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12 PACIFIC GAS AND ELECTRIC COMPANY

13 UNITED STATES BANKRUPTCY COURT
14 NORTHERN DISTRICT OF CALIFORNIA
15 SAN FRANCISCO DIVISION

16 In re
17 PACIFIC GAS AND ELECTRIC
18 COMPANY, a California corporation,
19 Debtor.
20 Federal I.D. No. 94-0742640

Case No. 01-30923 DM

Chapter 11 Case

Date: June 20, 2002
Time: 1:30 p.m.
Place: 235 Pine Street, 22nd Floor
San Francisco, California

21 NOTICE OF MOTION AND MOTION FOR AUTHORITY TO INCUR
22 EXPENSES RELATED TO THE FERC LICENSE APPLICATION FOR
23 HAMILTON BRANCH HYDROELECTRIC FACILITY; MEMORANDUM OF
24 POINTS AND AUTHORITIES IN SUPPORT THEREOF

25 [Supporting Declaration of Thomas A. Jereb Filed Concurrently Herewith]
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Asst
Mod:
Ridgely Hillman

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1 **MEMORANDUM OF POINTS AND AUTHORITIES**

2 Pacific Gas and Electric Company, the debtor and debtor in possession in the
3 above-captioned Chapter 11 case ("PG&E"), requests authority to incur expenses for
4 environmental studies and reports that will be required in connection with a license
5 application to the Federal Energy Regulatory Commission ("FERC") for a currently
6 unlicensed hydroelectric facility. This request is made pursuant to Bankruptcy Code Section
7 363(b)(1).
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9 **I. FACTUAL BACKGROUND¹**

10 PG&E filed a voluntary petition for relief under Chapter 11 of the Bankruptcy
11 Code on April 6, 2001. A trustee has not been appointed, and PG&E continues to function
12 as a debtor-in-possession pursuant to Sections 1107 and 1108 of the Bankruptcy Code.

13 On April 19, 2002, PG&E, together with its parent corporation, PG&E
14 Corporation, filed its amended Plan of Reorganization (as amended from time to time, the
15 "Plan"). The Court-approved Disclosure Statement for the Plan (the "Disclosure
16 Statement"), along with the Plan, will be mailed to creditors for voting on June 17, 2002. A
17 Plan confirmation hearing has been set for August 1, 2002.

18 The Plan generally provides for the creation of three new companies, ETrans
19 LLC, GTrans LLC and Electric Generation LLC, whereby PG&E will separate its operations
20 into four lines of business based on PG&E's historical functions. Accordingly, the
21 Reorganized Debtor will continue the retail gas and electric distribution business, ETrans
22 LLC will operate the electric transmission business, GTrans LLC will operate the interstate
23 gas transmission business, and Electric Generation LLC will operate the electric generation
24 business.
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27 ¹ The evidentiary basis and support for the facts set forth in this Motion are contained
28 in the Declaration of Thomas A. Jereb filed concurrently herewith.

1 A. **Description of Environmental Studies and Reports Required for the**
2 **FERC License Application for Hamilton Branch Hydroelectric Facility.**

3 Section VI. D.1. of the Disclosure Statement sets forth PG&E's agreement to file
4 an application for a FERC operating license for the Hamilton Branch Hydroelectric Facility
5 ("Hamilton Branch"). FERC previously determined that PG&E is not required to obtain a
6 FERC license to operate Hamilton Branch. However, after reviewing previous versions of
7 PG&E's Plan and Disclosure Statement, the California Public Utilities Commission
8 ("CPUC") contended that Hamilton Branch would be "completely unregulated" under the
9 Plan, as a result of the transfer of Hamilton Branch to Electric Generation LLC ("Gen").
10 PG&E disagreed with the CPUC since Hamilton Branch is and would remain subject to state
11 regulation. Nonetheless, PG&E agreed to file an application with FERC for a license for
12 Hamilton Branch and added the following language to the final version of the Disclosure
13 Statement:

14 Additionally, the Debtor currently owns three small hydroelectric projects that
15 are not subject to FERC operating licenses because the FERC has disclaimed
16 mandatory licensing jurisdiction over these projects. Two of these projects, Lime
17 Saddle and Coal Canyon (and their associated lands, appurtenances and water
18 contracts), will be retained by the Reorganized Debtor, subject to existing
19 regulatory jurisdiction. [footnote omitted]. The third project, Hamilton Branch,
will be transferred to Gen or a subsidiary of Gen and will be incorporated within
its FERC license application for the Upper North Fork Feather River Project,
FERC Project No. 2105, to be submitted to the FERC no later than October 31,
2002, or an amendment to that application. See Disclosure Statement, Section
VI. D.1.

20 The first and most immediate step in preparing the application for a FERC license
21 is to perform environmental studies and prepare environmental reports (collectively, the
22 "Environmental Studies") for Hamilton Branch. The Environmental Studies are required as
23 part of the FERC-mandated "Environmental Report" to be included as part of the license
24 application, and include the following study areas: (i) water use and quality; (ii) fish, wildlife
25 and botanical resources; (iii) historical and archeological resources; (iv) recreational
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resources; and (v) land management and aesthetics.² After the Environmental Studies are completed, a draft of the license application, including the Environmental Report, must be made available to various resource agencies (state and federal) and Indian tribes for comment during a 90-day review period. In addition, PG&E typically makes the draft license application available to the public for comment during this same time period. Depending on the comments received, the Environmental Report may need to be amended before it is filed with FERC.

PG&E proposes to use the following consultants for the Environmental Studies, including any related work in amending the Environmental Report that may be necessary after the review and comment period:³

Consultant Firm

Study Subject

Foster Wheeler Environmental Corp.
EDAW Inc.
Confluence Research and Consulting
Resource Decisions
ECORP Consulting, Inc.
Garcia and Associates
Spring Rivers Ecological Sciences
Hydroacoustic Technology, Inc.
Thomas R. Payne & Assoc.
Entrix, Inc.
Wreco
PAR Environmental
Albian Environmental

Land Use, Visual
Recreation
Boating and Fishing
Recreation Economics
Aquatic
Amphibians and Rare Plants
Mollusk
Fish Entrainment
Fisheries and Water Temperature
Geomorphology
Sediments and Erosion
Prehistoric and Historic Resources
Cultural Resources

PG&E requests approval to incur approximately \$1 million in expenses to be paid to the consultants for the Environmental Studies and related work that may be necessary after the review and comment period.

² See 18 Code of Federal Regulations, Section 4.50 et seq. Section 4.51(f) lists the required contents of the Environmental Report.

³ As the project proceeds, it may be necessary to retain additional consultants that are not identified here. However, the budget set forth herein includes anticipated expenses for all consulting work that may be required in connection with the Environmental Studies.

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2 **B. Current Need for Approval of Expenses for Environmental Studies**
3 **Related to the FERC License Application for Hamilton Branch**

4 As noted above, PG&E has agreed to apply for a FERC license for Hamilton
5 Branch in connection with the Plan. Hamilton Branch is located in Plumas and Lassen
6 Counties, California, in the same general area as other PG&E hydroelectric facilities that are
7 part of the Upper North Fork Feather River Project ("Feather River Project"). PG&E is
8 currently in the process of preparing an application to re-license these hydroelectric
9 facilities, to be filed by October 31, 2002. PG&E intends to amend the Feather River Project
10 application to add Hamilton Branch, so that Hamilton Branch will become part of the
11 Feather River Project.

12 The consultants described above are already under contract with PG&E for
13 similar work in connection with the Feather River Project. PG&E believes that the total cost
14 for the FERC license application for Hamilton Branch can be minimized by amending the
15 Feather River Project application to include Hamilton Branch, along with using the same
16 consultants.

17 After the Feather River Project application is filed and FERC has reviewed it,
18 FERC will establish a deadline for filing amendments to the application, including an
19 amendment related to Hamilton Branch. PG&E anticipates that the amendment deadline
20 may be set as early as June 1, 2003. However, the work required to perform the
21 Environmental Studies is season-dependent. Many of the studies must be commenced prior
22 to the summer season or risk being delayed an entire year. If the Environmental Studies are
23 not performed during the summer of 2002, the delay could jeopardize Gen's ability to apply
24 for a FERC license for Hamilton Branch in a timely manner. Therefore, it is critical that this
25 work begin now, in advance of Plan confirmation.

26 To the extent that subsequent events demonstrate that the Environmental Studies
27 will not be necessary, the work can be terminated immediately. PG&E's standard
28 contractual provisions in place with the consultants listed above do not guarantee any future
work or any minimum amount of revenue. PG&E also maintains the right to terminate the

1 contracts at any time without cause, in which case PG&E is liable only for the work
2 performed to the date of termination plus costs reasonably incurred by the consultants in
3 terminating any work in progress.

4 5 II.

6 THE COSTS FOR ENVIRONMENTAL STUDIES FOR 7 HAMILTON BRANCH SHOULD BE APPROVED PURSUANT 8 TO SECTION 363(b)(1) OF THE BANKRUPTCY CODE

8 As set forth above, PG&E seeks approval to pay the various consultants
9 approximately \$1 million as a use of estate property that is outside of the ordinary course of
10 business under Bankruptcy Code Section 363(b)(1). Since the services relate to a license
11 application required by the Plan, PG&E believes that the purpose and scope of this
12 expenditure may be characterized as outside of the ordinary course of business and is
13 therefore seeking Court approval.

14 PG&E believes that the consultants described above should not be considered
15 "professional persons" requiring any approval under Bankruptcy Code Section 327(a). This
16 is due both to the nature of the services to be provided and to the consultants' limited role in
17 connection with PG&E's reorganization proceeding. See In re That's Entertainment Mktg.
18 Group, Inc., 168 B.R. 226, 230 (N.D. Cal. 1994); see also In re Saybrook Mfg. Co., Inc., 108
19 B.R. 366, 368-369 (Bankr. M.D. Ga. 1989) (in determining whether a person is a
20 professional for purposes of Section 327, courts consider not only the nature of the services
21 provided but also how central the services are to the reorganization proceeding). Although
22 the Environmental Studies are related to implementation of the Plan, PG&E believes that
23 these services should not be considered "central" to the Chapter 11 case or the Plan
24 proceedings.

25 The Court has considerable discretion in approving a request pursuant to Section
26 363(b)(1) of the Bankruptcy Code ("[t]he trustee, after notice and a hearing, may use, sell,
27 or lease, other than in the ordinary course of business, property of the estate"). See In re
28 Montgomery Ward Holding Corp., 242 B.R. 147, 153 (D. Del. 1999) (affirming the

1 bankruptcy court's decision to approve expenditure for employee incentive programs, noting
2 that bankruptcy court has considerable discretion in approving a Section 363(b) motion).

3 In determining whether to authorize a transaction under Section 363(b)(1), courts
4 require a debtor to show that a sound business purpose justifies such actions, applying the
5 business judgment test. See, e.g., Stephens Indus., Inc. v. McClung, 789 F.2d 386, 389-90
6 (6th Cir. 1986); Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.), 722
7 F.2d 1063, 1071 (2d Cir. 1983); see also 3 Lawrence P. King, Collier on Bankruptcy
8 ¶363.02[1][g] (15th ed. rev. 1998).

9 Once the debtor has articulated a rational business justification, a presumption
10 attaches that the decision was made "on an informed basis, in good faith and in the honest
11 belief that the action taken was in the best interest of the [debtor]." See, e.g., Official
12 Comm. of Subordinated Bondholders v. Integrated Res., Inc. (In re Integrated Res., Inc.),
13 147 B.R. 650, 656 (S.D.N.Y. 1992) (citing Smith v. Van Gorkom, 488 A.2d 858, 872 (Del.
14 1985)).

15 Here, sound business justifications exist for approval of the expenditures related
16 to preparing a FERC license application for Hamilton Branch. PG&E requires the expertise
17 and resources of the consultants to perform the Environmental Studies that will be integral to
18 the preparation of the Environmental Report required by FERC. Delaying the work would
19 likely jeopardize PG&E's ability to timely meet its commitment set forth in the Disclosure
20 Statement, as the work is essential to preparing the amendment to the Feather River Project
21 application.

22 Also, PG&E is solvent and has sufficient cash to pay these expenses without
23 causing any detriment to its creditors.⁴ Thus, while there is the possibility that the Plan will
24 not be confirmed and therefore some of the Environmental Studies will become unnecessary,
25 this does not justify denial of the expenditure. See Montgomery Ward, 242 B.R. at 154 (no
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27 ⁴ As reflected in PG&E's April 2002 Monthly Operating Report, PG&E held more than
28 \$4.5 billion in cash reserves as of April 30, 2002.

1 requirement for debtor to show a successful prospect of reorganization in order to justify
2 expenditure request under Section 365(b)(1)). It is sufficient that PG&E currently has sound
3 business reasons for the expenditure. As shown above, any delay in performing the
4 Environmental Studies would likely prevent PG&E from submitting a license application for
5 Hamilton Branch in a timely manner. Performing the Environmental Studies now will
6 enable PG&E to file the FERC license application for Hamilton Branch in a timely and cost-
7 effective manner.

8
9 **CONCLUSION**

10 For all of the foregoing reasons, PG&E respectfully requests that the Court
11 approve the expenditures for the Environmental Studies and related work as set forth herein
12 and grant such other and further relief as may be just and appropriate.

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14 DATED: May 31, 2002

15 Respectfully,

16 HOWARD, RICE, NEMEROVSKI, CANADY,
17 FALK & RABKIN
A Professional Corporation

18 By: Julie Landau
19 JULIE B. LANDAU

20 Attorneys for Debtor and Debtor in Possession
21 PACIFIC GAS AND ELECTRIC COMPANY

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