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7 PACIFIC GAS AND ELECTRIC COMPANY

8 UNITED STATES BANKRUPTCY COURT
9 NORTHERN DISTRICT OF CALIFORNIA
10 SAN FRANCISCO DIVISION

11 In re
12 PACIFIC GAS AND ELECTRIC
COMPANY, a California corporation,
13 Debtor.

Case No. 01 30923 DM
Chapter 11 Case

Date: March 14, 2003
Time: 1:30 p.m.
Place: 235 Pine Street, 22nd Floor
San Francisco, California

14 Federal I.D. No. 94-0742640
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18 NOTICE OF MOTION AND MOTION FOR ORDER APPROVING
AMENDMENT TO THE TERMINATION AGREEMENT
19 BETWEEN EAST BAY MUNICIPAL UTILITY DISTRICT
AND PACIFIC GAS AND ELECTRIC COMPANY;
20 MEMORANDUM OF POINTS AND AUTHORITIES IN SUPPORT THEREOF

21 [Declaration of David C. Landes Filed Concurrently Herewith]
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25

26 *Appl*
27 *Add: Kids Ogc Mail Center*
28

1 MEMORANDUM OF POINTS AND AUTHORITIES

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3 INTRODUCTION

4 Pacific Gas and Electric Company ("PG&E" or "Debtor"), the debtor and debtor in
5 possession in the above-captioned Chapter 11 case, seeks the Court's entry of an Order
6 Approving Amendment To The Termination Agreement Between East Bay Municipal
7 Utility District And Pacific Gas & Electric Company (the "Motion").

8 From 1981 until 1999, East Bay Municipal Utility District ("EBMUD") had a
9 bilateral power purchase contract with PG&E for power EBMUD generated at its Pardee and
10 Camanche powerhouses. In 1999, EBMUD and PG&E (together the "Parties") agreed to
11 terminate their agreement in order to settle a dispute regarding the contract's price
12 adjustment term. The termination was approved by the California Public Utilities
13 Commission ("CPUC") in April, 2000.

14 Pursuant to the terms of the 1999 termination agreement (the "Termination
15 Agreement"), EBMUD agreed to make monthly payments to PG&E until 2008 (the
16 "Royalty Payments"). The Royalty Payments were to be based on a percentage of the
17 market price for power, as set by the California Power Exchange (the "PX") or, in the event
18 the PX no longer existed, its successor or the market that most closely approximated it.

19 Since the PX ceased operations in January 2001, PG&E and EBMUD have not been
20 able to agree on a successor or market that most closely approximates the PX. To resolve all
21 of their disputes, PG&E and EBMUD now wish to amend the Termination Agreement by
22 providing that the Royalty Payments be calculated as a percentage of EBMUD's actual sales
23 revenues.

24 PG&E seeks this Court's authorization to compromise the dispute with EBMUD by
25 amending the Termination Agreement on terms beneficial to both parties on the basis that
26 such a result would best promote the business interests of PG&E's estate.
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2 **FACTS AND PROCEDURAL HISTORY¹**

3 PG&E and East Bay Municipal Utility District (“EBMUD”) entered into a
4 Revised Contract for Purchase of Electric Power on or about February 10, 1981 (“1981
5 Contract”), which was amended by the First Amendment thereto, executed on or about
6 December 4, 1986 (“1986 Amendment”). The 1981 Contract and 1986 Amendment,
7 together with any other amendment thereto are known as the Power Purchase Contract
8 (“Power Purchase Contract” or “PPC”).

9 After various disagreements as to the interpretation of the PPC and the respective
10 rights and obligations of PG&E and EBMUD thereunder, the Parties decided to terminate
11 their agreement. On or about October 13, 1999, the Parties entered into a termination
12 agreement (the “Termination Agreement”). Pursuant to the Termination Agreement,
13 EBMUD agreed to make monthly payments to PG&E until 2008 (the “Royalty Payments”).
14 The Termination Agreement specified that the Royalty Payments were to be calculated
15 based on the market price for power set by the PX, according to a detailed formula termed
16 the base payment (the “Base Payment”). In its definition of PX, the Termination Agreement
17 provided that in the event the California Power Exchange ceased operations, the term would
18 then refer to “its successor. If there is no single successor, then that market for California
19 electricity that most closely approximates the PX during the last full calendar year period
20 that the PX operated.” Termination Agreement at § 1.5. In April, 2000, the California
21 Public Utilities Commission (the “CPUC”) approved the Termination Agreement.

22 The PX ceased operations as of January, 2001. Since that time, the Parties have
23 not been able to agree on which entity or market fits the definition of the Termination
24 Agreement. The Parties have discussed the proper replacement of the PX price and the
25 potential alternative of a lump-sum buyout by EBMUD but have been unable to agree on
26 either possibility.

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28 ¹The evidentiary basis and support for the facts set forth herein are contained in the Declaration of David C. Landes filed concurrently herewith.

1 In an effort to resolve their disagreement, the Parties have negotiated an
2 amendment to the Termination Agreement (the "New Amendment") which eliminates
3 confusion by changing the calculation of the Base Payment. In lieu of a formula dependent
4 on the PX or other market price, the New Amendment provides that the Royalty Payments
5 shall be based on EBMUD's actual sales revenues, as specified in § 1 of the New
6 Amendment. New Amendment § 1.

7 The New Amendment also provides that no earlier than June 30, 2004, upon 30
8 days notice, either of the Parties may elect to return to the original Base Payment formula set
9 forth in the Termination Agreement, using a "PX Substitute" for the remaining term, as the
10 term "PX Substitute" is defined in the New Amendment. New Amendment § 3.b.

11 The New Amendment also institutes certain protective measures for both PG&E
12 and EBMUD, including audit rights. New Amendment § 2.b. Furthermore, the Parties have
13 each agreed to waive and release any and all claims they may have against one another
14 related to the Termination Agreement to the date the New Amendment was made. New
15 Amendment § 4.

16 PG&E believes that the terms of the New Amendment are fair, equitable and in
17 the best interests of the estate. See Declaration of David C. Landes at ¶12.

18 19 20 ARGUMENT

21 **A. The New Amendment Compromises The Dispute With EBMUD Under** 22 **Terms Fair To Both Parties Without The Expense And Diversion Of** 23 **Resources Involved In Litigation And Should Be Authorized Pursuant To** **Bankruptcy Rule 9019.**

24 Bankruptcy law favors compromises, which are considered "a normal part of the
25 process of reorganization." Protective Comm. for Indep. Stockholders of TMT Trailer Ferry
26 Inc. v. Anderson, 390 U.S. 414, 424 (1968). Accordingly, the Bankruptcy Court has great
27 latitude in approving compromise agreements. See Martin v. Kane (In re A & C Props.),
28 784 F.2d 1377, 1380-81 (9th Cir. 1986). The Court's discretion is not, however, unlimited.

1 See Arden v. Motel Partners (In re Arden), 176 F.3d 1226, 1228 (9th Cir. 1999). The Court
2 may approve a compromise only if it is “fair and equitable.” Protective Comm. for Indep.
3 Stockholders of TMT Trailer Ferry Inc., 390 U.S. at 424. In evaluating any proposed
4 compromise, the Court must consider the following factors:

5 (a) The probability of success in the litigation; (b) the difficulties, if
6 any, to be encountered in the matter of collection; (c) the complexity
7 of the litigation involved, and the expense, inconvenience and delay
8 necessarily attending it; (d) the paramount interest of the creditors and
9 a proper deference to their reasonable views in the premises.
10 (Woodson v. Fireman’s Fund Ins. Co. (In re Woodson), 839 F.2d 610,
11 620 (9th Cir. 1988) (quoting In re A & C Props., 784 F.2d at 1381).

12 Courts weigh these factors to determine whether the compromise is in the best interests of
13 the estate. See A & C Props., 784 F.2d at 1382 (court must “weigh certain factors to
14 determine whether the compromise is in the best interest of the bankrupt estate”).

15 Bearing these points in mind, the A & C Properties factors weigh in favor of
16 authorizing PG&E’s entry into the New Amendment. Litigating these issues against
17 EBMUD would undoubtedly prove time-consuming and costly, with no assurance of a
18 successful legal outcome.

19 By entering into the New Amendment, PG&E will obtain the benefit of mutual
20 liability releases and continued Royalty Payments. Amending the Termination Agreement is
21 a fair and equitable resolution of potential disputes and in the best interests of PG&E’s
22 estate.
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CONCLUSION

For all of the foregoing reasons, PG&E respectfully requests that this Court grant the Motion and enter its Order approving the said New Amendment as an appropriate compromise in the interest of the estate pursuant to Bankruptcy Rule 9019.

DATED: February 13, 2003.

Respectfully,

HOWARD, RICE, NEMEROVSKI, CANADY,
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By: 
WILLIAM J. LAFFERTY

Attorneys for Debtor and Debtor in Possession
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