JAMES L. LOPES (No. 63678)
JANET A. NEXON (No. 104747)
JULIE B. LANDAU (No. 162038)
HOWARD, RICE, NEMEROVSKI, CANADY,
FALK & RABKIN
A Professional Corporation
Three Embarcadero Center, 7th Floor
San Francisco, California 94111-4065
Telephone: 415/434-1600
Facsimile: 415/217-5910

50-275
323

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

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

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 Date: October 2, 2002 Time: 9:30 a.m. Place: 235 Pine Street, 22nd Floor San Francisco, California

NOTICE OF MOTION AND MOTION FOR AUTHORITY TO INCUR ADDITIONAL MISCELLANEOUS IMPLEMENTATION EXPENSES; MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT THEREOF

[SUPPORTING DECLARATIONS OF M. KIRK JOHNSON, LANCE MAEDA, MICHAEL MEKO, STEPHANIE MAGGARD AND JUNE RUCKMAN FILED SEPARATELY]

Add OGC ~~[illegible]~~ Mail Center
A001

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN

TABLE OF CONTENTS

TABLE OF AUTHORITIES

Page(s)

Cases

Statutes

Other Authorities

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

NOTICE OF MOTION AND MOTION

PLEASE TAKE NOTICE that on October 2, 2002 at 9:30 a.m., or as soon thereafter as the matter may be heard in the Courtroom of the Honorable Dennis Montali, located at 235 Pine Street, 22nd Floor, San Francisco, California, Pacific Gas and Electric Company, the debtor and debtor in possession in the above-captioned Chapter 11 case ("PG&E"), will and hereby does move the Court for entry of an Order Authorizing Additional Miscellaneous Implementation Expenses (the "Motion").

This Motion is based on this Notice of Motion and Motion, the accompanying Memorandum of Points and Authorities, the Declarations of M. Kirk Johnson, Lance Maeda, Michael Meko, Stephanie Maggard and June Ruckman, filed concurrently herewith, the record of this case and any evidence presented at or prior to the hearing on this Motion.

PLEASE TAKE FURTHER NOTICE that pursuant to Rule 9014-1(c)(2) of the Bankruptcy Local Rules for the Northern District of California, any written opposition to the Motion and the relief requested herein must be filed with the Bankruptcy Court and served upon appropriate parties (including counsel for PG&E, the Office of the United States Trustee and the Official Committee of Unsecured Creditors) at least five (5) days prior to the scheduled hearing date. If there is no timely objection to the requested relief, the Court may enter an order granting such relief without further hearing.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

MEMORANDUM OF POINTS AND AUTHORITIES

Pacific Gas and Electric Company, the debtor and debtor in possession in the above-captioned Chapter 11 case ("PG&E"), requests an order authorizing PG&E to incur additional miscellaneous expenses related to implementation of PG&E's proposed Plan of Reorganization, pursuant to Bankruptcy Code Section 363(b)(1).

I.

FACTUAL BACKGROUND

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

PG&E, together with its parent corporation, PG&E Corporation, has proposed a Plan of Reorganization (as amended from time to time, the "Plan"), which has recently been voted on by creditors, along with the competing plan of reorganization proposed by the California Public Utilities Commission. The confirmation hearing has been scheduled to commence on November 12, 2002.

The Plan generally provides for the creation of three new companies, ETrans LLC, GTrans LLC and Electric Generation LLC (collectively, the "New Entities"), whereby PG&E will separate its operations into four lines of business based on PG&E's historical functions. Accordingly, the Reorganized Debtor will continue the retail gas and electric distribution business, ETrans LLC will operate the electric transmission business, GTrans LLC will operate the interstate gas transmission business, and Electric Generation LLC will operate the electric generation business.

PG&E previously filed and obtained orders approving 11 motions seeking authority to incur costs related to implementation of the Plan. In the Motion for Authority to Incur Information Technology Consulting Expenses and the accompanying Declaration of Stephanie Maggard (the "Maggard Declaration"), filed on July 23, 2002, PG&E identified additional implementation projects that will need to commence before the Plan is confirmed

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

(the "Implementation Projects") and estimated that the total expenses for these Implementation Projects will range from $10.8 to $17.8 million. In the Motion for Authority to Incur Miscellaneous Implementation Expenses ("Miscellaneous Motion") filed on August 15, 2002, a portion of the Implementation Projects were covered for a total estimated cost of $1,397,180. This Motion covers additional Implementation Projects for a total estimated cost of $5,602,810.[1]

As explained in the supporting declarations, the cost estimates set forth herein are based on PG&E's initial scoping of the project requirements and negotiations with the consultants who have been selected to perform the work (or preliminary discussions with the potential consultants, as noted below). For each of the consulting firms, PG&E's standard contractual provisions in place with these firms (or to be included in any contracts to be executed hereafter) do not guarantee future work or any minimum amount of revenue. PG&E will also maintain the right to terminate the work at any time without cause, in which case PG&E is liable only for work performed to the date of termination plus costs reasonably incurred by the consultant in terminating any work in progress. There are a few exceptions, however, where PG&E has been unable to obtain the services without paying an initial set-up or flat fee, which cannot be recovered if the work is subsequently terminated. These exceptions have been described below, where applicable. In addition, the software license fees described below involve one time charges that cannot be recovered if the work is subsequently terminated.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

A. GTRANS BUSINESS PROCESSES.[2]

The following projects relate to the business requirements of GTrans LLC

[1] PG&E anticipates filing one or more motions in October to cover additional Implementation Projects not covered in the Miscellaneous Motion or this Motion. Also, certain projects described herein involve work that PG&E has decided can wait until Plan confirmation to commence, but will need to commence immediately thereafter. Where these projects have been included herein, it is noted that the expense will not be incurred until immediately after Plan confirmation.

[2] The facts set forth in this Section A are supported by the Declaration of M. Kirk Johnson filed concurrently herewith.

("GTrans"), the New Entity that will operate the interstate gas transmission line of business.

1. Credit Evaluations (Cost Estimate—$40,000).

GTrans will require credit evaluations to be performed for approximately 80 customers who hold Qualifying Facilities ("QF") agreements with PG&E. Under the terms of the QF agreements, PG&E purchases electricity from QF customers. PG&E also provides QF customers with gas and electric transmission services. PG&E currently may offset payments to the QF customers (for electricity purchased from them) with amounts due from the QF customers (for gas and electric transmission services). The ability to offset payments is a consideration in determining the creditworthiness of these QF customers.

Upon separation from PG&E, GTrans will provide gas transmission services to the QF customers but will not buy electricity from them and therefore not have the ability to offset described above. Accordingly, the QF customers must be evaluated to ensure their creditworthiness. This work must be completed prior to the Effective Date under the Plan (the "Plan Effective Date") in order for GTrans to commence gas transmission services to these customers after the Plan Effective Date. PG&E intends to conduct the credit evaluations immediately after the Plan is confirmed in order to allow sufficient time to complete the evaluation process, as well as the drafting and execution of any necessary credit instruments, in advance of the Plan Effective Date. PG&E is seeking approval of this expense now to avoid any delay in commencing this work immediately after Plan confirmation. In the event that the Plan is not confirmed, this work will not be performed.

PG&E has selected a management consulting and engineering firm, ESS Consulting, to perform the credit evaluations. The cost for this work will be approximately $40,000.

2. Virtual Metering (Cost Estimate—$140,000).

After the Plan Effective Date, GTrans will be a gas transmission business and PG&E will be one of its customers for gas deliveries. In order to bill PG&E for gas

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

deliveries, GTrans will need to measure the quantity of gas delivered to PG&E. Currently, the over 5,000 interconnection points between what will be the GTrans gas transmission system and the PG&E gas distribution system are not metered. In view of the large number of interconnection points, it is not economically feasible to install meters.

Therefore, instead of meters, the gas deliveries will be measured pursuant to a "virtual metering" methodology, which has been proposed pursuant to the Metered Quantity Determination Agreement ("MQDA"). As part of PG&E's applications filed on November 30, 2001 with the Federal Energy Regulatory Commission ("FERC") to approve the transactions contemplated by the Plan, PG&E filed the proposed MQDA and requested FERC's approval for its virtual metering methodology.

In order to create this virtual metering, a new database will be developed to serve as the central data repository for MQDA gas delivery information. The database will be used to calculate and provide a record of GTrans' gas deliveries to PG&E, and will be the sole source of information about these gas deliveries. It is estimated that the process of designing and developing the new database will take approximately three months. Following the development of the database, PG&E requires additional time to test the database in advance of the Plan Effective Date.

PG&E has selected two applications developers from Blackstone Technology Group to design, develop and implement the new database, working with PG&E business and systems analysts. Blackstone Technology Group is a consulting firm specializing in utility application solutions. PG&E estimates that this project will cost approximately $140,000.

B. REORGANIZED PG&E BUSINESS PROCESSES.

PG&E has identified several projects related to the business operations of Reorganized PG&E (referred to herein as PG&E), as described below, to be completed by or in advance of the Plan Effective Date. All of the work described below is necessary to establish important PG&E business processes that need to be developed as a result of the separation contemplated by the Plan.

1. Software Licenses And Related Expenses (Cost Estimate—$9,200).[3]

Currently, PG&E Corporation provides certain services to PG&E utilizing software products that are licensed by PG&E Corporation. As a result of the separation under the Plan, PG&E must purchase and install several software products so that it will be able to perform these functions internally. The total costs for these software licenses and related training and support services is approximately $9,200.

The types of software licenses that PG&E will need to purchase include: (i) software used to track employee contributions to PG&E's political action committee; (ii) software used to manage PG&E's pension and pension benefits funds; (iii) software used to train PG&E employees over the Internet on business ethics and compliance with legal and regulatory requirements; (iv) software used to track risk management and insurance requirements; and (v) software used for tax return preparation and tax solutions.

The foregoing software licenses must be purchased promptly to allow for time to install and configure the software as part of a particular business system or set of business processes, to test the installation, and, in some cases, to convert existing data or create separate databases to account for the separation of PG&E from the New Entities. Also, PG&E requires additional time to provide instruction and training to the employees who will be using the various software products.

2. Stock Option Management (Cost Estimate—$25,000).

PG&E Corporation currently administers a stock option plan for PG&E employees who hold options to purchase PG&E Corporation stock. Pursuant to the Plan, employees who hold options to purchase PG&E Corporation stock will also be granted

[3]The facts set forth in this Section B.1 and Section B.2 below are supported by the Declaration of Lance Maeda filed concurrently herewith ("Maeda Declaration").

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

options to purchase PG&E stock, which will be publicly traded after the Plan Effective Date. Therefore, PG&E will require a new PG&E stock option plan, which it will administer for all individuals who are granted PG&E stock options.

PG&E has selected Salomon Smith Barney, a member of Citigroup ("Salomon"), to develop a system for administering the new stock option plan. Salomon provides corporations with a range of corporate financial services, including stock option plan services. The process of developing and implementing the new stock option plan is expected to take approximately three months.. Specifically, Salomon will: (i) design and develop a system to administer the stock option plan, including the online access features, (ii) install and test the system, (iii) set up accounts for option holders, and (iv) develop a communication plan to inform option holders on how to use the new system. All of these tasks must be completed by the Plan Effective Date, since option holders may wish to exercise their options immediately after the Plan Effective Date.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

Salomon will provide these services to PG&E for a cost of approximately $25,000. This cost includes an initial set-up fee of $5,000, which PG&E will be required to pay even if the project is cancelled before completion.

C. <u>NEW ENTITY BUSINESS PROCESSES.</u>

PG&E has identified several projects related to the business operations of all of the New Entities, described below, which must be completed by or in advance of the Plan Effective Date.

1. <u>Human Resources Software (Cost Estimate—$75,810).</u>[4]

PG&E has identified a number of software tools that are critical for the human resources functions required by the New Entities. PG&E requests authority to purchase the

[4] The facts set forth in this Section C.1 and Sections C.2 and C.3 below are supported by the Maeda Declaration.

following items of software now in order to allow sufficient time to obtain the software, as well as to install, configure and test it so that all critical human resources functions will be in place for the New Entities by the Plan Effective Date. PG&E will obtain the necessary software licenses but the licenses will be transferable to the New Entities upon the Plan Effective Date. If the Plan is not confirmed, PG&E anticipates that it will be able to use all of the software tools described below, which represent current (and therefore upgraded) versions of software already in use by PG&E.[5]

a. <u>Random Drug Testing</u>: "Heidi/Assistant" is a software tool currently used by PG&E to manage random drug testing of certain classes of employees in order to comply with Department of Transportation regulations. The New Entities will also be subject to the Department of Transportation regulations requiring certain classes of employees to be randomly drug-tested. Therefore, PG&E intends to purchase a similar software license for the New Entities from Compliance Information Systems for approximately $6,590, which includes the software and support for 2,500 tests per year.

b. <u>Affirmative Action Plan</u>: "Great AAP" is a software tool currently used by PG&E to create and manage affirmative action plans to comply with state and federal regulations. The New Entities will also require this tool to manage their affirmative action plans. PG&E intends to purchase this software license from Berkshire Associates, Inc. for approximately $2,995, which includes the Great AAP Master Edition Single License and one year of technical support.

c. <u>Training Management</u>: "Training Server" is a software tool currently used by PG&E to manage training classes, training class enrollment and employee training records. It is currently the sole repository for PG&E employee training records. These training

---

[5] PG&E previously obtained authority to incur consulting expenses for PeopleSoft's implementation of a human resources management system for the New Entities. In addition, PG&E previously obtained authority to incur expenses related to additional human resource information technology applications, including applications related to an Employee Assistance Program, Salary Planning and the Test Results Tracking Database. The software identified in this Motion relates to additional human resource requirements that have not been covered in the previous motions.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

certifications are necessary to ensure that employees can continue to safely perform their jobs and operate certain specialized equipment. Therefore, the New Entities will require this software tool to track employee training records as well, including the records for current PG&E employees who may work for the New Entities. PG&E intends to purchase this software license from THINQ Learning Solutions Inc. for approximately $20,000. In addition, THINQ will provide installation, configuration and testing for this software at a cost of approximately $40,000.

d. Employee Testing: "Scan Tools" is a software tool currently used by PG&E to operate a bubble card scanner (used to score pre-employment and employee tests). This testing is required to ensure that employees in specific jobs can continue to perform the required job functions. Therefore, the New Entities will also require this software tool to conduct testing for new and continuing employees. In addition, "EEI Scanner Software" is currently used by PG&E in conjunction with the Scan Tools software to score employee tests. The New Entities will also require this software in order to score employee tests. PG&E intends to purchase the Scan Tools software license from NCS Pearson for approximately $1,725 and the EEI Scanner Software from the Edison Electric Institute for approximately $4,500.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

2. Banking & Money Management (Cost Estimate—$195,800).

By the Plan Effective Date, the New Entities will require certain software and information technology applications to handle banking and money management services.[6] Therefore, PG&E intends to purchase licenses for certain specialized software products, which must be installed and tested for use by the New Entities. In addition, existing banking

[6]PG&E previously obtained approval for approximately $32,400 in expenses related to technical writers and programmer analysts who are assisting with documenting and installing certain applications related to banking and money management as well as tax, legal compliance and business ethics (see Motion for Authority to Incur Information Technology Consulting Expenses approved by Order entered on August 21, 2002). The present project involves specialized banking and money management software that was not covered in the previous motion.

and money management data must be separated from PG&E and transferred to the applications to be used by the New Entities. The banking and money management projects described below are expected to take approximately three to four months to complete, which includes the software installation as well as the separation and transfer of data.

a. Cash Management Software and Related Services. PG&E currently licenses Resource IQ software, which it uses to manage its daily cash position and to record banking transactions to the general ledger accounting system. Therefore, for the New Entities, PG&E intends to purchase a similar license from Sunguard Treasury Systems ("Sunguard"), a banking software specialist, at a cost of approximately $110,950. Software consultants from Sunguard will assist with the installation, configuration and implementation of Resource IQ at an additional cost of approximately $32,000. In addition, PG&E will purchase a license for Mellon Bank's Telecash software for the New Entities at a cost of approximately $350. This software is used to approve wire transfers of money to and from Mellon Bank initiated through the Resource IQ software system.

b. Banking Relationship Software and Related Services. PG&E currently uses Banking Relationship Manager software to analyze banking fees and services. For the New Entities, PG&E will purchase a license for Banking Relationship Manager software from The Weiland Financial Group ("Weiland"), a financial services consulting firm, at a cost of approximately $20,500. Weiland will also provide one or more consultants who will assist PG&E in separating the data currently stored in the Banking Relationship Manager software used by PG&E. The cost for the consultants' services will be approximately $2,000.

c. Project Management. PG&E has selected Bort and Company, Inc., a cash management consulting firm, to provide project management services in connection with the implementation of the banking and money management processes for the New Entities at a cost of approximately $30,000. These services will include scheduling, tracking and reporting on the status of the foregoing banking and money management projects.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

3. **Electronic Data Interchange (Cost Estimate—$90,000).**

GE Global Exchange Services currently provides an Electronic Data Interchange ("EDI") program for PG&E's purchasing and accounts payable functions. The EDI program allows PG&E to communicate electronically with its vendors and exchange purchase orders, purchase order changes and invoices electronically. It also permits PG&E to pay vendors via Electronic Funds Transfer. PG&E has found that the EDI program reduces its costs and improves the overall efficiencies of its operations. Therefore, PG&E has decided to install the EDI program for the New Entities to ensure a smooth transition upon separation and to avoid inefficient and potentially inaccurate payment processing by the New Entities.

PG&E has selected GE Global Exchange Services to provide a similar EDI program for the New Entities. This will include analysis of current PG&E procedures, including special processes and reporting, modifications to various aspects of the existing EDI program to meet the special requirements of the New Entities, setting up the Electronic Funds Transfer system, adding an electronic connection between GE Global Exchange Services and the New Entities, and testing and implementation of the new EDI program with approximately 250 vendors. This project is expected to take approximately four months to complete. The set-up cost is $40,000 and the additional estimated cost for implementing the system is $50,000. The set-up cost of $40,000 cannot be avoided even if the contract is subsequently canceled before completion of the project. The remaining $50,000 is based on time and expenses and therefore could be partially or fully avoided upon contract termination.

4. **Procurement Management (Cost Estimate—$270,000).**[7]

Procuring goods and services for a large company such as PG&E is a substantial and complex task. Although the New Entities will not be as large as present day PG&E, it is

[7]The facts set forth in this Section C.4 are supported by the Declaration of Michael Meko filed concurrently herewith (the "Meko Declaration").

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

estimated that the New Entities collectively will spend approximately $200 million per year on materials (including supplies and equipment) and $300 million per year on services (including consulting services and technical assistance).

In order for the New Entities to be prepared to commence business operations by the Effective Date, it is critical to implement certain procurement processes in advance of the Effective Date.[8] Without an established system in place for the day-to-day management of procurement, the New Entities will not be able to operate efficiently, and would face substantial confusion and delay in the completion of important business tasks. For example, the following key procurement functions will be needed by the New Entities: materials planning and forecasting; purchasing; contract negotiation and administration; warehousing; and distribution of equipment and materials.

The process of creating, testing and implementing new procurement procedures for the New Entities may take up to six months. Therefore, PG&E believes that the work must begin promptly. Significant portions of this project will be handled by PG&E without the assistance of outside resources, including, for example, the configuration of the new Materials Management System[9] to be utilized by the New Entities. However, PG&E will require the assistance of the following consultants in connection with this project and also anticipates incurring certain printing costs as described below:

a. Project Management. Russell Harris of Source California Energy Services will provide project management services for this project, including the preparation of work plans, tracking project status, preparing reports, and otherwise facilitating and managing the

[8]PG&E previously obtained authority to incur expenses for services related to negotiating approximately 1,200 goods and services contracts for the New Entities (see Motion for authority to incur certain procurement expenses approved by Order entered on May 20, 2002). In addition, PG&E previously obtained authority to incur expenses related to setting up existing PG&E warehouse space for the temporary use by the New Entities as well as preliminary planning for a new materials distribution center (see Miscellaneous Motion, approved by Order entered on September 4, 2002). The present project covers expenses related to the planning, development and implementation of procurement procedures for the New Entities to manage the day-to-day procurement of goods and services.

[9]As described in the Miscellaneous Motion, the customized inventory system currently used by PG&E would be costly and difficult to adapt for use by the New Entities.

project. PG&E estimates that the cost for these services will be approximately $135,000.[10] In addition, Stan Miyamoto of Stan Miyamoto Consulting will provide project management support as well as oversee the coordination of this project with the related materials distribution center project (see footnote 9 above). PG&E estimates that the cost for Mr. Miyamoto's services will be approximately $25,000.

b. Consultants with Procurement Expertise. Three outside consultants will be needed to provide expertise and recommendations in the areas of warehouse management, paperless procurement and e-commerce technology. PG&E has not yet selected the consultants but estimates a total cost of approximately $75,000 for these services, based on its past experience with similar consultants and preliminary discussions to date with potential consultants.

c. Printing of Materials. PG&E estimates that it will incur approximately $35,000 for printing of training manuals, policies and procedures manuals, and other materials related to procurement procedures for use by the New Entities. PG&E intends to incur these printing expenses immediately after Plan confirmation.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN A Professional Corporation

5. Accounting Processes And Procedures (Cost Estimate—$1.5 Million).[11]

Currently, PG&E's principal accounting system is provided through a client server application developed by SAP America, Inc. ("SAP"). PG&E also uses more than 80 other software applications that support information recorded in the SAP accounting system and perform other accounting functions. These supporting accounting systems consist of subsidiary ledgers containing detail information for certain line items contained in the general ledger, as well as systems that perform computations of amounts to be recorded in the general ledger. Both manual and automated interfaces transfer information from the various accounting systems into the SAP accounting systems. Approximately five million

[10] Mr. Harris has performed preliminary services on this project beginning in July 2002.

[11] The facts set forth in this Section C.5 are supported by the Declaration of Stephanie Maggard filed concurrently herewith ("Maggard Declaration").

transactions are posted to the SAP accounting system each week. PG&E estimates that approximately 30 percent of these transactions relate to business activities of the New Entities.

By the Plan Effective Date, the New Entities will require accounting systems and applications that are fully implemented and operational in order to maintain their books and records.[12] Each of the accounting systems and applications will require associated processes and procedures to capture, record and validate accounting transactions to ensure that accurate and complete information is ultimately recorded in the general ledger. For example, the recording of revenue requires complex processes and procedures to capture the units sold or services provided, price the goods and services, estimate collectible amounts, and prepare and record revenue journal entries in the general ledger.

Although PG&E intends to replicate existing procedures and processes and introduce as little change as possible, the New Entities will be separate, new companies and out of necessity certain processes and procedures will change. In addition, it will be important that employees of the New Entities be trained in the use of all accounting processes and procedures. It will also be critical that PG&E review its existing accounting processes and procedures to ensure that these processes and procedures are not disrupted as a result of the separation.

PG&E has selected PricewaterhouseCoopers ("PWC"), a global accounting and financial services firm, to assist with the development of accounting processes and procedures for the New Entities.[13] PWC has extensive experience in the accounting field,

---

[12] Pursuant to the Miscellaneous Motion, PG&E obtained approval for application integration software and support related to the SAP system and other key systems that will be used by the New Entities. The present project relates to the overall development and implementation of accounting processes and procedures as opposed to the technical implementation.

[13] PWC is also approved as a professional in this case as the financial advisor to the Official Committee of Unsecured Creditors ("Committee"). PWC has informed PG&E that the Committee has no objection to PWC's representation of PG&E for the limited purposes set forth above and that PWC has ethical walls and procedures in place to protect both the Committee's and PG&E's confidential information. PG&E is informed and believes that PWC is filing a Supplemental Declaration of Michael Hamilton with the Court on or about September 13, 2002 disclosing its proposed services to be provided to PG&E.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

including the implementation of processes, procedures and internal controls associated with complex accounting systems. Specifically, this project will include the following components: (i) an inventory of existing accounting applications, procedures and controls; (ii) analysis of existing procedures and controls to determine which components can be duplicated, duplicated with modifications, or require a new design; (iii) recommendations of modifications to existing processes to accommodate organizational changes, application configuration and other changes necessitated by formation of the New Entities; (iv) assisting PG&E in designing new accounting procedures for functions that are new or require more substantial changes; (v) estimating resource requirements, including employee requirements, to perform accounting processes at the New Entities and at PG&E; (vi) reviewing interfaces between field locations and centralized processing functions and between and among accounting systems; (vii) testing of new procedures and controls for the New Entities and PG&E; (viii) determining training needs and assist in developing training materials; and (ix) assisting in the implementation of all new accounting processes.

Implementation of accounting systems, procedures and controls to capture, record and validate business transactions is a critical business function that must be completed before the New Entities commence business operations. PG&E must also ensure that there are no gaps in its accounting procedures as a result of the separation of the business lines. PG&E estimates that the accounting process and procedures work to be performed by PWC (and related work to be performed by PG&E) will take approximately six months. This project is designed to provide only the basic accounting requirements for the New Entities and PG&E to keep accurate financial records, develop financial statements, and perform basic financial functions, such as paying employees and billing customers. PG&E estimates that the total cost for PWC's services will be approximately $1.5 million.

D. GENERAL IMPLEMENTATION EXPENSES.[14]

The following projects relate to PG&E's planning and preparation for Plan implementation. PG&E believes that these project costs must be incurred well in advance of the Plan Effective Date due to the nature of the work, as described in more detail below.

1. Transactional Agreements And Schedules (Cost Estimate—$257,000).[15]

Implementation of the Plan will require the creation of up to 100 separate agreements, most of which will have several schedules attached listing or describing specific items related to the particular transaction; as a result, some of the schedules are expected to take up thousands of pages and will be maintained on computer discs rather than in paper format. These agreements will cover such critical matters as how each of the New Entities will be separated from PG&E and what assets each will own. Examples of these agreements include the asset transfer assignment and assumption agreement (which will contain voluminous schedules), and the substation/switchyard agreements. Due to the volume of information involved, substantial time is required to develop and review these documents. Each agreement and schedule requires extensive research, input and review by various subject-matter experts at PG&E. The development process for these documents could take several months, as a result of the time involved in assembling the necessary information, and the drafting and review process. There will be many PG&E representatives, as well as outside counsel, participating in the preparation of these documents.

PG&E has selected ZIA Information Analysis Group, Inc. ("ZIA") to provide data management support for this project. ZIA's work on a related project was previously approved by the Court (see PG&E's Motion for Authority to Incur Data Management Costs, approved by Order entered on June 20, 2002). The prior motion related to ZIA's

[14]This category of implementation work was not specifically described in the previous Maggard Declaration, but PG&E has recently become aware of the necessity of these projects and costs. PG&E anticipates that it will stay within its previous cost estimates for the Implementation Projects, notwithstanding this additional category of implementation work.

[15]The facts set forth in this Section D.1 are supported by the Maggard Declaration.

development and maintenance of an asset database to facilitate the preparation of the asset schedules needed for the asset transfer assignment and assumption documentation contemplated by the Plan. The present project relates to ZIA's development and maintenance of a secure website for all Plan-related transactional documentation in order to facilitate the exchange of information between PG&E, its outside counsel and any other parties assisting with Plan implementation who will be authorized to access the website. ZIA will also assist with the compilation, organization and review of the transactional documentation, including the input of all draft documents onto the website. PG&E estimates that the cost for this work will be approximately $257,000.

2. Permit And Franchise Application Fees (Cost Estimate—$3 Million).[16]

In its Motion for Order Authorizing Expenditures Related to Permits and Franchises ("Permits Motion"), approved by Order entered on May 17, 2002, PG&E explained that it holds tens of thousands of operating and land occupancy permits, licenses and related governmental entitlements, and is a party to over 520 franchise agreements with various cities and counties. PG&E further explained that the separation contemplated by the Plan required that certain permits and licenses be transferred or reissued to the New Entities, and that new franchises be obtained by the New Entities, in order for the New Entities to be authorized to conduct business operations by the Plan Effective Date. Pursuant to the Permits Motion, PG&E obtained authority to hire various consultants to assist PG&E with the process of obtaining the necessary permits and franchises ("Permits and Franchises") for the New Entities. In addition, pursuant to the Motion for Authority to Incur Additional Permit Expenses, approved by Order entered on June 20, 2002, PG&E obtained authority to incur additional expenses related to the permit transfer process.

Considerable work has been done on this project since the previous motions were

[16] The facts set forth in this Section D.2 are supported by the Declaration of June Ruckman filed concurrently herewith.

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation

approved. PG&E and its consultants have now contacted many of the applicable government entities to begin the lengthy process of arranging for the Permits and Franchises to be in place in advance of the Plan Effective Date. In some cases, applications have been submitted. Some government entities are requesting that PG&E submit application fees and/or cost recovery fees to help defray costs in processing the applications (collectively, "Application Fees"). In addition, upon issuance of Franchises, PG&E may be required to post a surety or performance bond to secure performance, in the absence of which PG&E will lose the Franchise altogether.[17] PG&E anticipates that it will have bonding capacity and will therefore only need to pay bond premiums. At this time, PG&E does not know the exact amount of the Application Fees or bond premiums that will be owed, but PG&E estimates that it could be approximately $3 million. This estimate is based on communications to date with the various government entities, and the past experience of PG&E employees and consultants in working with government entities on related matters.

PG&E requests authority to pay these fees so that the process of obtaining the necessary Permits and Franchises for the New Entities can continue. Since the Application Fees are ordinarily required up front, it is important that PG&E have some flexibility in paying these fees when requested without repeatedly filing motions for Court approval. Similarly, it is important to avoid jeopardizing the issuance of a franchise as a result of not having authority to incur costs for a performance bond. Since PG&E will be receiving the fee requests from various government agencies at staggered times, it is neither feasible to bring a motion now with more precise information, nor is it feasible to wait and jeopardize the implementation of the Plan. Therefore, PG&E requests authority to pay up to $3 million as the Application Fees and bond requirements arise. PG&E will bring a further motion seeking approval to pay any amounts in excess of $3 million, if this becomes necessary.

---

[17]Under the Franchise Act of 1937, cities and counties may request bonds upon granting of the franchise. Based on discussions to date, PG&E anticipates that most cities and counties will require the bonds. Under the statute, the franchise is forfeited if the bond is not posted within 5 days of the granting of the franchise.

II.

THE ADDITIONAL MISCELLANEOUS IMPLEMENTATION EXPENSES SHOULD BE APPROVED PURSUANT TO SECTION 363(B)(1) OF THE BANKRUPTCY CODE

PG&E seeks approval for the various implementation expenses set forth above as a use of estate property that is outside of the ordinary course of business under Bankruptcy Code Section 363(b)(1). Since these projects are related to the implementation of the Plan, PG&E believes that the purpose and scope of the expenditure may be characterized as outside of the ordinary course of business and therefore requires Court approval.[18]

The Court has considerable discretion in approving a request pursuant to Section 363(b)(1) of the Bankruptcy Code ("[t]he trustee, after notice and a hearing, may use, sell or lease, other than in the ordinary course of business, property of the estate"). See In re Montgomery Ward Holding Corp., 242 B.R. 147, 153 (D. Del. 1999) (affirming the bankruptcy court's decision to approve expenditure for employee incentive programs; noting that bankruptcy court has considerable discretion in approving a Section 363(b) motion).

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

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

---

[18] PG&E believes that the consultants described above should not be considered "professional persons" requiring approval under Bankruptcy Code Section 327(a). This is due both to the nature of the services to be provided and to the consultants' limited role in connection with PG&E's reorganization proceeding.

1985)).

Sound business justifications exist for approval of the various implementation costs described above. PG&E does not have sufficient capacity or skills in-house to perform and complete the work without the assistance of the outside consultants. Also, PG&E is solvent and has sufficient cash to pay the expenses described herein without causing any detriment to its creditors.[19]

Consistent with PG&E's previous implementation expense requests, PG&E continues to enter into contracts with consulting firms that allow PG&E to terminate without cause and without any penalty, so that in the event that the implementation work is no longer necessary, PG&E can minimize its costs (with limited exceptions as noted above). Furthermore, PG&E has included only those projects that have been identified as critical for completion by or in advance of the Plan Effective Date, and which require long lead time or must be completed before subsequent, related implementation work can be performed. On that basis, PG&E believes that the implementation projects described herein are necessary and should be approved so that work can commence promptly.

[19] As reflected in PG&E's July 2002 Monthly Operating Report, PG&E held more than $3.9 billion in cash reserves as of July 31, 2002.

CONCLUSION

For all of the foregoing reasons, PG&E respectfully requests that the Court approve the costs described above and grant such other and further relief as may be just and appropriate.

DATED: September 12, 2002

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

By: Julie Landau
JULIE B. LANDAU

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

WD 091202/F-1419905/Y12/1021609/v1

HOWARD RICE NEMEROVSKI CANADY FALK & RABKIN
A Professional Corporation