot be approved), because the plan rests on a misapprehension of the preemptive effect of the Bankruptcy Code and would violate California's sovereign immunity if confirmed. The Commission expressly preserves all of the arguments previously set forth, and to be raised hereafter, in support of its Objection, including its other arguments that the Proposed Amended Plan cannot be confirmed.

(A) retention by the debtor of all or any part of the property of the estate;

(B) transfer of all or any party of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;

(C) merger or consolidation of the debtor with one or more persons;

(D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate;

(E) satisfaction or modification of any lien;

(F) cancellation or modification of any indenture or similar instrument;

(G) curing or waiving of any default;

(H) extension of a maturity date or a change in an interest rate or other term of outstanding securities;

(I) amendment of the debtor's charter; or

(J) issuance of securities of the debtor, or of any entity referred to in subparagraph (B) or (C) of this paragraph, for cash, for property, for existing securities, or in exchange for claims or interests, or for any other appropriate purpose.

PG&E evidently takes the position that, by enacting this section of the Bankruptcy Code, Congress intentionally swept aside virtually all state regulatory authority over public utilities that file for bankruptcy.[4]

Congress intended nothing of the kind. Construing section 1123(a)(5) in the manner PG&E proposes, in order to hold that the State of California is powerless to enforce its sovereign regulatory authority over a public utility, would stretch the section beyond recognition. Where the Ninth Circuit has had occasion to address similar, albeit far more modest, efforts to misuse the Bankruptcy Code in this way, it has declined to accept any such overbroad interpretation. *See Baker & Drake*, 35 F.3d 1348 (9th Cir. 1994).

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[4] PG&E does not want to preempt all state laws regarding public utilities, only those that it does not like. For example, while PG&E demands that the Court order that just about every state law that imposes any burden or inconvenience on PG&E be preempted, PG&E nevertheless contends that another section of the Public Utilities Code should remain in full force and effect, because, as PG&E reads that section, it imposes a burden on the Commission to market value PG&E's non-nuclear facilities. (Am. Discl. Stmt. at 131 n.19.,

A. Section 1123(a)(5) Does Not Authorize Preemption of the State Regulatory Laws That PG&E Seeks to Avoid

The Supreme Court has classified two general categories of preemption: express preemption and implied preemption. Express preemption occurs when Congress clearly indicates its intent to preclude state regulation in a given area. *See, e.g., Cipollone v. Liggett Group, Inc.*, 505 U.S. 504, 517 (1992). Implied preemption refers to a situation in which Congress, through its legislation, has by implication prohibited certain state regulation in a given area. *See, e.g., Buckman Co. v. Plaintiffs' Legal Comm.*, 531 U.S. 341, 348 (2001). Neither of these categories of preemption applies to the state statutes and regulations PG&E contends are preempted.

1. Section 1123(a)(5) Governs the Required Contents of a Plan, Not the Substantive Legality of the Transactions Described in the Plan

Section 1123(a), which is entitled "Contents of plan," lists features that a debtor is required to include in any proposed plan. The text of section 1123(a) imposes a duty on the proponent to include the enumerated mandatory plan provisions in any proposed plan—"[n]otwithstanding any otherwise applicable nonbankruptcy law" that might excuse the debtor from this duty or impose inconsistent duties concerning the mandatory contents of a plan. Subsection 5 of section 1123(a), on which PG&E evidently relies here, provides that a plan shall "provide adequate means for the plan's implementation . . . ." Thus, if a debtor fails to set forth, in the proposed plan, adequate means of implementation, the debtor's failure demonstrates a lack of good faith under section 1129(a)(5) and precludes confirmation of the plan.[5] Section 1123(a)(5) does *not*, however, say or mean that "notwithstanding any otherwise applicable nonbankruptcy law," the debtor may take any action that arguably constitutes "adequate means for the plan's implementation," regardless of whether the means selected or the plan provision to be implemented violate the criminal or civil statutes of the United States or one or more of the States. Any such interpretation would be inconsistent with the natural meaning of

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[5] *See Crestar Bank v. Walker (In re Walker)*, 165 B.R. 994, 1003-04 (E.D. Va. 1994) (collecting cases).

the text and, in particular, with the natural meaning of the "notwithstanding" phrase at the outset of section 1123(a).

An analogy may clarify the point. If a hypothetical statute stated "the plan must demonstrate how it will be funded," that mandate would not entitle the proponent to declare that it intended to steal the money. The requirement on its face would go to the required contents of the plan, and would not address the legality of the proposed method of funding. And if the hypothetical statute stated "notwithstanding any otherwise applicable nonbankruptcy law, the plan must demonstrate how it will be funded," the result would be the same. The "notwithstanding" phrase, read naturally, would mean that the proponent must formulate and disclose a proposed method of funding, notwithstanding any other law that might limit, modify, or expand the duty to formulate and disclose such a method. It would still not mean that the plan could be funded through theft or other violations of nonbankruptcy law. For the same reasons, actual subsection 1123(a)(5) means that a plan proponent has a duty, not subject to abolition or qualification under otherwise applicable nonbankruptcy law, to formulate and disclose adequate means for implementation. Section 1123(a)(5) does *not* mean that the debtor, in the process of implementation, may freely violate any and all nonbankruptcy laws.

This textual analysis does not, of course, mean that a plan may never displace any provision of otherwise applicable nonbankruptcy law. Section 1123(a) does not expressly address what happens if the plan proposes an action that is substantively inconsistent with nonbankruptcy federal or state law. It leaves that problem, in the absence of an applicable provision for express preemption elsewhere in the Code, to principles of *implied* preemption that have been developed through many years of bankruptcy case law, and that historically have proven adequate to the delicate problem of reconciling bankruptcy-related interests and interests arising from nonbankruptcy federal and state law. In this Circuit, the definitive and controlling exposition of those principles is the Ninth Circuit's decision in *Baker & Drake*, which is discussed below.

The structure, legislative history, and overall purpose of section 1123(a) support the Commission's reading. As to structure, subsections of section 1123(a) other than subsection 5 focus on commands *to the plan proponent* that it include various features in the proposed plan. More specifically, subsections (1) through (3) require designation of classes of claims, and specification of claims or interests that are not impaired or are impaired. Subsection (4) commands the proponent to provide the same treatment for each claim or interest of a particular class, absent consent by the relevant holder. Subsection (6) contains mandatory provisions for the charter of a corporate debtor or successor entity. And subsection (7) provides that plan provisions governing the selection of certain fiduciaries must be consistent with the interests of creditors and equity security holders and with public policy.

These provisions all either direct the proponent to include features in the proposed plan, or, as to subsection (7), limit the scope of certain plan provisions. Subsection (5) should be read in the same way: it requires the proponent to explain why the proposed plan is workable by showing that the plan "provide[s] adequate means for . . . implementation." Subdivisions (A) through (J) of subsection 5 specify particular actions that the proponent may include in its proposals for implementation. And the requirements set forth in section 1123(a), including that of subsection 5, are binding on the proponent "notwithstanding any otherwise applicable nonbankruptcy law" that might be read to limit (or, evidently, to expand) those requirements.[6]

PG&E's view also results in a misfit between section 1123 and section 1142(a) of the Code. Under section 1142(a), "[n]otwithstanding any otherwise applicable nonbankruptcy law, rule, or regulation *relating to financial condition*, the debtor . . . shall carry out the plan . . . . (Emphasis added.) The obvious negative pregnant arising from section 1142(a) is that a debtor, in carrying out a plan, must generally abide by otherwise applicable non-bankruptcy law that

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6 *FCX, Inc. v. Universal Cooperatives, Inc.*, 853 F.2d 1149, 1155 (4th Cir. 1988), reads § 1123(a)(5) as an "empowering statute," in the sense that it authorizes a proponent to propose steps that may enlarge the debtor's prebankruptcy rights. That terminology is consistent with the Commission's view that a plan may preempt state law only in the circumstances identified in *Baker & Drake*.

does *not* relate to financial condition. That negative pregnant, and indeed the necessity for this portion of section 1142(a), would be overridden if, as PG&E evidently contends, section 1123 immunizes a debtor from any duty to comply with *any nonbankruptcy law at all* in carrying out the provisions of the plan.[7]

This reading finds further support in the legislative history of the statute that added the phrase "[n]otwithstanding any otherwise applicable nonbankruptcy law" to section 1123(a). That phrase was not included in section 1123(a) as enacted in the Bankruptcy Code of 1978. The phrase apparently first appeared in S. 658 as submitted by the House Judiciary Committee to the House in July 1980. The Judiciary Committee proposed to amend section 1123(a) in relevant part as follows. (The Judiciary Committee indicated deleted language in bold brackets, added language in italics, and unchanged language in roman type.)

> (a) **[A]** *Notwithstanding any otherwise applicable nonbankruptcy law, a* plan shall-- . . . .
>
> (5) provide adequate means for the plan's [execution] *implementation*, such as-- . . . .

An Act to Correct Technical Errors, Clarify and Make Minor Substantive Changes to Public Law, Pub. L. No. 95-598, S. 658, 96th Cong., 2d Sess. (1980), H.R. Rep. No. 96-1195, 96th Cong., 2d Sess. 122-23 (July 25, 1980) (hereinafter "H.R. Rep. No. 96-1195," Ex. A Tab 1).[8]

Two points concerning the Report of the House Judiciary Committee are highly significant. First, the Judiciary Committee's comments on section 102(a) of the proposed legislation (which contained the proposed amendment to section 1123(a)) in the section-by-section analysis read as follows:

> *This amendment makes clear that the rules governing what is to be contained in the reorganization plan are those specified in this section*; deletes a redundant word; and makes several stylistic changes.

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[7] In commenting on section 1142, *Collier on Bankruptcy* notes that "if the plan called for a transfer of a broadcast license . . ., an order implementing confirmation should not allow the debtor to evade the necessary regulatory process for obtaining such a transfer." 8 Lawrence P. King, *Collier on Bankruptcy* ¶ 1142.03[2] (2001).

[8] Copies of the relevant portions of the legislative history cited herein are contained in a Legislative History Appendix attached hereto as Exhibit A.

H.R. Rep. No. 96-1195, at 22 (emphasis added) (Ex. A Tab 2).

Thus, according to the Judiciary Committee, the "notwithstanding" phrase was added to clarify that "*this section*"—i.e., section 1123(a)—definitively states "the rules governing what is to be contained in the reorganization plan."[9] The phrase "[n]otwithstanding any otherwise applicable nonbankruptcy law" fits with that purpose *only* if the phrase is understood to mean that otherwise applicable nonbankruptcy law is ineffective to vary the specification in section 1123(a) of the mandatory provisions of a proposed plan. In other words, nonbankruptcy law is ineffective to excuse a debtor from including all mandatory elements in the proposed plan, and is evidently ineffective to require the inclusion of additional elements. That is exactly the reading that the Commission gives to section 1123(a).

Second, the Report of the House Judiciary Committee is completely inconsistent with the revolutionary significance that PG&E apparently attributes to the "notwithstanding" phrase. PG&E's proposed plan, which calls for wholesale preemption of California regulatory law, appears to rest on the assumption that under the "notwithstanding" phrase, a bankruptcy court has unlimited discretion to preempt state regulatory law that prohibits either transactions contemplated by a restructuring or certain post-restructuring activities. If the "notwithstanding" phrase of section 1123(a) had been intended to effect such a revolutionary change, notwithstanding the patent inadequacy of the text for this purpose, one would at least expect documentation in the legislative history of this amazing new development. To the contrary, however, the Report of the House Judiciary Committee treats this amendment to section 1123(a) as entirely mundane.

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9 Examination of all the amendments to section 1123 proposed by S. 658, as reported by the House Judiciary Committee, discloses that the first portion of the section-by-section analysis (which is italicized in the block quotation above in text) could refer *only* to the addition of the "notwithstanding" phrase. A complete copy of those proposed amendments to section 1123 appears as Exhibit A, Tab 3, to the Legislative History Appendix. *See* An Act Correcting Technical Errors and Making Minor Substantive Changes to Public Law 95-598, S. 658, 96th Cong., 2d Sess. 1980, *reprinted in* 30 Bankr. L. Rep. 83, 198 (CCH) (Nov. 20, 1980) (text of amendment to statute) (Ex. A Tab 3).

In its introduction to that Report, the House Judiciary Committee noted that technical amendments were required to correct "[e]rrors in printing, spelling, punctuation, grammar, syntax, and numeration . . . ." H.R. Rep. No. 96-1195, at 1 (Ex. A Tab 4). Though "[s]uch matters [constitute] the vast majority of the Technical Amendments Act," some items of a substantive nature were also said to be included. *Id.* at 2. The Report listed general areas in which substantive changes were made, none of which embraced the subject matter of section 1123(a). *See id.* at 2-5 (Bankruptcy Judge's Retirement); 5-6 (Municipal Financing), 6-7 (Stockbroker/Commodity Broker Liquidation), 7-8 (Tax Provisions).

In December 1980, the House passed S. 658 by unanimous consent with additional amendments. *See* S. Rep. No. 98-65, 96th Cong., 1st Sess., Calendar No. 102, at 51 (chronicling legislative history) (hereinafter "S. Rep. No. 98-65," Ex. A Tab 6). The Senate reintroduced the bill as S. 3259 and passed it unanimously. *Id.* at 51-52. The House, however, took no action on the final Senate changes, and consequently the bill was never enacted into law. *Id.*

The remaining legislative history for the "notwithstanding" phrase confirms that it was not intended to have the meaning apparently attributed to it by PG&E. On April 2, 1981, three Senators introduced S. 863, which incorporated all of the provisions of S. 3259 (including the "notwithstanding" amendment to section 1123(a)). *See* Bankruptcy Amendments Act of 1981, S. 863, 97th Cong., 1st Sess. (1981), S. Rep. No. 97-150, 97th Cong., 1st Sess. at 2 (July 10, 1981) (Ex. A Tab 7). After hearings on April 3 and 6, 1981, during which no statements appear to have been made concerning proposed amendments to section 1123(a), the Senate Judiciary Committee reported S. 863 to the Senate. *Id.* In the section-by-section analysis of its report, the Judiciary Committee described the proposed to amend section 1123(a) as follows:

> Paragraphs (1) through (5) make technical stylistic changes. Paragraph (6) makes clear that preferred stock without voting rights can be issued under the plan and the prohibition against issuing stock that cannot be voted extends only to common stock.

Id. at 15, Ex. A Tab 8.

The Senate passed S. 863, but the House did not consider it. S. Rep. No. 98-65, at 52 (Ex. A Tab 9). Accordingly, the bill was not enacted. Then, in 1983, S. 455 was introduced in the Senate. S. Rep. No. 98-65, at 1. S. 455 contained numerous technical amendments and certain substantive amendments. The technical amendment section of S. 455 contained the proposed amendment to section 1123(a) with the "notwithstanding" phrase. S. Rep. No. 98-65, at 51-53 (Ex. A Tab 10). The Senate Judiciary Committee submitted S. 455, with the amendment to section 1123(a), to the Senate. S. Rep. No. 98-65, at 2. The amendment to section 1123(a) was contained in Subtitle I, entitled "Technical and Clarifying Amendments," of the bill as reported. The summary section of the accompanying Committee Report noted that:

> [T]he bulk of the provisions in this subtitle [I] are drawn from S. 863 [the 1981 predecessor bill], which passed the Senate by unanimous consent in 1981. The provisions correct grammatical, punctuation and spelling errors in the code, clarify the intent of the drafters in certain sections, and generally refine procedures.

S. Rep. No. 98-65, at 52-53 (Tab 11).

The section-by-section analysis in the Committee Report reiterated that the amendment to section 1123(a) "make[s] technical stylistic changes." *Id.* at 84 (Tab 11).[10]

S. 455 was ultimately incorporated in S. 1013, which in turn formed the basis for a Conference Committee appointed to reconcile differing bankruptcy legislation passed by the Senate and the House. The bill reported by the Conference Committee contained the amendment to section 1123(a) that included the "notwithstanding" phrase. The Conference Report contained only the text and did not explain its contents. *See* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L. No. 98-353, 98th Cong., 2d Sess. (1984), H.R. Conf. Rep. No. 98-882 (June 29, 1984) *reprinted in* Arnold & Porter Legislative History: Pub. L. No. 98-353 at *55 (Tab 13). A concurrently issued document entitled *Statements by Legislative Leaders* did discuss the bill, but that document made no mention of the amendment to section 1123(a). *See* Bankruptcy Amendments and Federal Judgeship Act of 1984, Pub. L.

[10] A complete copy of the proposed amendments to section 1123 appears at Tab 12 to the Legislative History Appendix.

No. 98-353, *Statements by Legislative Leaders, reprinted in* 1984 U.S.C.C.A.N. 576-606 (Tab 14). Both the Senate and the House passed the bill proposed by the Conference Report, again without discussion of the provision pertinent here, and the President signed it into law on July 10, 1984. *See* Bankruptcy Federal Judgeship Act, Pub. L. No. 98-353, 98 Stat. 333 (Tab 15). This legislative history, which uniformly treated the amendment to section 1123(a) as technical and mundane, squares perfectly with Commission's reading of the statute and is impossible to reconcile with PG&E's.

The Commission's reading also makes sense in light of the purposes of section 1123(a) and the nuanced overall approach taken by Congress in the Bankruptcy Code and elsewhere to reconciling interests arising from bankruptcy law and interests arising from nonbankruptcy federal and state law. That approach is reflected in provisions such as section 362(b)(4) of the Bankruptcy Code (the police and regulatory powers exception to the automatic stay) and section 959(b) of the Judicial Code (requiring debtors in possession to comply with valid state laws). On the Commission's view, section 1123(a) requires and authorizes the plan proponent to include certain features in a proposed plan. The section does not directly speak to whether a bankruptcy court may confirm a plan calling for actions inconsistent with applicable nonbankruptcy law; rather, that problem is left to traditional case-by-case adjudication under principles of implied preemption.

PG&E, in contrast, apparently views section 1123(a) as an engine of destruction for federal and state laws that, in the view of a plan proponent, stand in the way of a desired reorganization or of desired post-reorganization activities. PG&E's proposed plan implausibly assumes that Congress conferred unfettered discretion on plan proponents and bankruptcy courts to abrogate rights under federal and state law.

2. At Most, Section 1123(a)(5) Merely Codifies General Principles of Implied Preemption, as Set Forth by the Ninth Circuit in *Baker & Drake*

As explained above, the Commission does not view the "notwithstanding" phrase in section 1123(a) as preempting nonbankruptcy laws that would otherwise prohibit proposed actions to be taken pursuant to a plan. That phrase, in the Commission's view, displaces only nonbankruptcy laws that might otherwise regulate the contents of the plan. If, however, the Court does not accept this view, the Court will need to formulate principles limiting the scope of any express preemption flowing from the "notwithstanding" phrase.

The appropriate limiting principles here are those developed in implied preemption cases and set forth in *Baker & Drake*. That interpretation gives appropriate respect to the uniform treatment in the legislative history of the "notwithstanding" phrase as technical and non-substantive. That interpretation also appropriately reconciles this provision with other provisions of the Bankruptcy and Judicial Codes, as described above; with the approach of the case law before enactment of the "notwithstanding" phrase, which is surveyed in *Baker & Drake* and is appropriately considered in order to give meaning to this technical and clarifying change; and with applicable general presumptions and canons of construction, including the presumption that Congress is presumed not to displace state regulation in traditional areas of state concern and must be clear and explicit in order to do so. *See Medtronic*, 518 U.S. at 485.

There are only two alternatives to this interpretation of the "notwithstanding" phrase, should it be read as an express preemption provision applicable to nonbankruptcy laws that would otherwise prohibit proposed actions to be taken pursuant to a plan. One alternative would empower every bankruptcy judge in the country, if so urged by a plan proponent, to preempt any and all federal or state laws thought to impede a restructuring. As the Court has recognized, that cannot be the law. To use the Court's example, a bankruptcy court obviously lacks the authority to authorize a bankrupt liquor store to sell liquor to minors in violation of state law, even if the liquor store were to show that a restructuring would be impossible in the absence of that authorization, and even though sales of property of the estate are among the transactions enumerated in section 1123(a)(5)(D). The other alternative would be to say that Congress, by enacting the "notwithstanding" phrase as a technical change, intended to require the courts to make up entirely new limiting principles in this area, without any express guidance in the "notwithstanding" phrase itself and without being bound by prior case law, despite the total absence of any Congressional intent to reject that case law. That, too, is not a plausible theory of Congress's intent.

3. The Scope of Preemption Sought by PG&E Is Inconsistent on its Face with the Ninth Circuit's Controlling Decision in *Baker & Drake*

In this Circuit, *Baker & Drake* is the controlling exposition of the extent to which a plan of reorganization may authorize the debtor to take actions in violation of state law. There, the debtor, which operated a taxicab company, proposed in its plan of reorganization to have the employee-drivers of its taxicabs become independent contractors who would lease their cabs from the debtor. This feature of the proposed plan would have diminished the debtor's tort liability for personal injury lawsuits arising from the operation of the cabs; would have reduced the debtor's insurance premiums; and would have eliminated the debtor's liability for payroll taxes. This feature of the plan, however, also violated an applicable Nevada administrative regulation, which prohibited the debtor from leasing its taxicabs. Nevada defended its regulation as intended to further the public convenience and safety, evidently by promoting the company's control over the operation of the taxicabs.

The bankruptcy court in *Baker & Drake* approved the plan of reorganization and enjoined the Nevada agency from enforcing its regulation against the reorganized debtor. Adopting an approach similar to that urged here by PG&E (albeit in circumstances where the preemption sought was far more limited than PG&E seeks here), the court ruled as follows:

> I'm setting the [state] law aside in this instance. I'm not applying it. The Constitution of the United States says that Congress shall prescribe bankruptcy laws. It has. It takes precedence in given situations, and I think this is one.

Baker & Drake, 35 F.3d at 1350 (quoting oral ruling of bankruptcy court).

The district court reversed the bankruptcy court's decision, and the Ninth Circuit affirmed the district court's decision. The Ninth Circuit, after surveying the case law, formulated the applicable inquiry as follows:

> As we view these cases, they suggest that federal bankruptcy preemption is more likely (1) where a state statute facially or purposefully carves an exception out of the Bankruptcy Code, or (2) where a state statute is concerned with economic regulation rather than with protecting the public health and safety. With these principles in mind, we first note that [the Nevada administrative regulation] makes no reference to the Bankruptcy Code, and that its subject matter

> is unrelated to the Bankruptcy Code. Second, while [the Nevada regulation] may not be as essential to the protection of health of health and safety as, for example, toxic waste laws, it was promulgated in part as a safety measure, and its substantive provisions do not facially belie that goal. On the contrary, the district court found that the regulation was reasonably designed to protect public safety.

Id. at 1353-54; *see also Commonwealth of Massachusetts v. First Alliance Mortgage Co. (In re First Alliance Mortgage Co.)*, 263 B.R. 99, 112 (9th Cir. BAP 2001).

Applying these principles to the facts of the case, the Ninth Circuit concluded emphatically and without hesitation that the plan of reorganization could not be confirmed. (The Ninth Circuit did not remand the case to the Bankruptcy Court, and therefore necessarily concluded that the plan of reorganization was unconfirmable *as a matter of law.*) The Ninth Circuit wrote as follows:

> The Bankruptcy Code does not preempt [the Nevada administrative regulation]. Nevada's ban on taxi leasing is a broadly applicable regulation, not an individual, discretionary agency decision directed only at [the debtor]. Moreover, [the regulation] is not just an economic regulation, but one reasonably intended to secure the public convenience and safety. More importantly, it does not directly conflict with the purposes of the Bankruptcy Code in any way which could be generalized beyond the particular facts of the present case. The fact that a particular debtor's Chapter 11 reorganization is made more difficult because of compliance with otherwise valid state regulation is not a sufficient basis to invoke preemption.[11]

The *Baker & Drake* decision gives appropriate weight and respect to the legislation of a sovereign State, and to the expertise of its regulators, in areas of public convenience and safety. A bankruptcy judge may be able to police the fairness of strictly and narrowly economic aspects of a bankruptcy reorganization. Bankruptcy courts, however, lack authorization or expertise to substitute their judgment for that of a State and its expert regulators in other areas of public policy, as the division drawn in *Baker & Drake* recognizes.

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[11] *Id.* at 1354-55. The *Baker & Drake* court also clarified that the principles of that case apply even when applicable state law would render a successful reorganization impossible. On that point, the Ninth Circuit wrote that "Congress's purpose in enacting the Bankruptcy Code was not to mandate that *every company* be reorganized *at all costs*, but rather to establish a preference for reorganizations, where they are legally feasible and economically practical. Thus, if compliance with [the Nevada regulation] were to render [the debtor] financially unable to reorganize, neither [the debtor] nor Nevada would thereby be violating any provision of the Bankruptcy Code." *Id.* at 1353-54 (emphasis in original).

The principles of *Baker & Drake* plainly render PG&E's proposed plan unconfirmable as a matter of law. PG&E seeks preemption of virtually the entire regulatory scheme of the California Public Utilities Code (and various other California laws) with respect to the transactions constituting the proposed reorganization, and it seeks preemption of fundamental provisions of the California Public Utilities Code with respect to PG&E's post-reorganization activities. The various provisions of the Public Utilities Code that regulate such activities are generally applicable to all electric utilities subject to state regulation. The Public Utilities Code is not to be equated to "an individual, discretionary agency decision directed only at [PG&E]." *Id.* at 1354.

Equally obviously, the Public Utilities Code in general, and in respects relevant here, is plainly a body of law "reasonably intended to secure the public convenience and safety." The fundamental mandate of the Commission is to insure the provision of services by regulated utilities to California citizens at just and reasonable rates. That mandate has economic components, but its scope goes vastly beyond economic regulation in the sense of that term relevant under *Baker & Drake.* Finally, the Public Utilities Code obviously "does not directly conflict with the purposes of the Bankruptcy Code in any way which could be generalized beyond the particular facts of the present case." *Id.* at 1354-55.

The facts of *Baker & Drake* involved preemption of a single regulation respecting the ownership of taxicabs. The Ninth Circuit nonetheless found the preemption sought to "constitute a much greater intrusion into state power" than was authorized by prior case law. *Id.* at 1354. The scope of preemption sought by PG&E so far surpasses the preemption sought in *Baker & Drake* as to make argument on the point ridiculous. Both the result in *Baker & Drake* on the facts and the principles laid down in that case render PG&E's proposed plan unconfirmable as a matter of law.

4. Background Principles of Preemption Demonstrate That Section 1123(a) Should Not Be Read to Authorize Preemption of State Law Protecting Public Safety and Welfare, Especially <u>in an Area Traditionally Reserved to State Regulatory Authority</u>

The states are independent sovereigns within the federal system, and a litigant seeking preemption thus must shoulder a difficult burden. *See Nat'l Warranty Ins. Co. RRG v. Greenfield*, 214 F.3d 1073, 1076-1077 (9th Cir. 2000). "In all preemption cases, and particularly those in which Congress has legislated . . . in a field which the States have traditionally occupied, we start with the assumption that the historic police powers of the States were not to be superseded . . . unless that was the clear and manifest purpose of Congress." *Medtronic*, 518 U.S. at 485; *see also Gen. Motors Corp. v. Tracy*, 519 U.S. 278, 304, 308-09 (1997); *Midlantic Nat'l Bank v. N.J. Dep't of Envir. Protection*, 474 U.S. 494, 506-07 (1986) (prohibiting abandonment of property by debtor where such action violates laws protecting public health and safety, despite absence of express limitation in the Bankruptcy Code on the abandonment power).

PG&E confronts these presumptions at their most vigorous. Not only was the Public Utilities Code enacted in an area that has traditionally been left to state control, it concerns one of the most important spheres of state police power, the regulation of public utilities. *See Ark. Elec. Coop. Corp. v. Ark. Pub. Serv. Comm'n*, 461 U.S. 375, 377 (1983).

5. PG&E's Position, Which Calls for Unprecedented Preemption of Core California Regulatory Law Protecting Public Safety <u>and Welfare, Finds No Support in the Case Law</u>

Universal Cooperatives, Inc. v. FCX, Inc., 853 F.2d 1149 (4th Cir. 1988), is consistent with the result for which the Commission contends here, and certainly does not support the massive and unprecedented preemption PG&E seeks. There, the debtor proposed to distribute certain collateral to a secured creditor in order to satisfy a claim secured by the collateral. The secured creditor, however, apparently had a right under its by-laws, which had been adopted pursuant to state law, to refuse to accept the collateral in satisfaction of the claim.

The Fourth Circuit held that the bankruptcy court nonetheless had the power to approve the specific transaction under challenge. That result is consistent with a reasonable application of the principles subsequently delineated in *Baker & Drake*. The debtor proposed the distribution of collateral pursuant to section 1123(a)(5)(D). The displaced by-law concerned the particular creditor that had adopted it, and could reasonably be viewed as "economic," in the narrow sense, in character. This case is entirely different.

Public Service Co. of New Hampshire v. New Hampshire (In re Public Service Co. of New Hampshire), 108 B.R. 854 (Bankr. D.N.H. 1989), surveys some of the general issues raised here, but for numerous reasons does not provide the answers. In that case, the State of New Hampshire argued that the Bankruptcy Code did not and could not preempt any provision of New Hampshire law requiring the approval of the State's Public Utilities Commission for any transaction contemplated by the restructuring. The ultimate holding in *Public Service Co.* was limited to a finding that in principle, the Bankruptcy Code might, under appropriate circumstances, permit preemption of New Hampshire law. The court did not approve any particular plan of reorganization; it did not approve any particular proposed preemption of New Hampshire law; and it underscored that it had not provided "'carte blanche' for the debtor to run roughshod over all types of state regulatory processes both before and after confirmation of any plan of reorganization." 108 B.R. at 891. The opinion is therefore inconclusive concerning the extent to which a plan of reorganization may authorize a debtor to take actions in violation of otherwise applicable nonbankruptcy federal or state law. The proposed plan underlying the opinion was eventually abandoned, so the *Public Service Co.* proceeding never clarified this question.

The opinion does contain very extensive dicta on preemption. We note, in summary fashion, several reasons why those dicta are not controlling here. First, the *Public Service Co.* court viewed the preemption sought there as involving "only a possible transfer of economic regulatory jurisdiction as contrasted with the more acute situation where a transfer of state regulatory authority over health or safety matters is argued to be the effect of federal preemption." 108 B.R. at 859. The arguments and facts here are otherwise. Second, the New Hampshire bankruptcy court obviously demonstrated far less respect for state law than did the Ninth Circuit in *Baker & Drake*. The opinion in *Public Service Co.*, for example, speaks of the "wisdom of Congress' intent to largely remove regulatory agencies from the 'restructuring' necessary in a complex reorganization case." 108 B.R. at 891. Rhetoric of this kind is impossible to square with the Ninth Circuit's adamant refusal in *Baker & Drake* to preempt the authority of a Nevada regulatory agency over a common carrier. Third, *Public Service Co.* extensively discussed and relied upon the district court's decision in *In re MCorp.*, 101 B.R. 483 (S.D. Tex.1989), *rev'd, vacated, and remanded*, 900 F.2d 852 (5th Cir. 1990), *aff'd in part and rev'd in part*, 502 U.S. 32 (1991), which the New Hampshire court said "involved a problem somewhat analogous to the question in the present case." 108 B.R. at 867. The Fifth Circuit, however, rejected the relevant portions of the district court's analysis in *MCorp.*, and the Supreme Court, in a unanimous decision (with one Justice not participating) rejected the district court's decision in its entirety. Fourth, *Public Service Co.* viewed the "notwithstanding" phrase of section 1123(a) as *unambiguously* preempting at least some nonbankruptcy law that would otherwise regulate the restructuring transactions (as opposed to the contents of the proposed plan)—a conclusion that the language of that phrase simply will not sustain. (*Supra* at 9-11.) On that flawed basis, the *Public Service Co.* court rejected inferences from the legislative history supporting a more restrained reading, although the court failed to consider the passage from the 1980 Report of the House Judiciary Committee, *see supra* at 13, that bears most directly on the meaning of this phrase.[12]

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[12] The *Public Service Co.* court also drew certain inferences respecting preemption from Congress's failure to reenact, in the 1978 Bankruptcy Code, prior sections 77B(e)(2) and 77B(f) of the Bankruptcy Act of 1898, as amended in 1934. Those sections provided, among other things, that a plan of reorganization for a utility regulated by a State could not be confirmed until the plan had been submitted to state regulatory authorities; the authorities had had an opportunity to suggest amendments or objections; and the judge had considered those amendments or objections at a hearing. After the hearing, confirmation was possible only if the judge was satisfied that the debtor had obtained appropriate authorizations, approvals, or consents of regulatory authorities. 108 B.R. at 863-64.

The inferences drawn by the court were not warranted. These subsections of the Bankruptcy Act created special federal rights and procedures. It is perfectly reasonable to say that Congress decided to withdraw these special federal provisions, leaving state regulatory authorities to their independent rights and powers under *state* law. Preemption of state law is certainly not to be presumed from Congressional withdrawal of special federal rights that extend beyond, and exist separately from, state law. To the contrary, the applicable presumptions weigh against finding preemption of state regulatory law.

In short, no case has ever authorized anything like the result PG&E seeks here: essentially total preemption of state law that would otherwise regulate the dismemberment of an enormous electric utility, and partial preemption of state law regulating the post-restructuring operations of the utility, in circumstances where ousting state authority could have grave consequences for the safety and welfare of California citizens.

6. Preemption Is Not Essential to a Successful Reorganization of PG&E and Accordingly Is Impermissible As a Matter of Law

At the very least, preemption of state law is impermissible if it is not essential to the consummation of a successful reorganization. *See Baker & Drake*, 35 F.3d at 1354-55. Preemption is not essential here. As the Commission states in its objection to PG&E's second request for an extension of plan exclusivity, the Commission has formulated an alternative plan that does not require preemption of state regulatory law, maintains adequate safeguards for the health and welfare of California's citizens, and provides PG&E's creditors with payment in full in cash (including accrued interest through the plan's effective date).

B. The State Regulatory Laws that PG&E Seek to Preempt Protect Public Safety and Welfare, and for That and Other Reasons Cannot Be Preempted

1. PG&E Impermissibly Seeks to Preempt State Regulation Affecting Public Safety and Welfare

In its proposed plan, PG&E seeks to preempt exactly the sort of state regulation affecting public safety and welfare that the Ninth Circuit held in *Baker & Drake* is not preempted by the Bankruptcy Code.

First, the regulations that PG&E seeks to preempt are "broadly applicable regulation[s], not an individual, discretionary agency decision directed only at" PG&E. *See*

Section 1129(a)(6) of the Code requires that prior to confirmation, regulatory authorities (whether federal or state) must have approved rate changes provided for in a plan, or that such rate changes must be "expressly" conditioned on approval. This provision protects the special bankruptcy interest in assuring that if the plan is funded through rate changes, either (i) that funding has been secured before confirmation through appropriate regulatory approvals, or (ii) the plan "expressly" notifies parties in interest that at the time of confirmation, those approvals have not yet been obtained. Section 1129(a)(6) therefore does not evidence any Congressional intent to abrogate federal or state regulation that protects nonbankruptcy interests.

Baker & Drake, 35 F.3d at 1354. All but a few of the regulations apply, at an absolute minimum, to all investor-owned public utilities in the State, including gas and electric utilities, water utilities, telecommunications utilities, and various transportation common carriers, not only PG&E. Moreover, most of the regulations apply to all public utilities, not just those which are investor-owned. In any event, there is no suggestion in *Baker & Drake* that a state regulation not of general applicability can necessarily be preempted. To the contrary, the focus in *Baker & Drake* was on whether the state regulation furthered public safety and welfare, and whether it directly conflicted with the Bankruptcy Code. *See also First Alliance*, 263 B.R. at 112.

Second, each of the regulations "is not just an economic regulation, but one reasonably intended to secure the public convenience and safety." *Id.* As explained in the Lynch Declaration, the state statutes and regulations that PG&E seeks to preempt not only are "reasonably intended" to secure public convenience and safety, they *directly* secure the State's sovereign police power to provide for the safety and welfare of its residents. (Lynch Decl. ¶¶ 25-55; *see supra* at 5.) At the very least, the state regulation at issue here no less secures public convenience and safety than the regulation which prohibited the debtor from leasing its taxicabs in *Baker & Drake*.

What is more, should PG&E succeed in preempting these statutes, the transactions proposed by PG&E would result in actual adverse effects to the safety and welfare of the public. As explained in the Lynch Declaration, the transactions PG&E proposes would have significant adverse effects to public health and safety, such as adverse environmental effects from the massive transfer of hydro and gas assets and nuclear facilities; the loss of in-state generation facilities that the State has determined, in its exercise of sovereign police power, are essential during the energy crisis and must remain dedicated to service for the benefit of the people of California; the potential that Commission will be unable to ensure the provision of basic service in the case of a supply or capacity crisis; the potential that the pricing of service for captive customers will undermine the availability of affordable service for California citizens and necessitate the widespread use of alternative fuels, thereby creating adverse impacts on the environment; and the adverse effects to the safety and welfare of California residents through the loss of local regulation. (Lynch Decl. ¶¶ 8, 11-13, 24, 33-34, 40-46, 48-57.)

And finally, none of the statutes or regulations "directly conflict[s] with the purposes of the Bankruptcy Code in any way which could be generalized beyond the particular facts of the present case." *Baker & Drake*, 35 F.3d at 1354-55; *see also First Alliance*, 263 B.R. at 112. The statutes and regulations are public health and safety regulations, not economic regulations. To be sure, in some sense *any* state regulation, even regulation directed solely at public safety and welfare, will have some adverse economic consequences, or otherwise could stand in the way of something that a debtor might want to do. But *Baker & Drake* requires (among other things) that the statute "*directly*" conflict with the purposes of the Bankruptcy Code before it can be preempted. Here, at the very least the regulations at issue here no more conflict with the purposes of Bankruptcy Code than the state regulation which prohibited the debtor from leasing its taxicabs in *Baker & Drake*.

2. The Extraordinary Scale of the Preemption Sought by PG&E, and the Fact That Preemption is the Central Purpose of the Proposed Plan, Further Demonstrate That the Proposed Plan is Unconfirmable

PG&E's proposed plan is a deregulation plan, not a reorganization plan. PG&E specifically indicates that it will not seek the approval of any California state or local government office or agency acting in a discretionary capacity, including the Commission. To be sure, upon confirmation of its proposed Plan, the reorganized PG&E (as distinct from the other Reorganized Entities) plans to engage exclusively in the business of retail distribution of gas and electricity, and to be subject to Commission regulation. But as we show immediately below, neither that fact, nor federal regulation of certain Reorganized Entities, even begins to fix the manifest defects of the proposed plan.

The centerpiece of PG&E's proposed plan is the massive and multi-billion dollar transfer of its critical generation and transmission assets to newly created entities *that, according to PG&E, will not be subject to regulation by the State of California*. (As we explain below, it is no answer for PG&E to point to federal regulation as an alleged substitute.) PG&E intends to make these critical transfers, moreover, without regard to the Commission's statutory obligation and authority to ensure that these transactions comport with state law and will not negatively impact the safety and welfare of the citizens of California. In short, the Plan is designed to use the bankruptcy laws to strip the Commission (and any other state agency) of jurisdiction over three of PG&E's four lines of business. Not only that, the three new entities pursuing those three lines of business, allegedly free from state regulation, will own and operate the very types of utility assets that generate the most intense local public safety and welfare concerns (such as power plants, dams, pipelines, and nuclear reactors) and that in the Commission's view should therefore remain subject to local oversight.

PG&E may contend that it has merely asked the Court to preempt the Commission's regulatory authority to review the restructuring transactions, but that the Commission will regain appropriate regulatory authority once the reorganization is complete. That would be a legally insufficient response, and in any event would not be accurate. By reorganizing in the manner contemplated, PG&E would transfer its "crown jewels" (the generation and transmission operations) to entities that PG&E contends will *never* be regulated by the Commission. PG&E would have *permanently* removed major portions of its business from Commission regulation.

The Commission respectfully submits that Congress could not possibly have intended section 1123(a)(5) to permit the result contemplated by PG&E here: the permanent self-deregulation of the bulk of the operations of a state-created public utility, without an iota of oversight by the Commission and against the sovereign will of the State. Under PG&E's proposed plan, the reorganized entities will operate hydroelectric and nuclear plants in California and transmit electricity and gas through a distribution network criss-crossing California; and the State of California will have absolutely no power to regulate or oversee any of it. This is especially objectionable in light of repeated Congressional indication that the states continue to have a critical role in the regulation of public utilities, even in light of federal regulation of those utilities, as we show immediately below.

3. The Preemptive Orders that PG&E Demands Would Frustrate Congressional Intent to Delegate Regulatory Authority to the States, and Leave Dangerous Gaps in the Regulatory Regime Applicable to the Reorganized PG&E Entities

To be sure, PG&E contends that the reorganized entities will remain subject to certain federal regulation, such as the Federal Power Act (the "FPA") and Natural Gas Act (the "NGA") which are overseen by FERC. *See* Am. Discl. St. at 126. Yet under PG&E's construction, section 1123(a)(5) must logically preempt (or at least be capable of preempting) all "nonbankruptcy" law, not just state law. Presumably, then, PG&E must believe that it could seek to avoid federal regulatory laws as well, should it conclude that those federal laws would make its proposed plan of reorganization more difficult. Some other debtor in some other state may prefer that state's regulation over federal regulation. If section 1123(a)(5) means what PG&E says it does, then such a debtor could use the section to avoid federal regulation. Indeed, because of the special presumptions insulating state law in areas of traditional state concern from federal preemption, it would arguably be slightly *more* rational to seek to displace federal regulation.

In any event, Congress cannot have intended to permit debtors to choose which regulatory regime they prefer and to ignore the other, or for that matter to seek preemption of both regimes. Federal law does not give a state-regulated public utility the right to restructure itself, in violation of state law, by divesting itself of operations potentially subject to federal regulation and placing those operations under actual federal, rather than state, regulation. To the contrary, federal law preserves state regulation of such a restructuring. As we show below, PG&E should not be able to achieve a different result by opportunistically exploiting its bankruptcy to frustrate the policies of highly important and technically complex federal and state regulatory law.

Furthermore, federal regulation is not an adequate substitute for state regulation on many levels, because for example, state regulation provides greater access for local citizens, businesses, and interest groups to participate in the process, and because the Commission's staff and employees has greater local expertise. (Lynch Decl. ¶¶ 56-57.) What is more, the preemptive relief PG&E demands would undermine Congressional intent to delegate enforcement authority to the states. Courts have repeatedly recognized the important role of state regulation of public utilities, and that federal law was meant to *supplement* and not to supplant state regulation of those utilities. The FPA and NGA were enacted to fill in the gaps not covered by state regulation, not to preempt the state. Generally, federal regulation has primarily if not solely concerned wholesale rates, leaving the remaining bulk of regulation to the states. *See Tracy*, 519 U.S. at 290-292; *Conn. Light & Power Co. v. Federal Power Comm'n*, 324 U.S. 515, 525 (1945) ("Progress of the [FPA] bill through various stages shows constant purpose to protect rather than to supervise authority of the states."); *Panhandle E. Pipe Line Co. v. Pub. Serv. Comm'n*, 332 U.S. 507, 517-518 (1947) (NGA "was drawn with meticulous regard for the continued exercise of state power, not to handicap or dilute it in any way.").

The federal regulatory regime that PG&E suggests might suffice to protect the public specifically depends on state regulation that would vanish under PG&E's plan. Notwithstanding that Congress declined to supplant state regulation of public utilities, PG&E would have this Court do just that.

The absence of state regulation would result in dangerous gaps in the regulatory regime applicable to the reorganized PG&E entities. To take but one example, PG&E is trying to avoid the state environmental review that the Commission would conduct under the California Environmental Quality Act ("CEQA"). Under Section 851 of the Public Utilities Code, PG&E has to obtain state approval to sell, lease, or spin off its utility facilities. An application under Section 851 triggers CEQA review. The massive reorganization contemplated by PG&E triggers CEQA, particularly in connection with the spin-off of PG&E's hydroelectric and nuclear facilities. PG&E owns the largest private system of hydroelectric facilities in the nation, consisting of 250 dams and diversions, 99 reservoirs, 68 powerhouses, and 140,000 acres of associated lands. (Lynch Decl. ¶ 9.) Moreover, the disaggregation of a vast hydroelectric system raises significant environmental issues, many of which were identified in the draft environmental impact report prepared when PG&E tried, prepetition, to divest its hydro assets. (*Id.* ¶ 9 & Ex. A.) Similarly, pressing environmental concerns would be raised by PG&E's

proposed spin-off of its Diablo Canyon nuclear power plant. Under PG&E's Plan, however, there would be no environmental review of the spin-off of either its hydro or nuclear generation facilities.

Even if PG&E's proposed transactions were subject to federal regulation, that regulation is less protective of local residents in many instances. For example, FERC uses a "public interest" test that considers certain economic concerns, but not necessarily environmental concerns. *See* Am. Discl. St. Ex. G at 1-2 (no mention of environmental review under FPA). In addition, FERC review under the National Environmental Policy Act ("NEPA"), if it occurs, would likely result in less environmental protection than Commission review under CEQA. *See City of Carmel-by-the-Sea v. U.S. Dep't of Transp.*, 123 F.3d 1142, 150 (9th Cir. 1997) (NEPA's requirements are procedural whereas CEQA's requirements are both procedural and substantive). And finally, PG&E's proposed spin-off of its utility-retained generation ("URG") into Limited Liability Corporations creates an equally large regulatory gap. These new LLCs are removed entirely from regulation. FERC does not regulate generation. *See, e.g., San Diego Gas & Elec. Co. v. Sellers of Energy & Ancillary Servs.*, 93 FERC ¶ 61,294 (2000).

Finally, the Commission has special authority that allow for diversion of gas supplies to captive core customers in emergencies. *See* Cal. Pub. Util. Code. § 739. Such emergency powers to protect the safety and welfare of California citizens would not be available under FERC regulation. Furthermore, the intrastate gas transmission system is closely integrated with the local gas distribution system, and under FERC regulation, this integration will be seriously impaired, interfering with the Commission's ability to protect the health and safety of captive core customers. California ratepayers have paid for the construction of PG&E's intrastate gas transmission system which was built to serve California gas customers. PG&E has an obligation to serve under Commission regulation. Under FERC regulation, there would be no obligation to serve, and captive core customers would lose most of their current rights and protections.

II.

PG&E'S PROPOSED PLAN IS UNCONFIRMABLE BECAUSE IT DEMANDS RELIEF AGAINST THE STATE OF CALIFORNIA THAT IS BARRED BY THE ELEVENTH AMENDMENT AND RELATED PRINCIPLES OF SOVEREIGN IMMUNITY

The doctrine of sovereign immunity embodied in the Eleventh Amendment forbids a federal court from exercising original jurisdiction over claims brought by private plaintiffs against a state or its agencies. *See Edelman v. Jordan*, 415 U.S. 651, 662-63 (1974). Eleventh Amendment immunity "serves to avoid 'the indignity of subjecting a State to the coercive process of judicial tribunals at the instance of private parties.'" *Seminole Tribe v. Florida*, 517 U.S. 44, 58 (1996) (citation omitted). The Eleventh Amendment absolutely bars an action by a private plaintiff in federal court directly against an unconsenting state (or an unconsenting state agency, such as the Commission) regardless of the relief requested.[13]

PG&E demands sweeping and unprecedented declaratory, injunctive, and monetary relief that the Commission and the State of California cannot enforce, against PG&E, not less than fifteen important state regulatory statutes aimed at promoting the safety and welfare of California citizens. These demands are aimed specifically and purposefully at the

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[13] *See Pennhurst State Sch. & Hosp. v. Halderman*, 465 U.S. 89, 100 (1984); *Alabama v. Pugh*, 438 U.S. 781 (1978) (per curiam); *In re Lazar*, 237 F.3d 967, 975-76 (9th Cir. 2001); Richard H. Fallon et al., *Hart and Wechsler's The Federal Courts and the Federal System* 1073 (4th ed. 1996).

Section 106(a) of the Bankruptcy Code purports to abrogate state sovereign immunity with respect to sections 105 and 362 of the Bankruptcy Code. Section 106(a) is unconstitutional in light of the Supreme Court's decision in *Seminole Tribe* that Congress may not abrogate a state's Eleventh Amendment immunity from suit in federal court pursuant to Congress's powers under Article I of the Constitution. *See Mitchell v. Franchise Tax Bd.*, 209 F.3d 1111, 1119 (9th Cir. 2000) ("Section 106(a) has been viewed by most courts addressing the issue as having been passed pursuant to the Bankruptcy Clause of Article I"), *aff'g* 222 B.R. 877, 881 (9th Cir. BAP 1998) ("§ 106(a) is ineffective to abrogate the State's Eleventh Amendment sovereign immunity") (citation omitted; collecting cases); *accord Sacred Heart Hosp. v. Pa. Dep't of Pub. Welfare*, 133 F.3d 237, 245 (3d Cir. 1998); *Dep't of Transp. & Dev. v. PNL Asset Management Co. LLC (In re Estate of Fernandez)*, 123 F.3d 241, 242 (5th Cir. 1997); *Schlossberg v. Maryland (In re Creative Goldsmiths of Washington, D.C., Inc.)* 119 F.3d 1140, 1147 (4th Cir. 1997).

Commission and the State in their capacities as a sovereign regulator, not as ordinary creditors. Moreover, PG&E's demands for relief seek to bar the Commission and the State from exercising sovereign powers that are absolutely fundamental to the State's regulatory authority over PG&E, a public utility, and consequently to the safety and welfare of the citizens of California. PG&E demands that this Court authorize a fundamental and permanent restructuring of its business as a public utility, without any oversight by the Commission or the State to ensure that the restructuring is consistent with state law and appropriately protects public safety and welfare, as those interests are defined under state law and enforced by the State and its agencies.

PG&E also asks for relief that would excuse it, after completion of the proposed reorganization, from compliance with fundamental features of California regulatory law. In particular, PG&E asks that this Court, in substance, enjoin the Commission and the State from enforcing California law that requires PG&E to purchase electricity sufficient to serve consumers in PG&E's service area. Instead, PG&E wants to use this Court to write a substitute statute placing conditions and limitations without any basis in California law on PG&E's duty, as a regulated utility, to serve. The Eleventh Amendment bars PG&E's effort to enjoin the State of California from enforcing basic California regulatory law.

As we show below, the relief that PG&E seeks in its proposed plan against the Commission and the State of California is barred by the Eleventh Amendment and related principles of sovereign immunity.

A. The Court Should Look to the Substance of the Relief Sought by PG&E in its Plan to Determine Whether the Relief is a "Suit" Against the State for Purposes of the Eleventh Amendment

PG&E chose to seek declaratory and injunctive relief against the Commission and the State of California in a chapter 11 plan, rather than in an adversary proceeding. (As we show below, PG&E also impermissibly seeks the functional equivalent of monetary relief.) Had PG&E attempted to obtain the relief it now seeks in an adversary proceeding, that relief would be barred by the Eleventh Amendment. *See Mitchell v. Franchise Tax Bd.*, 209 F.3d 1111, 1116-17 (9th Cir. 2000). That relief is equally barred if sought by way of a plan. The Eleventh

Amendment prohibition on requests for relief against a State encompasses, but extends beyond, requests contained in formal lawsuits or adversary proceedings against a State as a named party. Rather, the Supreme Court has [broadly] defined a "suit" barred by the Eleventh Amendment as "the prosecution, or pursuit, of some claim, demand, *or request* . . . in a court of justice." *Cohens v. Virginia*, 19 U.S. (6 Wheat) 264, 407 (1821) (emphasis added).

In keeping with the general rule that state sovereignty cannot be abrogated through technical evasions and artful pleading, courts take a practical view of what constitutes the prosecution or pursuit "of some claim, demand, or request" against a State. In making such a determination, courts look to "the essential nature and effect of the proceeding." *Ford Motor Co. v. Dep't of Treasury*, 323 U.S. 459, 464 (1945); *accord In re New York*, 256 U.S. 490, 500 (1921). *Cf. Ulaleo v. Paty*, 902 F.2d 1395, 1399 (9th Cir. 1990) (court should look to "the substance not the form of the relief"). If the "essential nature and effect of the proceeding" is the pursuit "of some claim, demand, or request" against a State, then that proceeding is a "suit" against the State for purposes of the Eleventh Amendment.

In the bankruptcy context, the Ninth Circuit has held that earmarks of a "suit" include the application of coercive process and the attempt to invoke the court's *in personam* jurisdiction over the state. *See Goldberg v. Ellet (In re Ellett)*, 254 F.3d 1135, 1139 (9th Cir. 2001) (citing *Mitchell*, 209 F.3d at 1117). Similarly, the Fourth Circuit has articulated the "test" in terms of both procedural and substantive elements, as follows:

> As to the case's procedural posture, two issues are important: first, the degree of coercion exercised by the federal court in compelling the state to attend; and second, whether the resolution, or the remedy, would require our jurisdiction over the state. The substantive consideration focuses upon whether the action was, as stated by Chief Justice Marshall, "the prosecution of some demand in a Court of justice," as opposed to the orderly disposition of an estate, with the states' role limited to that of any other creditor.

In re NVR, LP, 189 F.3d 442, 452 (4th Cir. 1999) (citing *Cohens*, 19 U.S. at 407 and *Ford Motor*, 323 U.S. at 464).

As we show below, the relief PG&E seeks against the State of California in its bankruptcy plan would require the State to pay huge sums of money that PG&E should fund; is specifically directed against the State of California as a sovereign regulator; and requires exercise of *in personam* jurisdiction over the State. The "essential nature and effect" of the relief PG&E demands in its plan clearly constitutes the pursuit "of some claim, demand, or request" against the State, and is therefore a "suit" barred under the Eleventh Amendment and related principles of sovereign immunity.

B. The "Essential Nature and Effect" of the Relief Demanded by PG&E Involves the Pursuit of a "Claim, Demand, or Request" Against the State, and Such Relief Is Therefore Barred by the Eleventh Amendment

1. The Relief that PG&E Requests Would Require Payment of Money by the State

The quintessential form of relief barred by the Eleventh Amendment, regardless of whether that relief is sought in an adversary proceeding or in a plan, is relief that requires the payment of money by the state. *See Mitchell*, 209 F.3d at 1116-17.

Here, PG&E demands (among other things) that it be exempted from its statutory obligation to fund the net open position to provide sufficient electric power to serve the public. Under California law, an electric utility operating as a monopoly, such as PG&E, has a fundamental "duty to serve" to provide electricity at all times to every ratepayer within its service area. (*Supra* at 5 & n.2.) If demand for power by ratepayers exceeds a utility's generation capacity, the utility must purchase and pay for that power from wholesale suppliers. To avert a disastrous statewide power shortage, the State authorized DWR to purchase electricity to cover the shortfall on behalf of PG&E, known as the "net open position," when PG&E became unable to meet the needs of the customers in its service territory. The legislation authorizing DWR to procure power to satisfy the net open position provides that "[n]othing in this division shall be construed to reduce or modify any electrical corporation's obligation to serve." Cal. Water Code § 80002. The cost to DWR to purchase this power and to fund the net open position has run into the billions of dollars and is increasing.[14]

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[14] The legislation permits DWR to recover those costs from ratepayers. *See* Assembly Bill ABX1 1, Stats. 2001, Ch. 4, as codified at Division 27 of the California Water Code, Section 80002 *et seq.* The administrative and financial burden on the State of having to procure power for PG&E's customers and to fund those activities are nevertheless substantial. In any event, it makes no difference whether the State may ultimately be able to collect the

The obligation to purchase this power, and to pay for it, are obligations of PG&E and should be borne by PG&E. They flow directly from PG&E's fundamental obligation as a public utility to serve its customers. Nevertheless, DWR paid the bill for the additional power and is still paying the bill for additional power. Even now, as power costs have relaxed to the point where PG&E's revenues are again exceeding costs, PG&E seeks to avoid having to assume the net open position. PG&E seeks relief in its proposed plan that would prevent PG&E from assuming the net open position—and, as a practical matter, would thus require DWR to continue paying—until PG&E's self-created "wish list" of conditions is met.

Not only is PG&E demanding that the Court usurp the sovereign regulatory authority of the State to determine the nature and conditions of PG&E's fundamental state obligation to serve, which is a violation of the Eleventh Amendment on its own, PG&E is effectively trying to stick the State with a bill that PG&E, under California law, should have to pay. To be sure, PG&E does not overtly demand that the State pay PG&E. Such a demand would obviously be barred by the Eleventh Amendment. *See Mitchell*, 209 F.3d at 1116-17. Rather, PG&E demands that the State pay third-party power generators on behalf of PG&E. That is a distinction without a difference, and especially where the focus is on the substance and not the form or technicalities of the relief requested.

PG&E attempts to phrase the relief it seeks in connection with the net open position as an injunction against itself. According to PG&E, the Court should order that the reorganized PG&E "will be prohibited from reassuming the net open position of its electric customers until [certain] conditions are met . . . ." (Am. Discl. St. at 112.) But regardless of how PG&E describes the relief requested—regardless, in other words, of whether PG&E asks the Court to order the State to pay the costs of the net open position, or tries to obscure reality by asking the Court to "prohibit" PG&E from complying with its duty under California law to fund

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payments it has made in connection with the net open position, either from taxpayers, ratepayers, or some other entity. *See Regents of the University of Cal. v. Doe*, 519 U.S. 425, 431 (1997) ("The Eleventh Amendment protects the State from the risk of adverse judgments even though the State may be indemnified by a third party.").

the position—the relief PG&E seeks would require the State to continue paying huge sums of money for PG&E. PG&E's highly artificial formulation of the relief it demands only shows how hard PG&E must struggle in its effort to obscure the utter incompatibility of its proposed plan with the Eleventh Amendment.

2. <u>PG&E Demands Affirmative Relief Specifically Directed Against the State of California As a Sovereign Regulator</u>

Whether or not a request for relief would require the payment of money by the State, a request for relief against a State nonetheless constitutes a "suit" against the State for purposes of the Eleventh Amendment if that request presents "some demand" against the State in any capacity other than as an ordinary creditor. *See NVR*, 189 F.3d at 452 (to determine whether a demand for relief is a "suit" under the Eleventh Amendment, the court should consider whether the demand is "'the prosecution of some demand in a Court of justice,' as opposed to the orderly disposition of an estate, with the states' role limited to that of any other creditor") (quoting *Cohens*, 19 U.S. at 407.

Here, PG&E makes just such "demands" against the Commission and the State of California. In fact, the relief PG&E demands in its plan could not be any more specifically directed against the State and its sovereign regulatory authority. As shown in the accompanying Lynch Declaration, the state statutes, regulations, and regulatory authority that PG&E seeks to displace protect important state sovereignty interests in providing for the safety and welfare of California citizens. (Lynch Decl. ¶¶ 25-55.) PG&E demands that the Court order that the Commission and the State are barred from fulfilling their sovereign missions as public regulators—both here and now during PG&E's bankruptcy and on an ongoing basis after PG&E emerges from chapter 11, should a plan ever be confirmed.

The Commission's position here is fully consistent with cases such as *Texas v. Walker*, 142 F.3d 813 (5th Cir. 1998). There, a debtor obtained a discharge order, and the State of Texas subsequently sued to collect a prepetition debt. The Fifth Circuit held that the Eleventh Amendment did not bar the debtor from asserting the discharge order as a defense to the State's claim. *Walker* carefully explained, however, that this result followed from the bankruptcy court's limited *in rem* jurisdiction over the bankruptcy estate. *See id.* at 822 (explaining that "the power of the bankruptcy court to enter an order confirming a plan . . . derives not from jurisdiction over the state or other creditors, but rather from jurisdiction over debtors and their estates") (quotations omitted). The Supreme Court has explained the limitations on the bankruptcy court's *in rem* jurisdiction:

> he who invokes the aid of the bankruptcy court by offering a proof of claim and demanding its allowance must abide by the consequences of that procedure. If the claimant is a State, the procedure of proof and allowance is not transmitted into a suit against the State because the court entertains objections to the claim. *The State is seeking something from the debtor. No judgment is sought against the State.* The whole process of proof, allowance, and distribution is, shortly speaking, an adjudication of interests claimed in a res. It is none the less such because the claim is rejected in toto, reduced in part, given a priority inferior to that claimed, or satisfied in some way other than payment in cash.

Gardner v. New Jersey, 329 U.S. 565, 573-74 (1947) (citation omitted, emphasis added); *see Goldberg*, 254 F.3d at 1140-41.

PG&E's demands for relief against the Commission and State here are entirely different. In the challenged provisions of the proposed plan, PG&E is not attempting to obtain a general discharge order, pursuant to this Court's *in rem* jurisdiction, that might then affect some claim for money by the Commission or the State against PG&E. It cannot be said here, as the Supreme Court said in *Gardner*, that "[t]he State is seeking something from the debtor." Nor can it be said here, as the Fourth Circuit said in describing certain permissible consequences of reorganization plans, that "the [State's] role [is] limited to that of any other creditor." *In re NVR*, 189 F.3d at 452. Rather, PG&E is seeking something extraordinary against the State: affirmative relief *directed specifically against the Commission and the State* as sovereigns that goes beyond any reasonable understanding of this Court's *in rem* jurisdiction, and that purports to bar the Commission and the State from exercising their regulatory authority over PG&E. Such a demand for relief against an unconsenting State is barred by the Eleventh Amendment.

3. The Relief that PG&E Requests Would Require the Court to <u>Exercise *In Personam* Jurisdiction Over the State of California</u>

PG&E's demand for relief in its proposed plan is barred by the Eleventh Amendment for a related but additional reason. A request for relief against a State constitutes a "suit" against the State for purposes of the Eleventh Amendment if adjudication of that request requires the exercise of personal jurisdiction over the State. *See Goldberg*, 254 F.3d at 1139; *Mitchell*, 209 F.3d at 1117; *NVR*, 189 F.3d at 452. Here, the relief PG&E demands would require the Court to assert personal jurisdiction over the State of California.

As explained above, the relief demanded by PG&E is not like the relief that may be granted in connection with the bankruptcy court's *in rem* jurisdiction over PG&E's estate. PG&E's demands for relief do not involve adjudication of any claim by the Commission or the State *as a creditor* for a share of the property of the estate. Rather, PG&E's demands are specifically directed at the State *as a sovereign* and seek to adjudicate claims that PG&E purports to have against the State. These demands do not involve the disposition of any property of the estate in the sense of who gets what, or the adjustment of debtor-creditor relationships with respect to that property. The demands are not primarily directed to adjudicating rights and interests in property of the estate. For these reasons, the Court's *in rem* jurisdiction over the property of the estate does not confer authority on the Court to order the State to take or not to take certain actions in connection with its sovereign regulatory authority, as PG&E has demanded. In order to bind the State in the way PG&E has demanded, the Court would have to exercise personal jurisdiction over the Commission and the State.

The *NVR* case is instructive here. In that case, the Fourth Circuit held that a motion for relief by contested matter was a "suit" against the State, and thus barred by the Eleventh Amendment, because the relief requested would be little more than an advisory opinion in the absence of personal jurisdiction over the State. *See NVR*, 189 F.3d at 453. As in *NVR*, here "[t]he real value of the judicial pronouncement—what makes it a proper judicial resolution of a 'case or controversy' rather than an advisory opinion—is in the settling of some dispute which affects the behavior of the [State] towards [PG&E]." *Id.* (quoting *Hewitt v. Helms*, 482 U.S. 755, 761 (1987)). Such a "judicial pronouncement" respecting the conduct of the State, the *NVR* court held, is barred by the Eleventh Amendment.

C. Neither the Commission Nor the State Has Waived Its Sovereign Immunity

PG&E has not contended in this Court that the Commission or the State has waived its sovereign immunity. PG&E, however, took the position during its appeal of this Court's decision to dismiss its adversary proceeding against the Commission and its Commissioners that the Commission has waived its sovereign immunity. PG&E is wrong.

On appeal, PG&E contended that the Commission had waived its sovereign immunity because state agencies had filed proofs of claim in the bankruptcy proceeding and because state agencies had "participated" in the chapter 11 case. If PG&E chooses to make those arguments to this Court, they should be rejected for the reasons set forth in the Commission's memorandum on appeal. (Ex. B hereto.)

CONCLUSION

For the foregoing reasons, the Commission respectfully submits that the Court should not approve PG&E's proposed disclosure statement because the statement describes a plan that is unconfirmable on its face.

Dated: January 8, 2002

Respectfully,

GARY M. COHEN
OFFICE OF THE GENERAL COUNSEL,
CALIFORNIA PUBLIC UTILITIES COMMISSION

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Attorneys for Defendants/Appellees/Cross-Appellants

EXHIBIT A

EXHIBIT A

LEGISLATIVE HISTORY APPENDIX

TAB 1

96TH CONGRESS 2d Session } HOUSE OF REPRESENTATIVES { REPORT No. 96-1195

AN ACT TO CORRECT TECHNICAL ERRORS, CLARIFY AND MAKE MINOR SUBSTANTIVE CHANGES TO PUBLIC LAW 95-598

JULY 25, 1980.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. RODINO, from the Committee on the Judiciary, submitted the following

REPORT

together with

DISSENTING VIEWS

[To accompany S. 658]

The Committee on the Judiciary, to whom was referred the bill (S. 658) to correct technical errors, clarify and make minor substantive changes to Public Law 95-598, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment to the text of the bill is a complete substitute therefor and appears in italic type in the reported bill.

INTRODUCTION

The Bankruptcy Reform Act of 1978 has now been in effect less than one year. It is clear even at this early time in the life of this law that technical amendments are required. Errors in printing, spelling, punctuation, grammar, syntax, and numeration arose in the bill as enacted because of the last-minute process of change through which the bill went when considered at the closing sessions of the 95th Congress.

These same last-minute changes also resulted in the enactment of a bill that contains incongruent provisions; material that was removed from earlier versions remained as either cross-references or antecedents for provisions changed or inserted. And, material added often was not completely integrated into the total fabric of the bill as enacted.

periods specified in subsection (c) of this section **and after notice and a hearing, the court may for cause reduce or increase the 120-day period or the 180-day period referred to in this section.**

* * * * * * *

§ 1123. Contents of plan

(a) [A] *Notwithstanding any otherwise applicable nonbankruptcy law, a* plan shall—

(1) designate, subject to section 1122 of this title, classes of claims, other than claims of a kind specified in section 507(a)(1), 507(a)(2), or 507(a)(6) of this title, and classes of interests;

(2) specify any class of claims or interests that is not impaired under the plan;

(3) [shall] specify the treatment of any class of claims or interests that is impaired under the plan;

(4) provide the same treatment for each claim or interest of a particular class, unless the holder of a particular claim or interest agrees to a less favorable treatment of such particular claim or interest;

(5) provide adequate means for the plan's [execution] *implementation*, such as—

(A) retention by the debtor of all or any part of the property of the estate;

(B) transfer of all or any part of the property of the estate to one or more entities, whether organized before or after the confirmation of such plan;

(C) merger or consolidation of the debtor with one or more persons;

(D) sale of all or any part of the property of the estate, either subject to or free of any lien, or the distribution of all or any part of the property of the estate among those having an interest in such property of the estate;

(E) satisfaction or modification of any lien;

(F) cancellation or modification of any indenture or similar instrument;

(G) curing or waiving *of* any default;

(H) extension of a maturity date or a change in an interest rate or other term of outstanding securities;

(I) amendment of the debtor's charter; or

(J) issuance of securities of the debtor, or of any entity referred to in subparagraph (B) or (C) of this paragraph, for cash, for property, for existing securities, or in exchange for claims or interests, or for any other appropriate purpose;

(6) provide for the inclusion in the charter of the debtor, if the debtor is a corporation, or of any corporation refered to in paragraph (5)(B) or (5)(C) of this subsection, of a provision prohibiting the issuance of nonvoting [equity securities] *common stock* and providing, as to the several classes of securities possessing voting power, an appropriate distribution of such power among such classes, including, in the case of any class of equity securities having a preference over another class of equity securi-

ties with respect to dividends, adequate provisions for the election of directors representing such preferred class in the event of default in the payment of such dividends; and

(7) contain only provisions that are consistent with the interests of creditors and equity security holders and with public policy with respect to the manner of selection of any officer, director, or trustee under the plan and any successsor to such officer, director, or trustee.

(b) Subject to subsection (a) of this section, a plan may—

(1) impair or leave unimpaired any class of claims, secured or unsecured, or of interests;

(2) subject to section 365 of this title, provide for the assumption [or rejection], *rejection, or assignment* of any executory contract or unexpired lease of the debtor not previously rejected under *such* section [365 of this title];

(3) provide for—

(A) the settlement or adjustment of any claim or interest belonging to the debtor or to the estate; or

(B) the retention and enforcement by the debtor, by the trustee, or by a representative of the estate appointed for such purpose, of any such claim or interest;

(4) provide for the sale of all or substantially all of the property of the estate, and the distribution of the proceeds of such sale among holders of claims or interests; and

(5) include any other appropriate provision not inconsistent with the applicable provisions of this title.

(c) In a case concerning an individual, a plan proposed by an entity other than the debtor may not provide for the use, sale, or lease of property exempted under section 522 of this title, unless the debtor consents to such use, sale, or lease.

§ 1124. Impairment of claims or interests

Except as provided in section 1123(a)(4) of this title, a class of claims or interests is impaired under a plan unless, with respect to each claim or interest in such class, the plan—

(1) leaves unaltered the legal, equitable, and contractual rights to which such claim or interest entitles the holder of such claim or interest;

(2) notwithstanding any contractual provision or applicable law that entitles the holder of such claim or interest to demand or receive accelerated payment of such claim or interest after the occurrence of a default—

(A) cures any such default [.] *that occurred before or after the commencement of the case under this title*, other than a default of a kind specified in section 365(b)(2) of this title [, that occurred before or after the commencement of the case under this title];

(B) reinstates the maturity of such claim or interest as such maturity existed before such default;

(C) compensates the holder of such claim or interest for any damages incurred as a result of any reasonable reliance by such holder on such contractual provision or such applicable law; and

TAB 2

96TH CONGRESS } HOUSE OF REPRESENTATIVES { REPORT
2d Session } { No. 96-1195

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These same last-minute changes also resulted in the enactment of a bill that contains incongruent provisions; material that was removed from earlier versions remained as either cross-references or antecedents for provisions changed or inserted. And, material added often was not completely integrated into the total fabric of the bill as enacted.

Section 100(a). This amendment makes several stylistic changes.

Subsection (b). This amendment makes it clear that the character of cause justifying the court's converting a case under chapter 11 to a case under chapter 7 includes a denial of additional time for filing a plan where such has been requested; and makes it clear that time limitations are in a correlative not conjunctive relationship with each other.

Section 101(a). This amendment makes a stylistic change.

Subsection (b). This amendment makes it clear that changes in the times for filing a plan under section 1121(c) can be made by the court only if the request for such a change is made within the time specified for each circumstance.

Section 102(a). This amendment makes it clear that the rules governing what is to be contained in the reorganization plan are those specified in this section; deletes a redundant word; and makes several stylistic changes.

Subsection (b). This amendment makes a conforming change; and deletes a redundant cross-reference.

Section 103. This amendment makes a stylistic change; and makes it clear that time period limitations are in a correlative not conjunctive relationship with each other.

Section 104(a). This amendment makes it clear that the requirement of providing adequate information about the plan does not include information about other plans which may be proposed; and makes several stylistic changes.

Subsection (b). This amendment makes it clear that the disclosure statement which is not subject to otherwise applicable nonbankruptcy law is the statement required by this section; and that the approval of such a statement is not subject to review other than through the process of approval required hereunder.

Subsection (c). This amendment makes it clear that the solicitation that is protected by the safe harbor provision is that of acceptances and rejections of the plan.

Section 105(a). This amendment makes a stylistic change.

Subsection (b). This amendment corrects an error in punctuation.

Subsection (c). This amendment corrects several errors in spelling.

Subsection (d). This amendment makes a stylistic change.

Section 106(a). This amendment makes several stylistic changes.

Subsection (b). This amendment makes a stylistic change.

Section 107(a). This amendment makes it clear that a plan may not be confirmed unless it and its proponent comply with, inter alia, all applicable provisions of title 11; makes several stylistic changes; and corrects a spelling and a punctuation error.

Subsection (b). This amendment deletes an erroneous cross-reference; makes several stylistic changes; makes it clear in the application of the absolute priority rule regarding the holders of unsecured claims that junior claim or interest holders may not receive or retain property under the plan unless those senior to them have been appropriately dealt with; and makes it clear that in determining the value of property interest holders must receive, such value may be based upon one or the other of the standards provided for in section 1129(b)(2)(C)(i).

TAB 3

3

Bankruptcy Law Reports

NUMBER 30 NOVEMBER 20, 1980 PART II

TECHNICAL AMENDMENTS TO BANKRUPTCY REFORM ACT OF 1978

Text of House Report No. 96-1195, Parts 1 and 2, as reported by the House Committee on the Judiciary; and Text of S. 658 as passed by the House with comments.

Extra copies are available from Commerce Clearing House, Inc., 4025 W. Peterson Ave., Chicago, Illinois 60646. Price: 1-4 Copies, \$2.50 each; 5-9 Copies, \$2.20 each; 10-24 Copies, \$2.00 each; 25-49 Copies, \$1.80 each.

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CORRECTING TECHNICAL ERRORS AND MAKING MINOR SUBSTANTIVE CHANGES TO PUBLIC LAW 95-598

Mr. EDWARDS of California. Mr. Speaker, I move to suspend the rules and pass the Senate bill (S. 658), to correct technical errors, clarify and make minor substantive changes to Public Law 95-598, as amended.

The Clerk read as follows:

S. 658

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled,

TITLE I—AMENDMENTS TO TITLE 11 OF THE UNITED STATES CODE

SECTION 1. (a) Section 101(2)(D) of title 11 of the United States Code is amended by striking out "or all" immediately after "business".

(b) Section 101(8)(B) of title 11 of the United States Code is amended by striking out the colon at the end thereof and inserting a semicolon in lieu thereof.

(c) Section 101(9)(B) of title 11 of the United States Code is amended by inserting "348(d), 502(e)(2)," immediately after "section".

(d) Section 101(14) of title 11 of the United States Code is amended by inserting "and" immediately after "trust,".

(e) Section 101(24) of title 11 of the United States Code is amended by striking out "stock broker" and inserting "stockbroker" in lieu thereof.

(f) Section 101(26)(B) of title 11 of the United States Code is amended—

(1) in clause (i), by striking out "the kind specified in subparagraph (A)(i) of this paragraph; and" and inserting "a kind specified in subparagraph (A)(i) of this paragraph; or" in lieu thereof; and

(2) in clause (ii) by striking out "separate" each place it appears and inserting "nonpartnership" in lieu thereof and by striking out "the kind specified in subparagraph (A)(ii)" and inserting "a kind specified in subparagraph (A)(i) or (A)(ii)" in lieu thereof.

(g) Section 101 of title 11 of the United States Code is amended—

(1) by redesignating paragraphs (35), (36), (37), (38), (39), and (40) as paragraphs (36), (37), (38), (40), (41), and (42) respectively; and

(2) by adding immediately after paragraph (34) the following new paragraph:

"(35) 'securities clearing agency' means person that is registered as a clearing agency under section 17A of the Securities Exchange Act of 1934 (15 U.S.C. 78q-1), or whose business is confined to the performance of functions of a clearing agency with respect to 'exempted securities', as defined in section 3(12) of such Act (15 U.S.C. 78c(12)) for the purposes of such section 17A;".

(h) Section 101(36)(A)(xii) of title 11 of the United States Code, as so redesignated, is amended by striking out "is the subject of a registration statement" and inserting "is required to be the subject of a registration statement" in lieu thereof.

(i) Section 101(36)(B)(iii) of title 11 of the United States Code, as so redesignated, is amended by striking out "commodity" the second place it appears.

(j) Section 101(36)(B)(vi) of title 11 of the United States Code, as so redesignated, is amended—

(1) by striking out "certificate specified in clause (xii) of subparagraph (A)" and inserting "certificate of a kind specified in subparagraph (A)(xii)" in lieu thereof; and

(2) by striking out "the subject of such a registration statement" and inserting "required to be the subject of a registration statement" in lieu thereof.

(k) Section 101 of title 11 of the United States Code is amended by inserting immediately after paragraph (38), as so redesignated, the following new paragraph:

"(39) 'State' includes the District of Columbia and Puerto Rico, except for the purpose of who may be a debtor under chapter 9 of this title;".

(l) Section 101(41) of title 11 of the United States Code, as so redesignated, is amended to read as follows:

"(41) 'stockbroker' means person—

"(A) with respect to which there is a customer, as defined in section 741 of this title; and

"(B) that is engaged in the business of effecting transactions in securities—

"(i) for the account of others; or

"(ii) with members of the general public, from or for such person's own account;".

(m) Section 101(42) of title 11 of the United States Code, as so redesignated, is amended by striking out the period and inserting "; and" in lieu thereof.

(n) Section 101 of title 11 of the United States Code is amended by adding at the end thereof the following new paragraph:

"(43) 'United States', when used in a geographical sense, includes all locations where the judicial jurisdiction of the United States extends, including territories and possessions of the United States.".

SEC. 2. Section 102(8) of title 11 of the United States Code is amended by striking out "continued" and inserting "contained" in lieu thereof.

SEC. 3. (a) Section 103(c) of title 11 of the United States Code is amended by striking out "stockholder" and inserting "stockbroker" in lieu thereof.

(b) Section 103(d) of title 11 of the United States Code is amended by striking out "except with respect to section 746(c) which applies to margin payments made by

United States Code is amended by striking out "estate, and" and inserting "estate and of the" in lieu thereof.

SEC. 96. Section 1106(b) of title 11 of the United States Code is amended by inserting ", except to the extent that the court orders otherwise," immediately before "any other".

SEC. 97. Section 1107(a) of title 11 of the United States Code is amended by inserting "serving in a case" immediately after "on a trustee".

SEC. 98. Section 1108 of title 11 of the United States Code is amended by inserting ", on request of a party in interest and after notice and a hearing," immediately after "court".

SEC. 99. Section 1111(b) of title 11 of the United States Code is amended to read as follows:

"(b)(1) Except where property of the estate that secures a claim is sold subject to section 363(k) of this title, abandoned under section 554 of this title, or surrendered to the holders of such claims, or is to be sold, abandoned, or surrendered under the plan—

"(A) a claim secured by such property shall be allowed or disallowed under section 502 of this title the same as if the holder of such claim had recourse against the debtor on account of such claim, whether or not such holder had such recourse, unless the class of which such claim is a part elects, by at least two-thirds in amount and more than one-half in number of allowed claims of such class, to be governed by subparagraph (B) of this paragraph; and

"(B) unless the aggregate value of the interests in such property of the holders of such claims is inconsequential, the class may elect, as provided under subparagraph (A) of this paragraph, that such claims of such class, whether or not the holders of such claims had recourse against the debtor and notwithstanding section 506(a) of this title, are secured claims to the full extent that such claims are allowed.

"(2) The provisions of paragraph (1)(A) of this subsection are limited to the purposes of this chapter and such paragraph does not in any other way alter, affect, or create any right or liability of any other entity.".

SEC. 100. (a) Section 1112(a) of title 11 of the United States Code is amended—

(1) in paragraph (2), by striking out "is an involuntary case originally commenced under this chapter" and inserting "originally was commenced as an involuntary case under this chapter" in lieu thereof; and

(2) in paragraph (3), by striking out "on other than" and inserting "other than on" in lieu thereof.

(b) Section 1112(b) of title 11 of the United States Code is amended—

(1) in paragraph (5), by inserting "a request made for" immediately before "additional"; and

(2) in paragraph (8), by striking out "and" inserting "or" in lieu thereof.

SEC. 101. (a) Section 1121(c)(3) of title 11 of the United States Code is amended by striking out "the claims or interests of which are" and inserting "of claims or interests that is" in lieu thereof.

(b) Section 1121(d) of title 11 of the United States Code is amended by inserting "made within the respective periods specified in subsection (c) of this section" immediately after "interest".

SEC. 102. (a) Section 1123(a) of title 11 of the United States Code is amended—

(1) by striking out "A" and inserting "Notwithstanding any otherwise applicable nonbankruptcy law, a" in lieu thereof;

(2) in paragraph (1), by inserting a comma immediately after "classes of claims" and immediately after "507(a)(6) of this title";

(3) in paragraph (3), by striking out "shall";

(4) in paragraph (5), by striking out "execution" and inserting "implementation" in lieu thereof;

(5) in paragraph (5)(G), by inserting "of" immediately after "waiving"; and

(6) in paragraph (6), by striking out "equity securities" the first place it appears and inserting "common stock" in lieu thereof.

(b) Section 1123(b)(2) of title 11 of the United States Code is amended by striking out "or rejection" and inserting ", rejection, or assignment" in lieu thereof and by striking out "under section 365 of this title" and inserting "under such section" in lieu thereof.

SEC. 103. Section 1124 of title 11 of the United States Code is amended—

(1) by amending paragraph (2)(A) to read as follows:

"(A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title;"; and

(2) in paragraph (3)(B)(i), by striking out "and" and inserting "or" in lieu thereof.

SEC. 104. (a) Section 1125(a) of title 11 of the United States Code is amended—

(1) in paragraph (1), by inserting ", but need not include such information about any other possible or proposed plan" immediately after "plan";

(2) in paragraph (2)(B), by inserting "the" immediately after "with"; and

(3) in paragraph (2)(C), by inserting "of" immediately after "holders".

(b) Section 1125(d) of title 11 of the United States Code is amended—

(1) by inserting "required under subsection (b) of this section" immediately after "statement" the first place it appears; and

(2) by inserting ", or otherwise seek review of," immediately after "appeal from".

(c) Section 1125(e) of title 11 of the

TAB 4

96TH CONGRESS 2d Session | HOUSE OF REPRESENTATIVES | REPORT No. 96-1195

AN ACT TO CORRECT TECHNICAL ERRORS, CLARIFY AND MAKE MINOR SUBSTANTIVE CHANGES TO PUBLIC LAW 95-598

JULY 25, 1980.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

Mr. RODINO, from the Committee on the Judiciary, submitted the following

REPORT

together with

DISSENTING VIEWS

[To accompany S. 658]

The Committee on the Judiciary, to whom was referred the bill (S. 658) to correct technical errors, clarify and make minor substantive changes to Public Law 95-598, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment to the text of the bill is a complete substitute therefor and appears in italic type in the reported bill.

INTRODUCTION

The Bankrupty Reform Act of 1978 has now been in effect lese than one year. It is clear even at this early time in the life of this law that technical amendments are required. Errors in printing, spelling, punctuation, grammar, syntax, and numeration arose in the bill as enacted because of the last-minute process of change through which the bill went when considered at the closing sessions of the 95th Congress.

These same last-minute changes also resulted in the enactment of a bill that contains incongruent provisions; material that was removed from earlier versions remained as either cross-references or antecedents for provisions changed or inserted. And, material added often was not completely integrated into the total fabric of the bill as enacted.

Such matters consitute the vast majority of the subject of the Technical Amendments Act. In addition, however, there are several items of a substantive nature which are included because: (1) it was intended that the particular subject was to be dealt with at the earliest possible time after the enactment of the Bankruptcy Refore Act in connection with whatever technical amendments would be considered; (2) further conforming changes were found to be necessary to complete the legislative work intended by the Bankruptcy Reform Act; (3) the treatment of a subject in the Bankruptcy Reform Act was found to be incomplete; or (4) there was overlooked some minor yet relevant matter. In each case the change proposed is consistent with policies adopted by Congress in its enactment of the Bankruptcy Reform Act.

Even with these substantive matters included and noting that they are consistent with the Bankruptcy Reform Act, nevertheless it is important to repeat that the Act as amended by this bill continues to represent a finely tuned and balanced treatment of the respective interests of debtors and creditors. Every effort has been made to abstain from reacting legislatively at every call for change and to maintain existing policy intact. At this time, there are known areas of bankruptcy activity which give the Committee concern and which the Committee intends to monitor closely. However, it is also premature to change a statute that has been in effect for such a short period of time where it is not really known to what extent these concerns are other than transitory.

Bankruptcy Judge's Retirement

H.R. 8200, as reported by the Committee during the 95th Congress, contained provisions to reorganize bankruptcy courts and include them within the category of United States courts subject to the standards of Article II of the Constitution. S. 2266, the bill passed by the Senate during the 95th Congress, which eventually became Public Law 95-598 (the Bankruptcy Reform Act of 1978), did not contain such provisions. Numbered among the provisions contained in H.R. 8200 were those which would have provided for retirement of bankruptcy judges. When this general subject was resolved between the House and the Senate, the matter of bankruptcy judge's retirement was eliminated with the understanding that at the earliest possible time it would be dealt with.

There are two classes of United States judges: life tenure; and fixed term tenure. Notwithstanding, all United States judges, for retirement purposes, participate in what loosely may be called "judicial retirement." The essential characteristics of this retirement system are: (1) it is noncontributory; (2) eligibility for retirement at 100 percent of the salary a judge received at the time of retirement is based upon the reaching of seventy years of age with 10 or more years of service, or sixty-five years of age with 15 or more years of service; and, in the case of fixed term judges, (3) provision for 100 percent or less benefits in the event of failure of reappointment.

Bankruptcy judges presently are participants in the civil service retirement system. The essential characteristics of this system are: (1) it is contributory; (2) benefits accrue at the rate of approximately

TAB 5

96TH CONGRESS 2d Session } HOUSE OF REPRESENTATIVES { REPORT No. 96-1195

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JULY 25, 1980.—Committed to the Committee of the Whole House on the State of the Union and ordered to be printed

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REPORT

together with

DISSENTING VIEWS

[To accompany S. 658]

The Committee on the Judiciary, to whom was referred the bill (S. 658) to correct technical errors, clarify and make minor substantive changes to Public Law 95-598, having considered the same, report favorably thereon with an amendment and recommend that the bill as amended do pass.

The amendment to the text of the bill is a complete substitute therefor and appears in italic type in the reported bill.

INTRODUCTION

The Bankrupty Reform Act of 1978 has now been in effect less than one year. It is clear even at this early time in the life of this law that technical amendments are required. Errors in printing, spelling, punctuation, grammar, syntax, and numeration arose in the bill as enacted because of the last-minute process of change through which the bill went when considered at the closing sessions of the 95th Congress.

These same last-minute changes also resulted in the enactment of a bill that contains incongruent provisions; material that was removed from earlier versions remained as either cross-references or antecedents for provisions changed or inserted. And, material added often was not completely integrated into the total fabric of the bill as enacted.

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2 percent per year for each year of service; (3) benefits are available only after the participant has reached the age of sixty-two years; and (4) there is an 80 percent cap on the amount of benefits receivable. The civil service retirement system does not provide an equitable basis for retirement for bankruptcy judges vis-a-vis other United States judges.

The civil service system is predicated upon an individual's coming to work for the Federal government at an early age, usually in a person's early twenties. The average age of bankruptcy judges ascending to the bench is forty-five.

The overwhelming opinion on this subject, including that of the Judicial Conference of the United States, is that bankruptcy judges should participate in the judicial retirement system. Differences of opinion exist regarding the extent to which credit for service should be given for service as a bankruptcy judge during the transition period (that time between the enactment of the Bankruptcy Reform Act and the taking effect of the new bankruptcy court created under that Act) and for service as a referee in bankruptcy prior to the enactment of the Bankruptcy Reform Act. This bill strikes a compromise between the position of giving such judges 100 percent credit for all such prior service and only allowing the participation in the judicial retirement system based upon service on the new court beginning April 1, 1984.

A complicated formula with a number of conditions and limitations has been created. The objective of this scheme is to not only provide an equitable basis for bankruptcy judges' retirement, but also to act as an incentive to keep on the bench the experience and ability of bankruptcy judges presently sitting. It is also important to understand that the system by which bankruptcy judges will be chosen has been changed by the Bankruptcy Reform Act. This change will undoubtedly have an adverse effect upon the ability of bankruptcy courts to retain some of the most knowledgeable and experienced of the bankruptcy judges.

Under the law that was repealed by the Bankruptcy Reform Act, bankruptcy judges were selected by the judges of the United States district court for the district wherein the bankruptcy judge would serve. Under the Bankruptcy Reform Act, bankruptcy judges will be nominated by the President. This change should not, in the best of all possible worlds, have the effect of displacing such experienced and knowledgeable judges. However, as this can be the case, enhancing bankruptcy judges' retirement will be an incentive for judges to seek presidential appointment and remain on the bench for a longer period of time.

The numerator for computing the amount of salary payable to a judge who is not reappointed at the end of his term is changed from sixteen years to fourteen years to conform to the term of office of a bankruptcy judge appointed under the Bankruptcy Reform Act.

Incumbent bankruptcy judges are given full credit for all service prior to April 1, 1984, for the purpose of determining eligibility for benefits, but the rate of accrual of salary payable to a bankruptcy judge upon relinquishing office by resignation or upon failure of reappointment is substantially less for service prior to November 6, 1978, the date of enactment of the Bankruptcy Reform Act.

The formula for computing the rate of accrual of salary payable to a bankruptcy judge upon relinquishment of office, if he meets the age and length of service requirements for benefits, is 1/28 for service as a bankruptcy judge prior to November 6, 1978 and 1/14 for service as a bankruptcy judge on and after that date. The difference in the rate of accrual of benefits for service as a bankruptcy judge prior to November 6, 1978 and for such service thereafter is adopted in recognition of the fact that the duties and responsibilities of the office of bankruptcy judge and the stature and jurisdiction of the bankruptcy court were greatly enhanced by the Bankruptcy Reform Act of 1978. The 1/14 formula will apply to all service as a bankruptcy judge prior to April 1, 1984 by a bankruptcy judge who is reappointed after that date if such a judge continues in service as a bankruptcy judge for a period of five years after the date of his reappointment or until he attains the age of seventy years.

Upon enactment of this bill an incumbent bankruptcy judge who is or may become eligible for benefits under section 373 of title 28 of the United States Code may elect coverage under that section, without regard to the date of such eligibility. To prevent so-called double-dipping, the election of benefits under section 373 voids the annuity rights of a bankruptcy judge under any other Federal employee pension plan.

An incumbent bankruptcy judge who has elected the benefits of section 373 of title 28 of the United States Code, but who has not attained the age of sixty-five years prior to April 1, 1984, forfeits all rights to future payments under that section unless such judge has filed with the President, the President of the Senate, and the Director of the Administrative Office of the United States Courts before April 1, 1984, a written notice agreeing to accept appointment as a bankruptcy judge after such date and, if offered such appointment, accepts such appointment.

The right of incumbent bankruptcy judges who meet the length of service requirements of section 373 of title 28 of the United States Code, to resign and receive payments under that section prior to April 1, 1984, is restricted to two categories of judges—(1) those judges who have attained the age of seventy years, and (2) any judge who has attained the age of sixty-five years and provides the Director of the Administrative Office of the United States Courts a certificate of disability signed by the chief judge of the circuit. Otherwise, incumbent bankruptcy judges are precluded from receiving benefits under the section prior to April 1, 1984.

Upon enactment of this bill, incumbent bankruptcy judges will become judges of the United States, which would ordinarily make them ineligible for continued coverage under the Civil Service Retirement system. However, the right of a bankruptcy judge continued in office by section 404(b) of the Bankruptcy Reform Act of 1978 to retain coverage under the Civil Service Retirement system is preserved until such time as he elects coverage under section 373 of title 28 of the United States Code.

The term "bankruptcy judge" is defined to include a referee in bankruptcy to make it clear that all service as a referee in bankruptcy is includible for purposes of this section.

A definition of "reappointment" to include appointment to the new bankruptcy court which comes into existence on April 1, 1984, is included to make clear the fact that incumbent bankruptcy judges, whose terms expire at the end of the transition period, who are not appointed to the new court by the President immediately following the transition period are deemed to have failed of reappointment for the purposes of this section.

The word "retires" and "retirement" are used in this section in a broad generic sense and are intended to include voluntary resignation or involuntary resignation because of failure of reappointment.

An incumbent bankruptcy judge who, after continuing to serve throughout the transition period, fails of reappointment, and who at the time of relinquishing office has fourteen or more years of service as a bankruptcy judge, is eligible to receive benefits under this section before attaining the age of sixty-five years. However, the salary payable to such judge shall be reduced by one-sixth of one percent for each full month such judge is under sixty-five years of age at the time he relinquishes office.

Municipal Financing

In structuring the Bankruptcy Reform Act, one of the objectives, simplification, was achieved by consolidating into one chapter (11) a number of the previously separate provisions dealing with reorganizations. Now, there are only four distinct types of proceedings under title 11: liquidation, under chapter 7; adjustment of debts of a municipality, under chapter 9; reorganization, under chapter 11; and adjustment of debts of individuals with regular income, under chapter 13. This organizational arrangement, however, required that the general provisions contained in chapters 1, 3, and 5 either be made applicable or inapplicable, as was appropriate.

One such provision, contained in section 552, deals with the post-petition effect of a security interest. In arriving at the treatment of this subject as it did, the Bankruptcy Reform Act expressed the general policy that upon the filing of a petition in bankruptcy, except for proceeds, there would be no post-petition effect of a security interest. The central frame of reference for this decision was commercial transactions and the recognition and acceptance of after-acquired property clauses by the Uniform Commercial Code (adopted universally by the States, with the exception of Louisiana). This provision was made applicable to a proceeding under chapter 9.

After the enactment of the Bankruptcy Reform Act, attention was called to the fact of this applicability and that as a result certain municipal bondholders' interests in specific funds might be jeopardized in the event of the filing of a petition by the municipality under chapter 9. Revenue bonds issued by a municipality are in effect longer term secured obligations, the security for which is a specific fund(s). The bond indenture is the security agreement setting forth the security interest which, invariably, contains a provision for the repayment of the bond obligation from a specific fund(s) as such fund(s) is generated from time to time. Therefore, with section 552 applicable in a chapter 9 proceeding, upon the filing of a petition by a municipality, bondholders' rights to the specific fund(s) would be impaired.

S. 658 as enacted by the Senate contains a provision, a new section 928, designed to overcome the potential limiting effect section 552 would have on municipal revenue bonds in the event of the filing of a petition by a municipal issuer of such securities. Because this Senate-proposed section 928 deals only with traditional revenue bonds and not other forms of municipally issued securities secured by specified funds, concerrn was raised that the Senate's section 928 of S. 658 was not adequate. In seeking to eliminate section 552's limiting effect upon all municipal securities secured by specified funds, whether of the traditional revenue bond type, or some other type, the Committee sought a way to do this without placing itself in the position of making any express representation to States and municipalities regarding the character or quality of their securities under non-bankruptcy law. The Committee believes that it was not the intent of Congress in the enactment of the Bankruptcy Reform Act of 1978 to make any such representations. Therefore, it has chosen to deal with the limiting effect of section 552 by deleting the reference to it from section 901, removing from application in a chapter 9 proceeding the operation of that section.

Further, the Committee believes that it was not the intent of Congress in the enactment of 547(c)(3) to penalize holders of municipal securities which are secured by future receipts of the issuer. The deletion from section 901 of the reference to section 547(e)(3) would avoid allowing such payments to be classified as voidable preferences under section 547.

Stockbroker/Commodity Broker Liquidations

Prior to the enactment of the Bankruptcy Reform Act special provisions existed in the bankruptcy laws for liquidations of stockbrokers. Much of this prior law served as the basis for what has become subchapter III of chapter 7 in the new Bankruptcy Code. The new subchapter IV, dealing with commodity broker liquidations, is new and not based upon any prior treatment under the repealed Bankruptcy Act. These subchapters were intended to provide comparable treatment for stockbroker and commodity broker liquidations. Moreover, it also was intended that in the event of a bankruptcy involving such an entity, the operations of the respective securities and commodities markets would be affected only minimally, i.e., that the financial failure of any one such entity would not have such an affect upon an entire marketplace so as to pose the potential for a massive disruption of the entire industry. However, quite soon after the enactment of the Bankruptcy Reform Act it was brought to the Committee's attention that the provisions in subchapters III and IV fell short of their intended mark. In short, the integrity of the securities and commodities markets was not adequately protected; and there was not comparability between the provisions of subchapters III and IV.

There are a number of provisions in the bill which pertain to stockbrokers, securities clearing agencies, commodity brokers and forward contract merchants. These are intended to clarify the application to these entities of certain provisions contained in the Bankruptcy Reform Act. The Bankruptcy Reform Act provides a number of protections to commodity brokers and commodity clearing organizations, and several amendments have been made to clarify that these same protections are intended to apply to stockbrokers and securities clearing agencies. The overall purpose of these provisions is to preserve the financial integrity of the nation's commodity and securities markets.

Provision was also necessary to clarify that the automatic stay provision does not affect the setoff of mutual debts and claims which relate to commodity contracts, forward contracts, leverage transactions or securities contracts; nor does it prevent setoffs against customer property held by a commodity broker, forward contract merchant, stockbroker or securities clearing agency for claims which are margin or settlement payments.

Related amendments also preserve the contractual rights of stockbrokers, securities clearing agencies, commodity brokers and forward contract merchants to liquidate a debtor's account. notwithstanding the automatic stay of Section 362, or any other provision of Federal or State law or court order, unless the court order is authorized under the Securities Investor Protection Act of 1970 (15 U.S.C. 78aaa et seq.) or is required because of a threat to the national security.

In Subchapter III, Section 749 has been amended to give the Securities and Exchange Commission the power to approve specified transfers so approved may not be avoided by the trustee. This authority corresponds to the authority given to the Commodity Futures Trading Commission in Section 764(b).

In Subchapter IV, the definition of "customer" has been amended to delete the reference to debtor and substitute in its place a broader reference. Under the previous definition, only an entity which was a debtor could have a customer. Such a result would have defeated the broad protections intended to be provided by the Act. Other clarifying amendments have been made to several of the definitions to be sure that if trading in commodity options is approved by the CFTC, such trading will be included within the scope of Subchapter IV provisions.

It is also made clear that the trustee may not avoid as a preference or fraudulent transfer, a margin payment, deposit or settlement payment made by or to a commodity broker, forward contract merchant, stockbroker or securities clearing agency, unless the payment is both made and received with intent to defraud.

Finally, Subchapter IV of chapter 7 has been amended to clarify that the proprietary accounts of commodity brokers are not entitled to share in any distribution from the customer property estate until such time as all other customer net equity claims have been paid in full.

Tax Provisions

The Bankruptcy Reform Act's repeal of the former Bankruptcy Act removed from applicability the special provisions for treatment of tax consequences of transactions arising in a bankruptcy context. This was done with the view that soon after the enactment of the Bankruptcy Reform Act there would be considered bankruptcy tax legislation. However, to initiate the process whereby such tax legislation would be considered, there was included in section 346 a number of provisions designed to identify a basis upon which tax consequences could be determined.

With the consideration of the Technical Amendments Act, this tax legislation has not yet been fully considered and the provisions of section 346, therefore, exist in a vacuum.

These section 346 provisions are being removed with the intention that (1) there should be a uniform treatment of tax consequences in bankruptcy under both State and federal law, (2) federal tax legislation should be considered at the earliest possible time, and (3) until such legislation is enacted it is most desirable that tax consequences of bankruptcy should be dealt with as they were under the former Bankruptcy Act.

SECTION-BY-SECTION ANALYSIS

TITLE I

Section 1(a). This amendment deletes a redundancy.

Subsection (b). This amendment corrects a typographical error.

Subsection(c). This amendment corrects the cross-references identifying the types of claims to be treated as pre-petition claims to include certain preconversion and co-debtor claims.

Subsection(d). This amendment corrects an omission by providing the connective to assure that "entity" is defined to include all of the types specified.

Subsection (e). This amendment corrects a typographical error.

Subsection (f). This amendment to the definition of "insolvent" with reference to a partnership clarifies that it is the general partner nonpartnership property that is the subject of valuation eliminating the ambiguity presented by the use of the term "separate" which allowed for the reference to noncommunity property in a community property stae; substitutes the indefinite article with reference to the types of property excluded from the valuation; and adds a cross-reference to include all property appropriately to be excluded from the valuation.

Subsection (g). This amendment redesignates paragraphs (35), (36), (37), (38), (39), and (40) to allow for the addition of two new definitions; and adds as one of the new paragraphs a definition for "securities clearing agency" to facilitate the treatment of stockbroker bankruptcies under subchapter III of chapter 7.

Subsection (h). This amendment clarifies that the term "security" is applicable to the designated contract or interest if such is required to be the subject of a Securities Act registration statement whether or not it is so subject.

Subsection (i). This amendment corrects the name of a type of contract excluded from the definition of "security".

Subsection (j). This amendment makes a stylistic change in the cross-reference; and clarifies that the contract or certificate excluded from the definition of "security" is not required to be the subject of a Securities Act registration statement whether or not it is so subject.

Subsection (k). This amendment adds a new paragraph which provides a definition for "State" primarily to assure that residents and domiciliaries of Puerto Rico can become debtors under title 11.

Subsection (l). This amendment makes a stylistic change.

Subsection (m). This amendment makes a change in punctuation to allow an additional paragraph to be added.

TAB 6

Calendar No. 102

98TH CONGRESS 1st Session | SENATE | REPORT No. 98–65

OMNIBUS BANKRUPTCY IMPROVEMENTS ACT OF 1983

REPORT

OF THE

COMMITTEE ON THE JUDICIARY UNITED STATES SENATE

[To accompany S. 445]

[Together with Additional Views]

Ordered to be printed

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WASHINGTON : 1983

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Calendar No. 102

98TH CONGRESS 1st Session | SENATE | REPORT No. 98-65

OMNIBUS BANKRUPTCY IMPROVEMENTS ACT OF 1983

APRIL 26, 1983—Ordered to be printed

Mr. THURMOND, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 445]

The Committee on the Judiciary, which considered the bill (S. 445) to make certain substantive changes to Public Law 95-598, the Bankruptcy Reform Act of 1978, having considered the same, reports favorably thereon as amended and recommends that the bill as amended do pass.

I. PURPOSE OF THE BILL

The purpose of the bill is to make certain substantive changes in Public Law 95-598, the Bankruptcy Reform Act of 1978.

II. INTRODUCTION AND HISTORY OF THE BILL

On July 12, 1978, the Committee on the Judiciary reported S 2226, the Senate version of the Bankruptcy Reform Act of 1978. On September 20, 1978, H.R. 8200, with further amendments, was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared the bill for signature by the President. On November 6, 1978, President Carter signed the bill and it became Public Law 95-598. On October 1, 1979, Public Law 95-598, styled the Bankruptcy Reform Act of 1978, went into effect.

In the 97th Congress, the Subcommittee on Courts, chaired by Senator Dole, held general oversight hearings on the Bankruptcy Reform Act of 1978 on April 3 and 6, 1981. As a result of those hearings, numerous amendments, largely technical in nature, were proposed which were passed by the Senate as S. 863, the Bankruptcy Amendments Act of 1981 on July 17 of that year. Additional hearings were held on October 29, 1981. During the course of these

comparative performance of courts in cases filed under the respective chapters of the Code.

In an effort to begin compiling comprehensive comparative statistics which would provide the Congress with more complete information concerning the performance of the courts in the respective judicial districts, the bill contains a directive to the Director of the Administrative Office of the United States Courts to begin assembling information concerning assets and liabilities of debtors; amount of debt discharged in cases under each chapter of title 11; the total amount of disbursements to creditors by the bankruptcy courts, and time elapsed between case filings and payments to creditors.

All of the information required to be collected under Subtitle "H" of the bill would be available from records which will be available in the bankruptcy courts from petition and motion filings, and it is the belief of the Committee that the compilations requested will pose no unmanageable burden upon the Administrative Office. The Director, of course, has complete discretion in establishing the procedures by which the information shall be gathered.

I. Technical Amendments

On July 12, 1978, the Committee on the Judiciary reported S. 2266, the Senate version of the Bankruptcy Reform Act of 1978. On September 7, 1978, the Senate took from the desk H.R. 8200, the House version of the Bankruptcy Reform Act of 1978, struck the text of the bill and inserted in its place the text of S. 2266 and passed the bill as amended. On September 20, 1978, H.R. 8200, with further amendments was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared the bill for signature. On November 6, 1978, the bill was signed into law with the designation Public Law 95-598, the Bankruptcy Reform Act of 1978.

Since the date of passage of the Act, judges, scholars, and bankruptcy practitioners have reviewed its provisions and numerous technical amendments and minor substantive changes have been suggested to clarify the intent of Congress.

On March 14, 1979, Senator DeConcini introduced S. 658 which embodied many of those recommendations. After additional revision, S. 658 was reported out of the Judiciary Committee on August 3, 1979, passed by unanimous consent of the Senate on September 7, 1979, and sent to the House. On September 22, 1980, the House with further amendments passed S. 658 by unanimous consent. On December 1, 1980, the Senate made additional amendments to the House-passed version of S. 658 and passed it by unanimous consent. On December 3, 1980 the House with further amendments passed S. 658 by unanimous consent. On December 9, 1980, the Senate with further amendments reintroduced the bill as S. 3259 and passed it by unanimous consent. Since the House during the remainder of the 96th Congress took no action on the final Senate changes, the bill was not enacted into law.

In the 97th Congress, on April 2, 1981, Senator Dole, with Senators Heflin and DeConcini as cosponsors, introduced S. 863, which

embodied all of the provisions of S. 3259, as passed by the Senate on December 1, 1980, with a few minor changes. On April 3 and 6, 1981, general oversight hearings on the Bankruptcy Code were held by the Subcommittee on Courts, at which time testimony in support of the bill's provisions was received.

On July 17, 1981, S. 863 was passed by the Senate. However, no action was taken on the bill by the House during the 97th Congress.

On January 24th, 1983, further hearings were held on needed amendments by the Judiciary Subcommittee on Courts. At the conclusion of hearings, Senator Dole introduced the substance of S. 863, with additional provisions, as Subtitle I of the Committee bill.

Significant provisions of Subtitle I are discussed in the sectional analysis which follows this summary of the bill contents.

IV. SUMMARY AND SECTIONAL ANALYSIS OF THE BILL

A. SUMMARY

The bill is divided into ten subtitles, the content of which are as follows:

Subt. A: *Consumer Credit Amendments*. Reformed procedures relating to consumer debtor cases.

Subt. B: *Grain Elevator Bankruptcy Amendments*. Text is drawn from S. 3037 in 97th Congress. Provides procedures for expedited abandonment of grain from bankrupt elevators.

Subt. C: *Shopping Centers Bankruptcy Amendments*. S. 2297 in 97th, S. 549 in 98th. Establishes a timetable within which trustee would have to accept or reject leases on shopping center properties in bankruptcy, and other purposes.

Subt. D: *Drunk Drivers' Nondischargeability of debts*. S. 2159 in 97th Congress. Prohibits debts incurred as a result of an act of drunk driving from being discharged in bankruptcy.

Subt. E: *Referee's Salary and Expense Fund Amendments*. (Drawn from S. 863 in 97th Congress). Corrects a drafting error in the 1978 Act which requires a handful of corporate debtors in bankruptcy to continue making payments to the non-existent fund.

Subt. F: *Repurchase Agreements Amendments*. Proposal of the Federal Reserve Board, which exempts repurchase agreements from the automatic stay in bankruptcy.

Subt. G: *Timesharing Agreements Amendments*. S. 3027 in the 97th Congress, S. 492 in the 98th. This subtitle provides that persons who hold timesharing agreements shall be granted a lien on the property involved when the timesharing contractor goes bankrupt and the trustee terminates the timesharing contract, and other provisions.

Subt. H: *Bankruptcy Oversight*. This subtitle directs the Administrative Office to collect information on bankruptcy filings regarding levels of debtor income and assets, debtor living expenses, and total amounts recovered for creditors in proceedings under Chapters 7, 11, and 13. This information will assist Congress in analyzing the functioning of the bankruptcy system.

Subt. I: *Technical and Clarifying Amendments*. The bulk of the provisions in this subtitle are drawn from S. 863, which passed the

TAB 7

Calendar No. 192

97TH CONGRESS } SENATE { REPORT
1st Session } { No. 97-150

BANKRUPTCY AMENDMENTS ACT OF 1981

JULY 10 (legislative day, JULY 8), 1981.—Ordered to be printed

Mr. THURMOND, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 863]

The Committee on the Judiciary, to which was referred the bill (S. 863) to correct technical errors, clarify, and make minor substantive changes to Public Law 95-598, the Bankruptcy Reform Act of 1978, having considered the same, reports favorably thereon with amendments and recommends that the bill as amended do pass.

PURPOSE OF THE AMENDMENT

The amendment is an amendment in the nature of a substitute and its purpose is identical to that of the bill as introduced: To correct technical errors, clarify and make minor substantive changes to Public Law 95-598.

PURPOSE OF THE BILL

The purpose of the bill is to correct technical errors, clarify and make minor substantive changes in Public Law 95-598, the Bankruptcy Reform Act of 1978.

INTRODUCTION

On July 12, 1978, the Committee on the Judiciary reported S. 2266, the Senate version of the Bankruptcy Reform Act of 1978. On September 7, 1978, the Senate took from the desk H.R. 8200, the House version of the Bankruptcy Reform Act of 1978, struck the text of the bill and inserted in its place the text of S. 2266 and passed the bill as amended. On September 20, 1978, H.R. 8200, with further amendments was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared the bill for signature by the President. On November 6, 1978, President Carter signed the bill and it became Public Law 95–598. Judge, scholars and bankruptcy practitioners have reviewed its provisions and numerous technical amendments and minor substantive changes to make clear the intent of Congress have been suggested to the Committee.

On March 14, 1979, Senator DeConcini introduced S. 658 which embodied many of those recommendations. After additional revision, S. 658 was reported out of the Judiciary Committee on August 3, 1979, passed by unanimous consent of the Senate on September 7, 1979, and sent to the House. On September 22, 1980, the House with further amendments passed S. 658 by unanimous consent. On December 1, 1980, the Senate made additional amendments to the House-passed version of S. 658 and passed it by unanimous consent. On December 3, 1980, the House with further amendments passed S. 658 by unanimous consent. On December 9, 1980, the Senate with further amendments reintroduced the bill as S. 3259 and passed it by unanimous consent. Since the House during the remainder of the 96th Congress took no action on the final Senate changes, the bill was not enacted into law.

In the 97th Congress, on April 2, 1981, Senator Dole, with Senators Heflin and DeConcini as cosponsors, introduced S. 863, which embodied all of the provisions of S. 3259, as passed by the Senate on December 1, 1980, with a few minor changes. On April 3 and 6, 1981, general oversight hearings on the Bankruptcy Code were held by the Subcommittee on Courts, at which time testimony in support of the bill's provisions was received.

Section-by-Section Analysis—Title I

The amendments contained in title I make amendments to title I of The Bankruptcy Reform Act of 1978, Public Law 95–598 ("the Reform Act"). In this title all section references within the section and subsection descriptions of the amendments will be to title I of the Reform Act unless otherwise indicated.

Section 1(a). This section deletes a redundancy. "Substantially all the property of the debtor" includes all of the property of the debtor and "all" can be deleted as redundant.

Subsection (b). This amendment corrects a typographical error.

Subsection (c). This amendment cross-references two additional sections to complete the intent that claims fixed after the filing of the petition are to be treated as pre-petition claims, and deletes the reference to present section 502(i), which is in effect repealed by section 30(g) of the bill.

Subsection (d). This amendment corrects a typographical error in definition of "entity".

Subsection (e). This amendment corrects a typographical error in the definition of "individual with regular income".

Subsection (f). This amendment to the definition of "insolvent" with respect to a partnership, clarifies that "separate" as used in the definition refers to the general partners' nonpartnership property, and removes the ambiguity that it might refer to his noncommunity property in a community property estate.

TAB 8

Calendar No. 192

97TH CONGRESS 1st Session } SENATE { REPORT No. 97-150

BANKRUPTCY AMENDMENTS ACT OF 1981

JULY 10 (legislative day, JULY 8), 1981.—Ordered to be printed

Mr. THURMOND, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 863]

The Committee on the Judiciary, to which was referred the bill (S. 863) to correct technical errors, clarify, and make minor substantive changes to Public Law 95-598, the Bankruptcy Reform Act of 1978, having considered the same, reports favorably thereon with amendments and recommends that the bill as amended do pass.

PURPOSE OF THE AMENDMENT

The amendment is an amendment in the nature of a substitute and its purpose is identical to that of the bill as introduced: To correct technical errors, clarify and make minor substantive changes to Public Law 95-598.

PURPOSE OF THE BILL

The purpose of the bill is to correct technical errors, clarify and make minor substantive changes in Public Law 95-598, the Bankruptcy Reform Act of 1978.

INTRODUCTION

On July 12, 1978, the Committee on the Judiciary reported S. 2266, the Senate version of the Bankruptcy Reform Act of 1978. On September 7, 1978, the Senate took from the desk H.R. 8200, the House version of the Bankruptcy Reform Act of 1978, struck the text of the bill and inserted in its place the text of S. 2266 and passed the bill as amended. On September 20, 1978, H.R. 8200, with further amendments was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared standards of 1103(b) has meant significant hardship to creditors in retaining the best, most informed counsel. Experience under the Code, particularly in rural areas, has shown that the cure for the potential conflict has been at great cost and is in all likelihood worse than the disease. Present 1103(b) is an example of paternalism on the part of the Federal Government that is hardly needed in the context of chapter 11 bankruptcy proceedings between businessmen dealing at arm's length.

As a result of oversight hearings that dealt in part with this provision, the committee concludes that 1103(b) should be modified. As presently written, 1103(b) (1) assumes a conflict that usually does not exist (and which professional rules of ethics already ban); (2) excludes from administration of the bankruptcy estate those professionals who are most experienced and knowledgeable about the estate (i.e., those who are already representing individual creditors); (3) inhibits expeditious bankruptcy administration and increases the cost of administration; and (4) may inhibit out-of-court settlements which should be encouraged.

The Committee feels the amendment adequately meets the concerns of those who see a potential for conflict by precluding dual representation by those who have an adverse interest. The courts are fully capable of making this determination. The Committee also feels that mere representation by a person of one or more creditors of the same class as are represented by a creditors' committee also represented by that person shall not per se constitute the representation of an adverse interest. The court should not presume to know better than the affected creditors except in clear instances of potential impropriety.

Subsection (b). Paragraph (1) makes clear that the creditors' committee is not required to make recommendations with respect to the plan and may solicit rejections as well as acceptances. Paragraph (2) deletes redundant language in section 1103(c).

Section 95. This amendment makes a necessary grammatical change.

Section 96. This amendment gives the court explicit power to regulate the duties of an examiner.

Section 97. This amendment makes clarifying changes.

Section 98. This amendment makes a clarifying change. The court may not ex parte order the trustee or debtor in possession to cease operating the debtor's business.

Section 99. This amendment makes clear that a deficiency claim will be eliminated only when the secured creditor has had an opportunity to credit bid the claim. The amendment adds abandonment or surrender of the collateral to the secured creditor as the possible events that would eliminate the deficiency claim.

Section 100(a). This amendment makes a technical clarifying change and corrects a typographical error.

Subsection (b). This amendment makes stylistic changes.

Section 101(a). This amendment makes a grammatical change.

Subsection (b). This amendment makes a technical stylistic change.

Section 102(a). Paragraphs (1) through (5) make technical stylistic changes. Paragraph (6) makes clear that preferred stock without voting rights can be issued under the plan and the prohibition against issuing stock that cannot be voted extends only to common stock.

TAB 9

Calendar No. 102

98TH CONGRESS *1st Session*	SENATE	REPORT No. 98-65

OMNIBUS BANKRUPTCY IMPROVEMENTS ACT OF 1983

REPORT

OF THE

COMMITTEE ON THE JUDICIARY UNITED STATES SENATE

[To accompany S. 445]

[Together with Additional Views]

Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE
WASHINGTON : 1983

19-562 O

Calendar No. 102

98TH CONGRESS
1st Session

SENATE

REPORT
No. 98-65

OMNIBUS BANKRUPTCY IMPROVEMENTS ACT OF 1983

APRIL 26, 1983—Ordered to be printed

Mr. THURMOND, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 445]

The Committee on the Judiciary, which considered the bill (S. 445) to make certain substantive changes to Public Law 95-598, the Bankruptcy Reform Act of 1978, having considered the same, reports favorably thereon as amended and recommends that the bill as amended do pass.

I. PURPOSE OF THE BILL

The purpose of the bill is to make certain substantive changes in Public Law 95-598, the Bankruptcy Reform Act of 1978.

II. INTRODUCTION AND HISTORY OF THE BILL

On July 12, 1978, the Committee on the Judiciary reported S. 2226, the Senate version of the Bankruptcy Reform Act of 1978. On September 20, 1978, H.R. 8200, with further amendments, was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared the bill for signature by the President. On November 6, 1978, President Carter signed the bill and it became Public Law 95-598. On October 1, 1979, Public Law 95-598, styled the Bankruptcy Reform Act of 1978, went into effect.

In the 97th Congress, the Subcommittee on Courts, chaired by Senator Dole, held general oversight hearings on the Bankruptcy Reform Act of 1978 on April 3 and 6, 1981. As a result of those hearings, numerous amendments, largely technical in nature, were proposed which were passed by the Senate as S. 863, the Bankruptcy Amendments Act of 1981 on July 17 of that year. Additional hearings were held on October 29, 1981. During the course of these

hearings, judges, scholars, and bankruptcy practitioners testified as to the effectiveness of the new Code as it applies to consumer debtors and suggested improvements. Comments centered upon provisions in Chapters 7 and 13 governing redemption of collateral, reaffirmation agreements, Federal exemptions, preferential transfers, and a number of additional procedural sections of the Code. Witnesses also raised questions concerning the statutorily mandated criteria for determining eligibility for bankruptcy, and certain witnesses requested committee consideration of various proposals to require the bankruptcy court to evaluate the future earnings capability of consumer petitioners in determining eligibility for Chapter 7 relief, while others opposed these proposals. At the hearings held in October, 1981, the Subcommittee on Courts explored the ramifications of these proposals.

On December 16, 1981, all of the Subcommittee members introduced S. 2000, which was favorably voted out of the Subcommittee on Courts, with an amendment in the nature of a substitute offered by Chairman Dole accepted thereto by a unanimous poll of February 12, 1982. The bill was placed on the Committee calendar early in March and was before the committee for several weeks prior to vote, during which time committee staff conducted discussions on areas of concern to members. As a result of these discussions, a number of amendments were accepted to S. 2000 with modifications prior to final Committee action. The Committee approved reporting of the bill with amendments by voice vote on April 20, 1982. Senators Kennedy and Metzenbaum requested that their votes be recorded in the negative, and the clerk was so instructed. No action was taken by the full Senate on S. 2000 during the 97th Congress.

On January 25, 1983, additional hearings were held and on February 3, 1983, Senator Dole introduced S. 445, which contained the provisions of S. 2000, in addition to provisions addressing other areas of proposed substantive amendments. Further hearings were held on S. 445 on April 6, 1983.

After these hearings and as a result of further discussions among Committee members, S. 445 was amended in several important respects. Provisions requiring debtors to file, with the court, statements of projected future earnings and expenses and authorizing the bankruptcy courts to dismiss Chapter 7 cases if debtors could pay a reasonable portion of their debts out of future income were deleted. Provisions for debtor counseling by the court-appointed trustee were added. S. 445 was also amended to include language authorizing courts—acting strictly on their own motion—to dismiss a case where the granting of Chapter 7 relief would represent a substantial abuse of that chapter. Further technical and clarifying amendments were made to sections of the bill dealing with grain elevators, shopping centers, and other technical matters.

On April 19, 1981, the Judiciary Committee approved reporting of the bill with the amendments agreed to.

During the course of Committee action on S. 445, Senators Dole, Heflin, Metzenbaum, Kennedy, Leahy, Baucus and DeConcini each played a critical role in shaping the legislation and in developing moderating language enhancing protections for debtors affected by changes in the law provided for in the bill.

comparative performance of courts in cases filed under the respective chapters of the Code.

In an effort to begin compiling comprehensive comparative statistics which would provide the Congress with more complete information concerning the performance of the courts in the respective judicial districts, the bill contains a directive to the Director of the Administrative Office of the United States Courts to begin assembling information concerning assets and liabilities of debtors; amount of debt discharged in cases under each chapter of title 11; the total amount of disbursements to creditors by the bankruptcy courts, and time elapsed between case filings and payments to creditors.

All of the information required to be collected under Subtitle "H" of the bill would be available from records which will be available in the bankruptcy courts from petition and motion filings, and it is the belief of the Committee that the compilations requested will pose no unmanageable burden upon the Administrative Office. The Director, of course, has complete discretion in establishing the procedures by which the information shall be gathered.

I. TECHNICAL AMENDMENTS

On July 12, 1978, the Committee on the Judiciary reported S. 2266, the Senate version of the Bankruptcy Reform Act of 1978. On September 7, 1978, the Senate took from the desk H.R. 8200, the House version of the Bankruptcy Reform Act of 1978, struck the text of the bill and inserted in its place the text of S. 2266 and passed the bill as amended. On September 20, 1978, H.R. 8200, with further amendments was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared the bill for signature. On November 6, 1978, the bill was signed into law with the designation Public Law 95-598, the Bankruptcy Reform Act of 1978.

Since the date of passage of the Act, judges, scholars, and bankruptcy practitioners have reviewed its provisions and numerous technical amendments and minor substantive changes have been suggested to clarify the intent of Congress.

On March 14, 1979, Senator DeConcini introduced S. 658 which embodied many of those recommendations. After additional revision, S. 658 was reported out of the Judiciary Committee on August 3, 1979, passed by unanimous consent of the Senate on September 7, 1979, and sent to the House. On September 22, 1980, the House with further amendments passed S. 658 by unanimous consent. On December 1, 1980, the Senate made additional amendments to the House-passed version of S. 658 and passed it by unanimous consent. On December 3, 1980 the House with further amendments passed S. 658 by unanimous consent. On December 9, 1980, the Senate with further amendments reintroduced the bill as S. 3259 and passed it by unanimous consent. Since the House during the remainder of the 96th Congress took no action on the final Senate changes, the bill was not enacted into law.

In the 97th Congress, on April 2, 1981, Senator Dole, with Senators Heflin and DeConcini as cosponsors, introduced S. 863, which

embodied all of the provisions of S. 3259, as passed by the Senate on December 1, 1980, with a few minor changes. On April 3 and 6, 1981, general oversight hearings on the Bankruptcy Code were held by the Subcommittee on Courts, at which time testimony in support of the bill's provisions was received.

On July 17, 1981, S. 863 was passed by the Senate. However, no action was taken on the bill by the House during the 97th Congress.

On January 24th, 1983, further hearings were held on needed amendments by the Judiciary Subcommittee on Courts. At the conclusion of hearings, Senator Dole introduced the substance of S. 863, with additional provisions, as Subtitle I of the Committee bill.

Significant provisions of Subtitle I are discussed in the sectional analysis which follows this summary of the bill contents.

IV. SUMMARY AND SECTIONAL ANALYSIS OF THE BILL

A. SUMMARY

The bill is divided into ten subtitles, the content of which are as follows:

Subt. A: *Consumer Credit Amendments.* Reformed procedures relating to consumer debtor cases.

Subt. B: *Grain Elevator Bankruptcy Amendments.* Text is drawn from S. 3037 in 97th Congress. Provides procedures for expedited abandonment of grain from bankrupt elevators.

Subt. C: *Shopping Centers Bankruptcy Amendments.* S. 2297 in 97th, S. 549 in 98th. Establishes a timetable within which trustee would have to accept or reject leases on shopping center properties in bankruptcy, and other purposes.

Subt. D: *Drunk Drivers' Nondischargeability of debts.* S. 2159 in 97th Congress. Prohibits debts incurred as a result of an act of drunk driving from being discharged in bankruptcy.

Subt. E: *Referee's Salary and Expense Fund Amendments* (Drawn from S. 863 in 97th Congress). Corrects a drafting error in the 1978 Act which requires a handful of corporate debtors in bankruptcy to continue making payments to the non-existent fund.

Subt. F: *Repurchase Agreements Amendments.* Proposal of the Federal Reserve Board, which exempts repurchase agreements from the automatic stay in bankruptcy.

Subt. G: *Timesharing Agreements Amendments.* S. 3027 in the 97th Congress, S. 492 in the 98th. This subtitle provides that persons who hold timesharing agreements shall be granted a lien on the property involved when the timesharing contractor goes bankrupt and the trustee terminates the timesharing contract, and other provisions.

Subt. H: *Bankruptcy Oversight.* This subtitle directs the Administrative Office to collect information on bankruptcy filings regarding levels of debtor income and assets, debtor living expenses, and total amounts recovered for creditors in proceedings under Chapters 7, 11, and 13. This information will assist Congress in analyzing the functioning of the bankruptcy system.

Subt. I: *Technical and Clarifying Amendments.* The bulk of the provisions in this subtitle are drawn from S. 863, which passed the

TAB 10

Calendar No. 102

98TH CONGRESS *1st Session*	SENATE	REPORT No. 98-65

OMNIBUS BANKRUPTCY IMPROVEMENTS ACT OF 1983

REPORT

OF THE

COMMITTEE ON THE JUDICIARY UNITED STATES SENATE

[To accompany S. 445]

[Together with Additional Views]

Ordered to be printed

U.S. GOVERNMENT PRINTING OFFICE

19-563 O WASHINGTON : 1983

hearings, judges, scholars, and bankruptcy practitioners testified as to the effectiveness of the new Code as it applies to consumer debtors and suggested improvements. Comments centered upon provisions in Chapters 7 and 13 governing redemption of collateral, reaffirmation agreements, Federal exemptions, preferential transfers, and a number of additional procedural sections of the Code. Witnesses also raised questions concerning the statutorily mandated criteria for determining eligibility for bankruptcy, and certain witnesses requested committee consideration of various proposals to require the bankruptcy court to evaluate the future earnings capability of consumer petitioners in determining eligibility for Chapter 7 relief, while others opposed these proposals. At the hearings held in October, 1981, the Subcommittee on Courts explored the ramifications of these proposals.

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On January 25, 1983, additional hearings were held and on February 3, 1983, Senator Dole introduced S. 445, which contained the provisions of S. 2000, in addition to provisions addressing other areas of proposed substantive amendments. Further hearings were held on S. 445 on April 6, 1983.

After these hearings and as a result of further discussions among Committee members, S. 445 was amended in several important respects. Provisions requiring debtors to file, with the court, statements of projected future earnings and expenses and authorizing the bankruptcy courts to dismiss Chapter 7 cases if debtors could pay a reasonable portion of their debts out of future income were deleted. Provisions for debtor counseling by the court-appointed trustee were added. S. 445 was also amended to include language authorizing courts—acting strictly on their own motion—to dismiss a case where the granting of Chapter 7 relief would represent a substantial abuse of that chapter. Further technical and clarifying amendments were made to sections of the bill dealing with grain elevators, shopping centers, and other technical matters.

On April 19, 1981, the Judiciary Committee approved reporting of the bill with the amendments agreed to.

During the course of Committee action on S. 445, Senators Dole, Heflin, Metzenbaum, Kennedy, Leahy, Baucus and DeConcini each played a critical role in shaping the legislation and in developing moderating language enhancing protections for debtors affected by changes in the law provided for in the bill.

comparative performance of courts in cases filed under the respective chapters of the Code.

In an effort to begin compiling comprehensive comparative statistics which would provide the Congress with more complete information concerning the performance of the courts in the respective judicial districts, the bill contains a directive to the Director of the Administrative Office of the United States Courts to begin assembling information concerning assets and liabilities of debtors; amount of debt discharged in cases under each chapter of title 11; the total amount of disbursements to creditors by the bankruptcy courts, and time elapsed between case filings and payments to creditors.

All of the information required to be collected under Subtitle "H" of the bill would be available from records which will be available in the bankruptcy courts from petition and motion filings, and it is the belief of the Committee that the compilations requested will pose no unmanageable burden upon the Administrative Office. The Director, of course, has complete discretion in establishing the procedures by which the information shall be gathered.

I. Technical Amendments

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Since the date of passage of the Act, judges, scholars, and bankruptcy practitioners have reviewed its provisions and numerous technical amendments and minor substantive changes have been suggested to clarify the intent of Congress.

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embodied all of the provisions of S. 3259, as passed by the Senate on December 1, 1980, with a few minor changes. On April 3 and 6, 1981, general oversight hearings on the Bankruptcy Code were held by the Subcommittee on Courts, at which time testimony in support of the bill's provisions was received.

On July 17, 1981, S. 863 was passed by the Senate. However, no action was taken on the bill by the House during the 97th Congress.

On January 24th, 1983, further hearings were held on needed amendments by the Judiciary Subcommittee on Courts. At the conclusion of hearings, Senator Dole introduced the substance of S. 863, with additional provisions, as Subtitle I of the Committee bill.

Significant provisions of Subtitle I are discussed in the sectional analysis which follows this summary of the bill contents.

IV. SUMMARY AND SECTIONAL ANALYSIS OF THE BILL

A. SUMMARY

The bill is divided into ten subtitles, the content of which are as follows:

Subt. A: *Consumer Credit Amendments*. Reformed procedures relating to consumer debtor cases.

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Subt. D: *Drunk Drivers' Nondischargeability of debts*. S. 2159 in 97th Congress. Prohibits debts incurred as a result of an act of drunk driving from being discharged in bankruptcy.

Subt. E: *Referee's Salary and Expense Fund Amendments* (Drawn from S. 863 in 97th Congress). Corrects a drafting error in the 1978 Act which requires a handful of corporate debtors in bankruptcy to continue making payments to the non-existent fund.

Subt. F: *Repurchase Agreements Amendments*. Proposal of the Federal Reserve Board, which exempts repurchase agreements from the automatic stay in bankruptcy.

Subt. G: *Timesharing Agreements Amendments*. S. 3027 in the 97th Congress, S. 492 in the 98th. This subtitle provides that persons who hold timesharing agreements shall be granted a lien on the property involved when the timesharing contractor goes bankrupt and the trustee terminates the timesharing contract, and other provisions.

Subt. H: *Bankruptcy Oversight*. This subtitle directs the Administrative Office to collect information on bankruptcy filings regarding levels of debtor income and assets, debtor living expenses, and total amounts recovered for creditors in proceedings under Chapters 7, 11, and 13. This information will assist Congress in analyzing the functioning of the bankruptcy system.

Subt. I: *Technical and Clarifying Amendments*. The bulk of the provisions in this subtitle are drawn from S. 863, which passed the

Senate by unanimous consent in 1981. The provisions correct grammatical, punctuation, and spelling errors in the code, clarify the intent of the drafters in certain sections, and generally refine procedures.

Subt. J: *Severance clause, effective dates.*

B. SECTIONAL ANALYSIS

1. Subtitle A

Sec. 201: Title.

Sec. 202(a)&(b): These sections amend sections 301 and 302 of title 11 for the purpose of creating a mechanism by which individual debtors in bankruptcy can obtain the protections of the automatic stay pending the completion of debtor counseling as provided for in Section 203 of the bill. Under the provisions of the bill, debtors would commence a case under Chapter 7 by filing a petition with the court which contains an initial designation of relief under that chapter. Upon the filing of such a petition, the debtor would have all the rights, including the right to the protections of the automatic stay, that would have been available under prior law and that would exist if the debtor were to make Chapter 7 his final designation. Similarly, a debtor would commence a case under Chapter 13 by filing a petition with the initial designation that relief was sought under that Chapter, and would have all the rights, including the right to the protections of the automatic stay, that would have been available under prior law and that would exist if the debtor were to make Chapter 13 his final designation. The only reason for referring to the initial designation as conditional is to assure that debtors receive counseling before making a final decision on whether to proceed under Chapter 7 or Chapter 13 in accordance with the new 521(a)(3) of title 11.

Sec. 202(c): This section authorizes a court to dismiss a case brought under Chapter 7 if the filing represents a substantial abuse of that Chapter. Under this provision, the court may not dismiss a case in response to a request or suggestion from any party in interest, nor may a party in interest make such a request or suggestion. Instead, the case may be dismissed only where the court acting independently on its own motion, finds substantial abuse and in such case, the court must make an express finding of substantial abuse.

This provision represents a balancing of two interests. It preserves the fundamental concept embodied in our bankruptcy laws that debtors who cannot meet debts as they come due should be able to relinquish non-exempt property in exchange for a fresh start. At the same time, however, it upholds creditors' interests in obtaining repayment where such repayment would not be a burden.

Crushing debt burdens and severe financial problems place enormous strains on borrowers and their families. Family life, personal emotional health, or work productivity often suffers. By enabling individuals who cannot meet their debts to start a new life, unburdened with debts they cannot pay, the bankruptcy laws allow troubled borrowers to become productive members of their communities. Nothing in this bill denies such borrowers with unaffordable

TAB 11

Calendar No. 102

98TH CONGRESS 1st Session | SENATE | REPORT No. 98–65

OMNIBUS BANKRUPTCY IMPROVEMENTS ACT OF 1983

APRIL 26, 1983.—Ordered to be printed

Mr. THURMOND, from the Committee on the Judiciary, submitted the following

REPORT

[To accompany S. 445]

The Committee on the Judiciary, which considered the bill (S. 445) to make certain substantive changes to Public Law 95–598, the Bankruptcy Reform Act of 1978, having considered the same, reports favorably thereon as amended and recommends that the bill as amended do pass.

I. PURPOSE OF THE BILL

The purpose of the bill is to make certain substantive changes in Public Law 95–598, the Bankruptcy Reform Act of 1978.

II. INTRODUCTION AND HISTORY OF THE BILL

On July 12, 1978, the Committee on the Judiciary reported S. 2226, the Senate version of the Bankruptcy Reform Act of 1978. On September 20, 1978, H.R. 8200, with further amendments, was passed again by the House. On October 5, 1978, the Senate repassed H.R. 8200, with additional amendments. Finally, on October 6, 1978, the House accepted the final Senate changes and cleared the bill for signature by the President. On November 6, 1978, President Carter signed the bill and it became Public Law 95–598. On October 1, 1979, Public Law 95–598, styled the Bankruptcy Reform Act of 1978, went into effect.

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Significant provisions of Subtitle I are discussed in the sectional analysis which follows this summary of the bill contents

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A. SUMMARY

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Subt. F: *Repurchase Agreements Amendments*. Proposal of the Federal Reserve Board, which exempts repurchase agreements from the automatic stay in bankruptcy.

Subt. G: *Timesharing Agreements Amendments*. S. 3027 in the 97th Congress, S. 492 in the 98th. This subtitle provides that persons who hold timesharing agreements shall be granted a lien on the property involved when the timesharing contractor goes bankrupt and the trustee terminates the timesharing contract, and other provisions.

Subt. H: *Bankruptcy Oversight*. This subtitle directs the Administrative Office to collect information on bankruptcy filings regarding levels of debtor income and assets, debtor living expenses, and total amounts recovered for creditors in proceedings under Chapters 7, 11, and 13. This information will assist Congress in analyzing the functioning of the bankruptcy system.

Subt. I: *Technical and Clarifying Amendments*. The bulk of the provisions in this subtitle are drawn from S. 863, which passed the

Senate by unanimous consent in 1981. The provisions correct grammatical, punctuation, and spelling errors in the code, clarify the intent of the drafters in certain sections, and generally refine procedures.

Subt. J: *Severance clause, effective dates.*

B. SECTIONAL ANALYSIS

1. Subtitle A

Sec. 201: Title.

Sec. 202(a)&(b): These sections amend sections 301 and 302 of title 11 for the purpose of creating a mechanism by which individual debtors in bankruptcy can obtain the protections of the automatic stay pending the completion of debtor counseling as provided for in Section 203 of the bill. Under the provisions of the bill, debtors would commence a case under Chapter 7 by filing a petition with the court which contains an initial designation of relief under that chapter. Upon the filing of such a petition, the debtor would have all the rights, including the right to the protections of the automatic stay, that would have been available under prior law and that would exist if the debtor were to make Chapter 7 his final designation. Similarly, a debtor would commence a case under Chapter 13 by filing a petition with the initial designation that relief was sought under that Chapter, and would have all the rights, including the right to the protections of the automatic stay, that would have been available under prior law and that would exist if the debtor were to make Chapter 13 his final designation. The only reason for referring to the initial designation as conditional is to assure that debtors receive counseling before making a final decision on whether to proceed under Chapter 7 or Chapter 13 in accordance with the new 521(a)(3) of title 11.

Sec. 202(c): This section authorizes a court to dismiss a case brought under Chapter 7 if the filing represents a substantial abuse of that Chapter. Under this provision, the court may not dismiss a case in response to a request or suggestion from any party in interest, nor may a party in interest make such a request or suggestion. Instead, the case may be dismissed only where the court, acting independently on its own motion, finds substantial abuse and in such case, the court must make an express finding of substantial abuse.

This provision represents a balancing of two interests. It preserves the fundamental concept embodied in our bankruptcy laws that debtors who cannot meet debts as they come due should be able to relinquish non-exempt property in exchange for a fresh start. At the same time, however, it upholds creditors' interests in obtaining repayment where such repayment would not be a burden.

Crushing debt burdens and severe financial problems place enormous strains on borrowers and their families. Family life, personal emotional health, or work productivity often suffers. By enabling individuals who cannot meet their debts to start a new life, unburdened with debts they cannot pay, the bankruptcy laws allow troubled borrowers to become productive members of their communities. Nothing in this bill denies such borrowers with unaffordable and may solicit rejections as well as acceptances. Paragraph (2) deletes redundant language in section 1103(c).

Sec. 398: This amendment makes a necessary grammatical change.

Sec. 399: This amendment gives the court explicit power to regulate the duties of an examiner.

Sec. 400: This amendment makes clarifying changes.

Sec. 401: This amendment makes a clarifying change. The court may not ex parte order the trustee or debtor in possession to cease operating the debtor's business.

Sec. 402: This amendment makes clear that a deficiency claim will be eliminated only when the secured creditor has had an opportunity to credit bid the claim. The amendment adds abandonment or surrender of the collateral to the secured creditor as the possible events that would eliminate the deficiency claim.

Sec. 403: (a). This amendment makes a technical clarifying change and corrects a typographical error.

Subsection (b). this amendment makes stylistic changes.

Sec. 404: (a). This amendment makes a grammatical change.

Subsection (b). This amendment makes a technical stylistic change.

Sec. 405: (a). Paragraphs (1) through (5) make technical stylistic changes.

Subsection (b). This amendment makes necessary stylistic changes.

Sec. 406: This amendment makes stylistic changes.

Sec. 407: (a). This amendment makes clarifying amendments

Subsection (b). This amendment makes clarifying amendments.

Subsection (c). This amendment makes stylistic changes.

Sec. 408: (a). This amendment corrects a cross-referencing error.

Subsection (b). This amendment makes a stylistic change.

Subsection (c). This amendment makes typographical stylistic changes.

Subsection (d). This amendment makes a necessary clarifying change in section 1126(g).

Sec. 409: (a). This amendment makes stylistic changes.

Subsection (b). This amendment makes stylistic changes.

Sec. 410: (a). Paragraphs (1) through (6) make clarifying and stylistic changes. Paragraph (7) makes a stylistic change. The Code is keyed to "holders of claims" for style as opposed to "creditors." Paragraph (9) makes clear that a government taxing unit may be required to accept certain tax payments over a period of six (6) years following confirmation of a plan of reorganization. The extension provisions are broadened to include taxes that result from the sale of a capital asset, the recapture of an investment tax credit, the recapture of depreciation, or a similar event. This provision is particularly important in a reorganization plan where the debtor has for a period of years had substantial unrealized income as a result of capital gain. This is common in the instance where a farmer seeks to reorganize and use the sale of all or a major part of his farm to pay the debts provided for under the plan of reorganization. Without this sort of provision, the capital gains taxes due upon the sale of the farm are immediately due upon confirmation

TAB 12

Sen. 445, 98th Cong., 1st Sess.
(Cite as: A&P SEN. 445)

Arnold & Porter Legislative History: P.L. 98-353

BILLS

IN THE HOUSE OF REPRESENTATIVES

S. 445

AN ACT To amend title 11, United States Code, and for other purposes.
May 5, 1983

*1 Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Omnibus Bankruptcy Improvements Act of 1983".

TITLE I-BANKRUPTCY CODE AMENDMENTS

Subtitle A-Consumer Credit Amendments

SEC. 201. This subtitle may be cited as the "Consumer Debtor Bankruptcy Amendments Act of 1983".

SEC. 202. (a) Section 301 of title 11 of the United States Code, is amended-

(1) by striking out "A voluntary" and inserting in lieu thereof "(a) For a debtor who is not an individual, a voluntary"; and

(2) by adding at the end thereof the following new subsection:

"(b) With respect to an individual debtor or debtors, a voluntary case under this title is commenced by the filing with the bankruptcy court of a petition which conditionally designates a chapter under which relief is sought. The filing of such a petition shall constitute an order for relief under the provisions of the chapter conditionally designated. A final designation of the chapter under which relief is sought shall be made within the time period specified in section 521 of this title.".

(b) Section 302(a) of title 11, United States Code, is amended to read as follows:

"(a) A joint case under this title is commenced by the filing, with the bankruptcy court, of a single petition pursuant to section 301(b) by an individual and such individual's spouse. The commencement of a joint case under a chapter of this title constitutes an order for relief under the chapter conditionally designated in accordance with section 301(b).".

SEC. 203. (a) Section 305 of title 11 of the United States Code is amended by adding at the end thereof the following new subsection:

"(d)(1) Subject to the provisions of paragraph (2), the court on its own motion according to procedures established by rule, and not at the request or suggestion of any party in thirds in amount and more than one-half in number of allowed claims of such class, to be governed by subparagraph (B) of this paragraph; and

"(B) unless the aggregate value of the interests in such property of the holders of such claims is inconsequential, the class may elect, as provided under subparagraph (A) of this paragraph, that such claims of such class, whether or not the holders of such claims had recourse against the debtor and notwithstanding *112 section 506(a) of this title, are secured claims to the full extent that such claims are allowed.

"(2) The provisions of paragraph (1) of this subsection are limited to the purposes of this chapter and such paragraph shall not in any other way alter, affect, or create any right or liability of or in any other entity who may be liable with the debtor on a debt to which the provisions of such paragraph apply.".

SEC. 403. (a) Section 1112(a) of title 11 of the United States Code is amended-

(1) in paragraph (2), by striking out "is an involuntary case originally commenced under this chapter" and inserting in lieu thereof "originally was commenced as an involuntary case under this chapter"; and

(2) in paragraph (3), by striking out "on other than" and inserting in lieu thereof "other than on".

(b) Section 1112(b) of title 11 of the United States Code is amended-

(1) in paragraph (5), by inserting "a request made for" before "additional"; and

(2) in paragraph (8), by striking out "and" and inserting in lieu thereof "or".

SEC. 404. (a) Section 1121(c)(3) of title 11 of the United States Code is amended by striking out "the claims or interests of which are" and inserting in lieu thereof "of claims or *113 interests that is".

(b) Section 1121(d) of title 11 of the United States Code is amended by inserting "made within the respective periods specified in subsection (c) of this section" after "interest".

SEC. 405. (a) Section 1123(a) of title 11 of the United States Code is amended-

(1) by striking out "A" and inserting in lieu thereof "Notwithstanding any otherwise applicable nonbankruptcy law, a";

(2) in paragraph (1), by inserting commas after "classes of claims" and after "507(a)(7) of this title";

(3) in paragraph (3), by striking out "shall";

(4) in paragraph (5), by striking out "execution" and inserting in lieu thereof "implementation"; and

(5) in paragraph (5)(G), by inserting "of" after

"waiving".

(b) Section 1123(b)(2) of title 11 of the United States Code is amended by-

(1) striking out "or rejection" and inserting in lieu thereof ", rejection, or assignment"; and

(2) striking out "under section 365 of this title" and inserting in lieu thereof "under such section".

SEC. 406. Section 1124 of title 11 of the United States Code is amended-

*114 (1) by amending paragraph (2)(A) to read as follows:

"(A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title;"; and

(2) in paragraph (3)(B)(i), by striking out "and" and inserting in lieu thereof "or".

SEC. 407. (a) Section 1125(a) of title 11 of the United States Code is amended-

(1) in paragraph (1), by inserting ", but need not include such information about any other possible or proposed plan" after "plan";

(2) in paragraph (2)(B), by inserting "the" after "with"; and

(3) in paragraph (2)(C), by inserting "of" after "holders".

(b) Section 1125(d) of title 11 of the United States Code is amended by-

(1) inserting "required under subsection (b) of this section" after "statement" the first place it appears; and

(2) inserting ", or otherwise seek review of," after "appeal from".

*115 (c) Section 1125(e) of title 11 of the United States Code is amended by-

(1) inserting "acceptance or rejection of a plan" after "solicits"; and

(2) inserting "solicitation of acceptance or rejection of a plan or" after "governing".

SEC. 408. (a) Section 1126(b)(2) of title 11 of the United States Code is amended by striking out "1125(a)(1)" and inserting in lieu thereof "1125(a)".

(b) Section 1126(d) of title 11 of the United States Code is amended by inserting a comma after "such interests" the first place it appears.

(c) Section 1126(f) of title 11 of the United States Code is amended by-

(1) striking out "is deemed" and inserting in lieu thereof ", and each holder of a claim or interest of such class, are deemed";

TAB 13

Citation Search Result Rank(R) 4 of 10 Database BANKR84-LH

A&P H.R. REP. 98-882
H.R. Rep. No. 882, 98th Cong., 2d Sess. 1984
(Cite as: A&P H.R. REP. 98-882)

Arnold & Porter Legislative History: P.L. 98-353

REPORTS

Bankruptcy Amendments of 1984
June 29, 1984

[To accompany H.R. 5174]

*1 Mr. Rodino, from the committee of conference, submitted the following

CONFERENCE REPORT

The committee of conference on the disagreeing votes of the two Houses on the
amendment of the Senate to the bill (H.R. 5174) to provide for the appointment
of United States Bankruptcy judges under article III of the Constitution, to
amend title 11 of the United States Code for the purpose of making certain
changes in the personal bankruptcy law, of making certain changes regarding
grain storage facilities, and of clarifying the circumstance which collective
bargaining agreements may be rejected in cases under chapter 11, and for other
rposes, having met, after full and free conference, have agreed to recommend
d do recommend to their respective Houses as follows:
That the House recede from its disagreement to the amendment of the Senate to
the text of the bill and agree to the same with an amendment as follows:
In lieu of the matter proposed to be inserted by the Senate amendment insert
the following:

That this Act may be cited as the "Bankruptcy Amendments and Federal Judgeship Act of 1984".

TITLE I--BANKRUPTCY JURISDICTION AND PROCEDURE

Sec. 101. (a) Section 1334 of title 28, United States Code, is amended to read as follows:

"s 1334. Bankruptcy cases and proceedings

"(a) Except as provided in subsection (b) of this section, the district courts
shall have original and exclusive jurisdiction of all cases under title 11.
*2 "(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction
on a court or courts other than the district courts, the district courts shall
have original but not exclusive jurisdiction of all civil proceedings arising
under title 11, or arising in or related to cases under title 11.
"(c)(1) Nothing in this section prevents a district court in the interest of
justice, or in the interest of comity with State courts or respect for State
law, from abstaining from hearing a particular proceeding arising under title 11
arising in or related to a case under title 11.
(2) Upon timely motion of a party in a proceeding based upon a State law claim
or State law cause of action, related to a case under title 11 but not arising

Sec. 500. (a) Section 1103(b) is amended by--
(1) inserting "having an adverse interest" after "entity"; and
(2) adding at the end thereof the following: "Representation of one or more creditors of the same class as represented by the committee shall not per se constitute the representation of an adverse interest.".
(b) Section 1103(c) of title 11 of the United States Code is amended--
(1) in paragraph (3), by--
*56 (A) striking out "recommendations" and inserting in lieu thereof "determinations"; and
(B) inserting "or rejections" after "acceptances"; and
(2) in paragraph (4), by striking out ", if a trustee or examiner, as the case may be, has not previously been appointed under this chapter in the case".
Sec. 501. Section 1105 of title 11 of the United States Code is amended by striking out "estate, and" and inserting in lieu thereof "estate and of the".
Sec. 502. Section 1106(b) of title 11 of the United States Code is amended by inserting ", except to the extent that the court orders otherwise," before "any other".
Sec. 503. Section 1107(a) of title 11 of the United States Code is amended by inserting "serving in a case" after "on a trustee".
Sec. 504. Section 1108 of title 11 of the United States Code is amended by inserting ", on request of a party in interest and after notice and a hearing," after "court".
Sec. 505. (a) Section 1112(a) of title 11 of the United States Code is amended -
(1) in paragraph (2), by striking out "is an involuntary case originally commenced under this chapter" and inserting in lieu thereof "originally was commenced as an involuntary case under this chapter"; and
(2) in paragraph (3), by striking out "on other than" and inserting in lieu thereof "other than on".
(b) Section 1112(b) of title 11 of the United States Code is amended--
(1) in paragraph (5), by inserting "a request made for" before "additional"; and
(2) in paragraph (8), by striking out "and" and inserting in lieu thereof "or".
Sec. 506. (a) Section 1121(c)(3) of title 11 of the United States Code is amended by striking out "the claims or interests of which are" and inserting in lieu thereof "of claims or interests that is".
(b) Section 1121(d) of title 11 of the United States Code is amended by inserting "made within the respective periods specified in subsection (c) of this section" after "interest".
Sec. 507. (a) Section 1123(a) of title 11 of the United States Code is amended--
(1) by striking out "A" and inserting in lieu thereof "Notwithstanding any otherwise applicable nonbankruptcy law, a";
(2) in paragraph (1), by--
(A) inserting a comma after "classes of claims"; and
(B) by striking out "507(a)(6) of this title" and inserting in lieu thereof "507(a)(7) of this title,";
(3) in paragraph (3), by striking out "shall";
(4) in paragraph (5), by striking out "execution" and inserting in lieu

thereof "implementation"; and
(5) in paragraph (5)(G), by inserting "of" after "waiving".
(b) Section 1123(b)(2) of title 11 of the United States Code is amended by--
(1) striking out "or rejection" and inserting in lieu thereof ", rejection, or assignment"; and
*57 (2) striking out "under section 365 of this title" and inserting in lieu thereof "under such section".
Sec. 508. Section 1124 of title 11 of the United States Code is amended--
(1) by amending paragraph (2)(A) to read as follows:
"(A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title;"; and
(2) in paragraph (3)(B)(i), by striking out "and" and inserting in lieu thereof "or".
Sec. 509. (a) Section 1125(a) of title 11 of the United States Code is amended--
(1) in paragraph (1), by inserting ", but adequate information need not include such information about any other possible or proposed plan" after "plan";
(2) in paragraph (2)(B), by inserting "the" after "with"; and
(3) in paragraph (2)(C), by inserting "of" after "holders".
(b) Section 1125(d) of title 11 of the United States Code is amended by
(1) inserting "required under subsection (b) of this section" after "statement" the first place it appears; and
(2) inserting ", or otherwise seek review of," after "appeal from".
(c) Section 1125(e) of title 11 of the United States Code is amended by--
(1) inserting "acceptance or rejection of a plan" after "solicits"; and
(2) inserting "solicitation of acceptance or rejection of a plan or" after "governing".
Sec. 510. (a) Section 1126(b)(2) of title 11 of the United States Code is amended by striking out "1125(a)(1)" and inserting in lieu thereof "1125(a)"
(b) Section 1126(d) of title 11 of the United States Code is amended by inserting a comma after "such interests" the first place it appears.
(c) Section 1126(f) of title 11 of the United States Code is amended by--
(1) striking out "is deemed" and inserting in lieu thereof ", and each holder of a claim or interest of such class, are conclusively presumed";
(2) striking out "solicitation" and inserting in lieu thereof "solicitation"; and
(3) striking out "interest" and inserting in lieu thereof "interests".
(d) Section 1126(g) of title 11 of the United States Code is amended by striking out "any payment or compensation" and inserting in lieu thereof "receive or retain any property".
Sec. 511. (a) Section 1127(a) of title 11 of the United States Code is amended by--
(1) inserting "of a plan" after "After the proponent"; and
(2) inserting "of such plan" after "modification".
(b) Section 1127(b) of title 11 of the United States Code is amended by striking out "the court, after notice and a hearing, confirms *58 such plan, as modified, under section 1129 of this title, and circumstances warrant such modification" and inserting in lieu thereof "circumstances warrant such

TAB 14

LEGISLATIVE HISTORY
P.L. 98-353

BANKRUPTCY AMENDMENTS AND FEDERAL JUDGESHIP ACT OF 1984

P.L. 98-353, see page 98 Stat. 333

House Conference Report No., 98-882
June 29, 1984 [To accompany H.R. 5174]

Cong. Record Vol. 130 (1984)

DATES OF CONSIDERATION AND PASSAGE

House March 21, June 29, 1984

Senate June 19, 29, 1984

No Senate Report or House Report was submitted with this legislation. The House Conference Report did not contain a Joint Explanatory Statement. Statements by Legislative Leaders are set out.

STATEMENTS BY LEGISLATIVE LEADERS

STATEMENT BY THE HON. PETER W. RODINO, JR., CHAIRMAN OF THE HOUSE COMMITTEE ON THE JUDICIARY, UPON THE CONSIDERATION OF THE CONFERENCE REPORT ON H.R. 5174.

130 Congressional Record H 7489, June 29, 1984

Mr. Speaker, today, to the surprise, amazement and relief of many, I am sure, if not all, I rise to take up the result of the conference on H.R. 5714, the bankruptcy amendments and Federal Judgeship Act of 1984.

Let me quickly outline the provisions of our agreement. As all of us know, that is a very complex, complicated measure. Title I creates a new bankruptcy court arrangement to replace the provisions enacted in the Bankruptcy Reform Act of 1978—Public Law 95-598—which were found unconstitutional by the U.S. Supreme Court in the case of *Northern Pipeline v. Marathon Pipeline Co.*, 458 U.S. 50 (1982).

The conferees adopted most of the provisions creating this new bankruptcy court arrangement that were contained in the bill passed by this body.

Title II creates 85 additional district court and court of appeals article III judgeships. Forty of these positions are to take effect in 1984 and forty-five are to take effect in 1985.

Title III provides for certain amendments to title 11 of the United States Code which is the Bankruptcy Code. This body and the other body agreed to the amendments contained in subtitle A of title III, commonly referred to as the consumer credit amendments. Identical provisions were passed by both bodies, and the conferees did not alter the consumer credit amendments. These amendments are fair to both debtors and creditors, and contain no threshold or future income test.

Subtitle B of title III contains amendments relating to a grain storage facility bankruptcy. Each body passed very similar grain elevator provisions. The conferees adopted the other body's language.

TAB 15

PUBLIC LAW 98-353 [H.R. 5174]: July 10, 1984

BANKRUPTCY AMENDMENTS AND FEDERAL JUDGESHIP ACT OF 1984

For Legislative History of Act, see p. 576

An Act to amend title 28 of the United States Code regarding jurisdiction of bankruptcy proceedings, to establish new Federal judicial positions, to amend title 11 of the United States Code, and for other purposes.

Be it enacted by the Senate and House of Representatives of the United States of America in Congress assembled, That this Act may be cited as the "Bankruptcy Amendments and Federal Judgeship Act of 1984". Bankruptcy Amendments and Federal Judgeship Act of 1984. 28 USC 151 note.

TITLE I—BANKRUPTCY JURISDICTION AND PROCEDURE

SEC. 101. (a) Section 1334 of title 28, United States Code, is amended to read as follows:

"§ 1334. Bankruptcy cases and proceedings

"(a) Except as provided in subsection (b) of this section, the district courts shall have original and exclusive jurisdiction of all cases under title 11. 11 USC 101 et seq.

"(b) Notwithstanding any Act of Congress that confers exclusive jurisdiction on a court or courts other than the district courts, the district courts shall have original but not exclusive jurisdiction of all civil proceedings arising under title 11, or arising in or related to cases under title 11.

"(c)(1) Nothing in this section prevents a district court in the interest of justice, or in the interest of comity with State courts or respect for State law, from abstaining from hearing a particular proceeding arising under title 11 or arising in or related to a case under title 11.

"(2) Upon timely motion of a party in a proceeding based upon a State law claim or State law cause of action, related to a case under title 11 but not arising under title 11 or arising in a case under title 11, with respect to which an action could not have been commenced in a court of the United States absent jurisdiction under this section, the district court shall abstain from hearing such proceeding if an action is commenced, and can be timely adjudicated, in a State forum of appropriate jurisdiction. Any decision to abstain made under this subsection is not reviewable by appeal or otherwise. This subsection shall not be construed to limit the applicability of the stay provided for by section 362 of title 11, United States Code, as such section applies to an action affecting the property of the estate in bankruptcy.

"(d) The district court in which a case under title 11 is commenced or is pending shall have exclusive jurisdiction of all of the property, wherever located, of the debtor as of the commencement of such case, and of the estate.". Gifts and property.

(b) The table of sections for chapter 85 of title 28, United States Code, is amended by amending the item relating to section 1334 to read as follows:

"1334. Bankruptcy cases and proceedings.".

(1) in paragraph (2), by striking out "is an involuntary case originally commenced under this chapter" and inserting in lieu thereof "originally was commenced as an involuntary case under this chapter"; and

(2) in paragraph (3), by striking out "on other than" and inserting in lieu thereof "other than on".

(b) Section 1112(b) of title 11 of the United States Code is amended—

(1) in paragraph (5), by inserting "a request made for" before "additional"; and

(2) in paragraph (8), by striking out "and" and inserting in lieu thereof "or".

SEC. 506. (a) Section 1121(c)(3) of title 11 of the United States Code is amended by striking out "the claims or interests of which are" and inserting in lieu thereof "of claims or interests that is".

(b) Section 1121(d) of title 11 of the United States Code is amended by inserting "made within the respective periods specified in subsection (c) of this section" after "interest".

SEC. 507. (a) Section 1123(a) of title 11 of the United States Code is amended—

(1) by striking out "A" and inserting in lieu thereof "Notwithstanding any otherwise applicable nonbankruptcy law, a";

(2) in paragraph (1), by—

(A) inserting a comma after "classes of claims"; and

(B) by striking out "507(a)(6) of this title" and inserting in lieu thereof "507(a)(7) of this title,";

(3) in paragraph (3), by striking out "shall";

(4) in paragraph (5), by striking out "execution" and inserting in lieu thereof "implementation"; and

(5) in paragraph (5)(G), by inserting "of" after "waiving".

(b) Section 1123(b)(2) of title 11 of the United States Code is amended by—

(1) striking out "or rejection" and inserting in lieu thereof ", rejection, or assignment"; and

(2) striking out "under section 365 of this title" and inserting in lieu thereof "under such section".

SEC. 508. Section 1124 of title 11 of the United States Code is amended—

(1) by amending paragraph (2)(A) to read as follows:

"(A) cures any such default that occurred before or after the commencement of the case under this title, other than a default of a kind specified in section 365(b)(2) of this title;" Ante p. 361

and

(2) in paragraph (3)(B)(i), by striking out "and" and inserting in lieu thereof "or".

SEC. 509. (a) Section 1125(a) of title 11 of the United States Code is amended—

(1) in paragraph (1), by inserting ", but adequate information need not include such information about any other possible or proposed plan" after "plan";

(2) in paragraph (2)(B), by inserting "the" after "with"; and

(3) in paragraph (2)(C), by inserting "of" after "holders".

(b) Section 1125(d) of title 11 of the United States Code is amended by—

(1) inserting "required under subsection (b) of this section" after "statement" the first place it appears; and