

1 WILLIAM J. LAFFERTY (No. 120814)
BARBARA GORDON (No. 52424)
2 HOWARD, RICE, NEMEROVSKI, CANADY,
FALK & RABKIN
3 A Professional Corporation
Three Embarcadero Center, 7th Floor
4 San Francisco, California 94111-4024
Telephone: 415/434-1600
5 Facsimile: 415/217-5910

6 Attorneys for Debtor and Debtor in Possession
PACIFIC GAS AND ELECTRIC COMPANY
7

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.
14 Federal I.D. No. 94-0742640
15

Case No. 01 30923 DM
Chapter 11 Case
Date: April 9, 2003
Time: 9:30 a.m.
Place: 235 Pine Street, 22nd Floor
San Francisco, California
Judge: Hon. Dennis Montali

HOWARD
RICE
NEMEROVSKI
CANADY
FALK
& RABKIN
A Professional Corporation

16 NOTICE OF MOTION AND MOTION OF PACIFIC GAS AND
17 ELECTRIC COMPANY FOR ORDER AUTHORIZING DEBTOR TO
18 REPAY CERTAIN GENERATOR ADVANCES; MEMORANDUM OF
POINTS AND AUTHORITIES IN SUPPORT THEREOF

19 [SUPPORTING DECLARATION OF DOUGLAS G. DANIELS FILED SEPARATELY]
20

21 PLEASE TAKE NOTICE that on April 9, 2003, at 9:30 a.m., or as soon
22 thereafter as the matter may be heard, in the Courtroom of the Honorable Dennis Montali
23 located at 235 Pine Street, 22nd Floor, San Francisco, California, Pacific Gas and Electric
24 Company, the debtor and debtor in possession in the above-captioned Chapter 11 case
25 ("PG&E" or the "Debtor"), will and hereby does move the Court, pursuant to Sections 363
26 and 105 of the Bankruptcy Code, for entry of an order authorizing the Debtor to repay
27 certain generator advances ordered by the Federal Energy Regulatory Commission
28 ("FERC").

0602
[Handwritten signatures and initials]

1 The Motion is based on this Notice of Motion and Motion, the accompanying
2 Memorandum of Points and Authorities in support thereof, the Declaration of Douglas G.
3 Daniels filed concurrently herewith, the record of this case and any evidence presented at or
4 prior to the hearing on this Motion.

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

13 PG&E is not attaching copies of the exhibits to the service copies of the Motion
14 because they are too voluminous. However, PG&E will make copies of such documents
15 available to anyone being served with the Motion. Any person served with the Motion may
16 obtain copies of the exhibits by written request by mail to Howard, Rice, Nemerovski,
17 Canady, Falk & Rabkin, Attn: Nathaniel Hunt, Three Embarcadero Center, 7th Floor, San
18 Francisco, California 94111-4024, or by email request to nhunt@howardrice.com.
19 Additionally, copies of the exhibits will be available at the hearing on the Motion if any
20 other person wishes to review them.

HOWARD
RICE
NEMEROVSKI
CANADY
FALK
& RABKIN
A Professional Corporation

1 **MEMORANDUM OF POINTS AND AUTHORITIES**

2 **INTRODUCTION**

3 Pacific Gas and Electric Company ("PG&E" or the "Debtor"), hereby moves this
4 Court for an order authorizing PG&E to repay certain Calpine generators (the "Generators")
5 for amounts advanced by Generators to PG&E for network upgrades installed to
6 interconnect thirteen Calpine power projects (the "Calpine Projects"). The repayment has
7 been ordered by the Federal Energy Regulatory Commission ("FERC") through a series of
8 recent rulings described in greater detail below.

9 As a highly regulated entity subject to FERC orders, PG&E believes that
10 effecting the repayments to Generators is in the ordinary course of its business. Because
11 some of the repayments relate to pre-petition advances, and because of the amount involved
12 in the repayment of funds for the thirteen Calpine Projects, PG&E seeks the approval of this
13 Court for the repayments.

14 **I.**

15 **FACTUAL BACKGROUND¹**

16
17 As explained in greater detail below, by this Motion, PG&E seeks permission to
18 pay three categories of FERC-ordered repayments: (1) to Generators for funds advanced to
19 PG&E prior to the filing of this Chapter 11 case; (2) to Generators for funds advanced post-
20 petition to PG&E; and, (3) to Generators for funds not yet advanced under interconnection
21 agreements, but contemplated hereunder when such amounts come due.

22 **A. Description of Interconnection Agreements with Generators**

23 When a generator constructs a new power plant, FERC permits transmission
24 providers such as PG&E to charge the generator the cost of upgrades to interconnect the
25 generator with the provider's transmission system. PG&E enters into a Generator Special
26 Facilities Agreement ("GSFA") and pursuant to the agreement, the generator advances the
27

28 ¹The evidentiary basis and support for the facts set forth in this Motion is contained in the Declaration of Douglas G. Daniels filed concurrently herewith.

HOWARD
RICE
NEMEROVSKI
CANADY
FAUK
& RABKIN
A Professional Corporation

1 funds for the upgrades. PG&E currently has certain GSFA's (collectively the
2 "Agreements") with the following Generators: Los Medanos Energy Center, LLC ("Los
3 Medanos"); Gilroy Energy Center, LLC ("Gilroy"); Los Esteros Critical Energy Facility,
4 LLC ("Los Esteros"); Yuba City Energy Center, LLC ("Yuba City"); Metcalf Energy
5 Center, LLC ("Metcalf"); Lambie Energy Center, LLC ("Lambie"); Goose Haven Energy
6 Center, LLC ("Goose Haven"); Creed Energy Center, LLC ("Creed"); King City Energy
7 Center, LLC ("King City"); Feather River Energy Center, LLC ("Feather River");
8 Riverview Energy Center, LLC ("Riverview"); Wolfskill Energy Center, LLC
9 ("Wolfskill"); and Delta Energy Center, LLC ("Delta") (collectively the "Generators").
10 Calpine Corporation owns all thirteen of the Generators.

11 With the exceptions of Delta and Los Medanos, the Agreements were entered into
12 post-petition between August 15, 2001 and October 26, 2002. Each Generator has
13 constructed or is in the process of constructing a new power facility which bears the same
14 name as the Generator. These facilities are collectively referred to as the "Calpine
15 Projects".

16 **B. Background Regarding Interconnection Agreements and FERC Rulings**
17 **Requiring Repayment to Generators for Funds Advanced for Interconnect**
18 **Upgrades**

19 Prior to late 2001, it was unclear whether FERC would require PG&E to credit or
20 repay Generators for the funds advanced under the Agreements. Commencing in late 2001,
21 FERC, through a series of decisions, indicated that transmission owners must develop a
22 crediting mechanism to repay generators for funds advanced for network upgrades. (No
23 credit is required for the cost of the tie line connecting the Generator to the grid). In later
24 rulings, discussed below, FERC directed PG&E to repay the Generators for funds advanced
25 when a new project comes on line and to recover those funds subsequently through
26 increased transmission rates.² These rulings affect the Calpine Projects constructed or

27 _____
28 ²Although PG&E will ultimately recover the amounts of the repayments to
Generators through increased transmission rates, such recovery will require a significant

1 under construction as well as future projects.

2 When FERC gave preliminary indications commencing late 2001 that utilities would
3 be required to develop crediting mechanisms to repay the advances and recover the
4 repayment through the adjustment of transmission rates, FERC conducted extensive
5 proceedings and issued binding orders to that effect. FERC has ruled that other
6 transmission owners must provide similar credits to generators, and that these rules apply
7 prospectively even when an agreement with the generator had been previously accepted
8 which directly assigned these costs to the generator.

9 PG&E seeks authority to make repayments in compliance with FERC orders.
10 PG&E has filed or intends to file requests for rehearing on the FERC rulings requiring
11 repayment to Los Medanos and Delta because the GSFA's for both Generators directly
12 assigned the cost of those upgrades to Calpine and had been filed and accepted by FERC.
13 While PG&E continues to dispute repayment to these two of the thirteen Calpine Projects,
14 no stays of FERC's Orders have been granted. PG&E is obligated to obey the orders and
15 commence repayment, pending FERC's potential reversal of its orders after rehearing.
16 PG&E does not dispute repayment for the remaining eleven Calpine Projects.

17 FERC-ordered repayments pertaining to the Los Medanos and Delta Projects may
18 constitute payment on account of funds advanced by these Generators prior to the filing of
19 this Chapter 11 case. PG&E's records indicate that Los Medanos advanced \$500,000 on
20 February 25, 2000 and \$3,408,000 on November 24, 2000 and that Delta advanced
21 \$100,000 on June 19, 2000 and \$500,000 on October 20, 2000³. As stated in the preceding
22 paragraph, PG&E disputes repayment of advances to Los Medanos and Delta solely
23 because the GSFA's for both Generators had been filed and accepted by FERC.

24 Certain FERC orders, and specifically 102 FERC ¶61,070 Issued January 29, 2003
25 attached hereto as Exhibit A and 102 FERC ¶61,232 issued February 27, 2003 attached
26 hereto as Exhibit B (collectively "FERC Orders"), directed PG&E to repay the Generators
27 period of time, as the facilities are depreciated under schedules set by FERC.

28 ³Additional advances were made by Delta post-petition in the sum of \$17,890,000.

1 for the network upgrades associated with all thirteen Calpine Projects.

2 PG&E filed credit mechanisms which provide in part for repayment through
3 monthly installments with interest at the rate specified by FERC amortized over a period of
4 five years. The thirteen Calpine Projects and estimated amounts of repayment for each are
5 as follows:

6	Los Medanos	\$3,904,000
7	Gilroy	1,355,000
8	Los Esteros	887,000
9	Yuba City	3,882,200
10	Lambie	1,206,167
11	Goose Haven	1,206,167
12	Creed	1,206,167
13	King City	298,050
14	Feather River	2,550,000
15	Metcalf	6,461,600
16	Riverview	660,000
17	Wolfskill	1,100,000
18	Delta	18,490,000
19	Total	\$43,206,351

20 These amounts will be trued up to actual cost, and interest will be added. Payments due
21 under the FERC Orders are estimated to equal approximately \$9,000,000 per year for five
22 years, assuming that each project comes on line. The FERC Orders provide that payments
23 shall begin 60 days after the latter of (a) the date FERC issues its order directing a credit
24 and (b) the project begins commercial operations. The FERC Orders also provide an
25 opportunity for PG&E to obtain approval of this Court. Although PG&E continues to seek
26 relief from the Orders requiring repayment to Los Medanos and Delta through requests for
27 rehearing before FERC, requests for stay of the FERC Orders pertaining to these Projects
28 have not been granted.

29 The FERC Orders require repayment to commence immediately for ten Calpine
30 Projects, all of the projects other than Metcalf, Riverview, Wolfskill, since these facilities
31 have begun commercial operations. PG&E seeks authority to commence repayment in
32 accordance with the FERC Orders, without prejudice to PG&E's right to recover such
33 payments, if FERC vacates its Orders pertaining to the payments to Los Medanos and Delta
34 Projects.

1
2
3
4
5
6
7
8
9
10
11
12
13
14
15
16
17
18
19
20
21
22
23
24
25
26
27
28

II.

ARGUMENT

A. **PG&E Should Be Authorized To Repay Generators Pursuant To Section 363(b)(1) Of The Bankruptcy Code On The Basis That It Makes Sound Business Sense**

PG&E should be authorized to pay the three categories of repayments discussed above pursuant to Section 363(b)(1) of the Bankruptcy Code, which provides that “[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.” 11 U.S.C. §363(b)(1).

In determining whether to authorize the use, sale or lease of property of the estate under Section 363(b)(1), courts require a debtor to show that a sound business purpose justifies such actions, applying essentially the same “business judgment” test that is used in determining whether to approve the assumption or rejection of an executory contract. See, e.g., Stephens Indus., Inc. v. McClung, 789 F.2d 386, 389-90 (6th Cir. 1986); Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.), 722 F.2d 1063, 1070-71 (2d Cir. 1983); 3 Lawrence P. King, Collier on Bankruptcy ¶363.02[1][g] (15th ed. rev. 1998).

The burden of establishing a valid business purpose for the use of property of the estate outside the ordinary course of business falls upon the debtor. See In re Lionel Corp., 722 F.2d at 1070-71. Once the debtor has articulated a rational business justification, however, a presumption attaches that the decision was made on an informed basis, in good faith and in the honest belief that the action 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. 1985)).

Sound business justifications support PG&E’s compliance with FERC rulings as described in the Motion. PG&E is obligated to submit to FERC jurisdiction and obey FERC orders. FERC has mandated that transmission owners across the country provide such credits. Because PG&E is subject to FERC regulations, it must abide by subsequent

1 mandates ordered by FERC. Repayment of the Generators for network upgrades pursuant to
2 FERC orders is without prejudice to PG&E's rights to rehearing and appeal regarding Los
3 Medanos and Delta. PG&E believes that the repayments are in the ordinary course of
4 business and can be undertaken without notice or hearing.

5 **B. Repayment Of The Advances Is Practical, "Legal And Factually**
6 **Inevitable," And In The Best Interests Of Creditors And The Estate;**
7 **Thus The Court Should Order Such Payment Under Section 105 Of The**
8 **Bankruptcy Code**

9 Although courts demonstrate some reluctance in allowing payment of pre-petition
10 claims prior to the confirmation of a plan in a Chapter 11 case, the Court has the power
11 under Section 105 of the Bankruptcy Code to order the payment of pre-petition claims where
12 circumstances warrant. In doing so, courts have been guided primarily by "practicality and
13 common sense" and the "legal or factual inevitability of payment." In re Payless Cashways,
14 Inc., 268 B.R. 543, 547 (Bankr. W.D. Mo. 2001); In re EqualNet Communications Corp.,
258 B.R. 368, 369 (Bankr. S.D. Tex. 2000).

15 Section 105 authorizes the court to "issue any order, process, or judgment that is
16 necessary or appropriate to carry out the provisions of this title." The purpose of Section
17 105 is "to assure the bankruptcy court's power to take whatever action is appropriate or
18 necessary in aid of the exercise of its jurisdiction." 2 Lawrence P. King, Collier on
19 Bankruptcy ¶105.01, at 105-106 (15th ed. rev. 2000); see, e.g., Crafts Precision Indus., Inc.
20 v. U.S. Healthcare, Inc. (In re Crafts Precision Indus., Inc.), 244 B.R. 178, 183 (B.A.P. 1st
21 Cir. 2000) (affirming authorization of vacation payments "pursuant to §105, irrespective of
22 them being non-priority obligations"); Michigan Bureau of Workers' Disability Corp. v.
23 Chateaugay Corp. (In re Chateaugay Corp.), 80 B.R. 279, 287 (S.D.N.Y. 1987) (bankruptcy
24 court has equitable power, in pre-plan stage of reorganization proceeding, to authorize
25 debtor-in-possession to pay pre-petition debt and to allow debtor to pay some creditors in
26 class without paying others without violating Bankruptcy Code, as a "rigid application of the
27 priorities of §507 would be inconsistent with the fundamental purpose of reorganization and
28

1 of the [Bankruptcy Code's] grant of equity powers to bankruptcy courts, which is to create a
2 flexible mechanism that will permit the greatest likelihood of survival of the debtor and
3 payment of creditors in full or at least proportionately"); see also In re Payless, 268 B.R. at
4 547. As discussed above, the repayments PG&E seeks authority to make have sound
5 business justifications and are FERC-ordered.

6 III.

7 CONCLUSION

8 For all of the foregoing reasons, PG&E respectfully requests that this Court enter its
9 Order granting the Motion and such other and further relief as the Court deems just and
10 appropriate.

11
12 DATED: March 20, 2003.

13 Respectfully,

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

16 By: 

17 BARBARA GORDON

18 Attorneys for Debtor and Debtor in Possession
19 PACIFIC GAS AND ELECTRIC COMPANY
20
21
22
23
24
25
26
27
28