

1 JAMES L. LOPES (No. 63678)  
2 JANET A. NEXON (No. 104747)  
3 KENNETH A. NEALE (No. 126904)  
4 HOWARD, RICE, NEMEROVSKI, CANADY,  
5 FALK & RABKIN  
6 A Professional Corporation  
7 Three Embarcadero Center, 7th Floor  
8 San Francisco, California 94111-4065  
9 Telephone: 415/434-1600  
10 Facsimile: 415/217-5910

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11 Attorneys for Debtor and Debtor in Possession  
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: July 30, 2002

Time: 1:30 p.m.

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

21 DECLARATION OF HUDSON T. MARTIN IN SUPPORT OF MOTION OF PACIFIC  
22 GAS AND ELECTRIC COMPANY FOR ORDER AUTHORIZING USE OF CASH  
23 COLLATERAL TO FACILITATE COMPLIANCE WITH APPLICABLE LAW

24 Add OGC Mail Center  
25 A001

26  
27  
28 DECLARATION OF HUDSON T. MARTIN ISO MOTION RE USE OF CASH COLLATERAL

HOWARD  
RICE  
NEMEROVSKI  
CANADY  
FALK  
& RABKIN  
A Professional Corporation

1 I, Hudson T. Martin, declare as follows:

2 1. I am the Director of the Insurance Department for PG&E Corporation,  
3 parent company of Pacific Gas and Electric Company, debtor and debtor in possession  
4 herein ("PG&E" or the "Debtor"), a position I have held since 1991. In such capacity, I am  
5 responsible for providing insurance and related risk-management services to PG&E, and  
6 managing the company's surety bond program. My department is responsible for filing  
7 applications to establish PG&E's self-insured status with local, state and federal agencies.

8 2. This Declaration is based on my personal knowledge of PG&E's operations  
9 and financial position. If called as a witness, I could and would testify competently to the  
10 facts stated herein.

11 3. I make this declaration in support of PG&E's motion for Order Authorizing  
12 Use of Cash Collateral to Facilitate Compliance with Applicable Law (the "Motion").

13 4. From time to time, in the ordinary course of its business, PG&E is involved  
14 in construction projects for which PG&E must hire outside contractors for purposes of the  
15 construction. In its capital budget for the current fiscal year, PG&E has allocated substantial  
16 funds for capital expenditures, some of which are slated for construction projects for which  
17 PG&E will hire outside contractors. California has recently enacted a law which requires  
18 PG&E to provide security to the contractor for PG&E's payment obligations under certain  
19 construction projects. In order to provide such security, PG&E will need to use up to \$24  
20 million of cash collateral for these purposes for projects commenced in 2002.

21 5. In addition, PG&E is required to provide certain financial assurances under  
22 applicable state and federal laws and regulations for environmental liability associated with  
23 closure remediation and/or post-closure monitoring and maintenance and third party  
24 compensation. While PG&E formerly was able to self-insure such liabilities, it is currently  
25 not able to meet the state's requirements for self-insurance, and thus is required to either  
26 provide escrow or trust accounts, letters of credit or bonds for such liabilities. PG&E could  
27 have up to \$30 million in such obligations over the next twelve months.

28 6. PG&E from time to time is required to provide financial assurances to

1 various local, state and federal agencies in connection with the ordinary course of its  
2 business. Where previously PG&E provided such financial assurances in the form of  
3 performance bonds, it no longer has the ability to obtain such bonds on an unsecured basis.

4 7. PG&E has determined that it will be required to post cash collateral for the  
5 required financial assurance arrangements—either to the bonding company, the letter of  
6 credit issuer, the trust account or escrow account, or the direct beneficiary of the financial  
7 assurance arrangement. PG&E intends to use cash escrow accounts or trust funds for these  
8 obligations whenever possible, as it believes that escrow accounts and trust funds represent  
9 the most cost-effective and readily available method for providing the necessary financial  
10 assurances.

11 8. Pursuant to California Civil Code Section 3110.5, an owner who contracts  
12 for a private work of improvement for construction, alteration, addition to or repair upon real  
13 property in an amount exceeding \$5,000,000 (if the owner's interest is a fee simple interest)  
14 or \$1,000,000 (if the owner's interest is less than a fee simple interest), must provide one of  
15 three specified forms of security for the project. The security must be in the form of (i) a  
16 payment bond from a California admitted surety meeting certain credit requirements; (ii) a  
17 letter of credit from a financial institution; or (iii) a cash payment to an escrow account  
18 maintained in California in which the contractor would have a first priority security interest.  
19 It is my understanding that the law requires collateral in the amount of 25% of the total  
20 amount of the contract if the contract is scheduled to be substantially completed within six  
21 months of commencement of the work, or 15% of the total amount of the contract in all  
22 other cases.

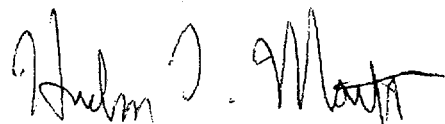
23 9. In the event that PG&E decides to use a payment bond or letter of credit to  
24 meet its obligations under Civil Code Section 3110.5 with respect to a particular  
25 construction contract, PG&E has determined that it will have to post cash collateral to secure  
26 its obligations to the surety or financial institution issuing such instrument. The use of an  
27 escrow account in which the contractor would have a security interest also would require  
28 PG&E to use cash collateral, but would be less expensive than the bond or letter of credit

1 alternative arrangements.

2 10. Under state and federal regulations, certain financial responsibility  
3 requirements are imposed on entities such as PG&E for environmental liability associated  
4 with remediation, third party compensation, closure, and/or post-closure monitoring and  
5 maintenance. For example, PG&E is required to place \$4,425,997 in trust for the benefit of  
6 the State of California Department of Toxic Substances Control for the Diablo Canyon  
7 Power Plant and the Martin Service Center by August 1, 2002. The trust is designed to  
8 cover closure and post-closure cost estimates and third party compensation for bodily injury  
9 and property damage, at certain sites. Further, on or before August 1, 2002, PG&E must  
10 place \$1,010,000 in trust for the benefit of the State of California Water Resources Control  
11 Board for third party compensation at petroleum underground storage tank sites (pursuant to  
12 the Code of Federal Regulations, Title 40, Part 280, Subpart H and the California Code of  
13 Regulations, Title 23, Division 3, Chapter 18, Article 3). PG&E anticipates that a number of  
14 other, similar requirements may be imposed in the future.

15 11. In addition to the categories set forth above, PG&E anticipates that it will  
16 need to provide additional financial assurances in the nature of cash deposits for a variety of  
17 different purposes. Examples of such purposes include satisfying requirements of  
18 governmental agencies, counties and cities in connection with applications for special  
19 licenses and permits, satisfying requirements of the Department of Motor Vehicles in  
20 connection with the ownership and operation of PG&E's vehicle fleet, and posting appeal  
21 bonds. PG&E anticipates that such miscellaneous financial assurance requirements will not  
22 exceed \$10 million over the next twelve-month period.

23 I declare under penalty of perjury under the laws of the United States of America  
24 and the State of California that the foregoing is true and correct. Executed this 10<sup>th</sup> day of  
25 July, 2002 at San Francisco, California.

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HUDSON T. MARTIN

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