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11 PACIFIC GAS AND ELECTRIC COMPANY
12

13 UNITED STATES BANKRUPTCY COURT
14 NORTHERN DISTRICT OF CALIFORNIA
15 SAN FRANCISCO DIVISION
16

17 In re

18 PACIFIC GAS AND ELECTRIC
19 COMPANY, a California corporation,
20

21 Debtor.
22

23 Federal I.D. No. 94-0742640
24

25 Case No. 01-30923 DM

26 Chapter 11 Case

27 Date: May 16, 2003

28 Time: 1:30 p.m.

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

29 NOTICE OF MOTION AND MOTION OF PACIFIC GAS AND ELECTRIC
30 COMPANY FOR ORDER AUTHORIZING DEBTOR TO PAY CERTAIN
31 REFUND OBLIGATIONS; MEMORANDUM OF POINTS AND
32 AUTHORITIES IN SUPPORT THEREOF

33 [SUPPORTING DECLARATION OF SUNITA JONES
34 FILED CONCURRENTLY HEREWITH]
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1 words, the effect of the settlement agreement, and FERC order approving it, are to require
2 PG&E to make adjustments and refunds for past charges, in this case going back to April 1,
3 1998, when the California Independent System Operator Corporation ("ISO") began
4 operating.

5 PG&E's electric transmission customers are divided into two general categories:
6 Existing Transmission Contract ("ETC") customers and Transmission Owner Tariff ("TO
7 Tariff") customers. The ETC customers are those customers who entered into binding long-
8 term transmission contracts with PG&E before the creation of the ISO. These ETC
9 customers are primarily municipal utilities and they are not the subject of this Motion.

10 TO Tariff customers, on the other hand, take any needed transmission service
11 pursuant to the current ISO and TO Tariffs, which allows the pass-through of certain ISO
12 costs. Accordingly, TO Tariff customers are obligated to reimburse PG&E for applicable
13 charges that PG&E receives from the ISO under the ISO Tariff, and are responsible for
14 paying transmission service rates as set out in PG&E's TO Tariff. TO Tariff customers are
15 divided into two groups: wholesale and retail.

16 The refund obligations that PG&E now seeks this Court's authority to satisfy,
17 reflect changes to various rates or rate structures under PG&E's TO Tariff. Simply put,
18 FERC has modified its approval for PG&E to charge certain TO Tariff rates and has adopted
19 the compromise rates reflected in a settlement agreement approved in the relevant FERC
20 proceeding. Thus, PG&E must adjust the way it charged certain of its customer groups and
21 FERC has ordered PG&E to make the appropriate adjustments. Because the reimbursements
22 relate to pre-petition payments, PG&E seeks this Court's approval to process the refunds.

23
24 **A. TO1 and TO2 Tariff Refunds**

25 On March 31, 1997, PG&E filed its first TO Tariff rate case with FERC ("TO1").
26 On December 17, 1997, FERC accepted PG&E's proposed tariff rates for filing, effective
27 March 31, 1998, subject to refund, suspended the rates for five months and set them for
28 hearing. On March 30, 1998, PG&E filed its second TO Tariff rate case with FERC

1 ("TO2"). On May 28, 1998, FERC accepted PG&E's proposed tariff rates for filing,
2 effective October 30, 1998, subject to refund, suspended the rates for one day, set them for
3 hearing and consolidated the case with the TO1 docket.

4 On March 31, 1999, PG&E filed its third TO Tariff rate case with FERC
5 ("TO3"). FERC accepted PG&E's proposed tariff rates for filing, effective May 31, 1999,
6 subject to refund. The effect of each of these successive TO Tariff rate case filings was to
7 limit the effective periods of the earlier filings. Specifically, the effective period for
8 PG&E's TO1 rates limisted to was March 31, 1998 though October 29, 1998, and the
9 effective period for PG&E's TO2 rates was October 30, 1998 through May 30, 1999.

10 On April 14, 1999, PG&E submitted an Offer of Settlement and Stipulation (the
11 "Settlement") that resolved all outstanding issues for both the TO1 and TO2 dockets. The
12 Settlement, *inter alia*, provided for an effective reduction of 4.24 percent to PG&E's TO1
13 rates and an effective reduction of 8.07 percent to PG&E's TO2 rates. FERC approved the
14 Settlement on January 28, 2003.

15 Because the Settlement had the effect of reducing the rates PG&E was authorized
16 to charge during the effective periods of the TO1 and TO2 cases, FERC has ordered PG&E
17 to refund customers accordingly. While some of these refunds can be addressed by
18 adjustments and credits to customer accounts, others necessitate actual payment.

19 As this Court is aware, as a result of California legislation known as Assembly
20 Bill ("AB") 1890, there has been a rate freeze with respect to overall retail electricity rates in
21 effect in California. Given that nearly all of PG&E's customers paid frozen rates and, as
22 such, were not impacted by the TO1 and TO2 rate cases, the Settlement will not result in
23 refunds to those retail customers. Instead, PG&E will account for the Settlement by making
24 an adjustment of approximately \$30 million to the Transmission Revenue Account ("TRA"),
25 which is a balancing account approved by and subject to review by the California Public
26 Utilities Commission (the "CPUC").

27 However, two relatively small groups of PG&E customers were not fully covered
28 by the AB 1890 rate freeze. Accordingly, FERC has ordered PG&E to make refunds to such

1 customers in accordance with the Settlement's reduction of the TO1 and TO2 rates.

2
3 **1. CTC-Exempt Retail TO Tariff Customers**

4 The TO Tariff transmission bills of certain retail customers who were exempt
5 from responsibility for Competition Transition Charges ("CTCs") under California's AB
6 1890 would have been lower if the reduced TO1 and TO2 rates of the Settlement had been in
7 effect. As such, PG&E has been ordered by FERC to make a refund to these CTC-Exempt
8 customers in the approximate amount of \$50,000.

9
10 **2. Wholesale TO Tariff Customers**

11 Similarly, the bills of the wholesale users of PG&E's TO Tariff, which were not
12 protected by the AB 1890 rate freeze either, would have been lower if the reduced TO1 and
13 TO2 rates of the Settlement had been in effect. As such, PG&E has been ordered by FERC
14 to make a refund to these customers in the approximate amount of \$725,000.

15
16 **III.**

17 **DISCUSSION**

18 **A. PG&E Should Be Authorized To Pay The Refund Obligations In The**
19 **Ordinary Course Of Business.**

20 Section 363(c)(1) of the Bankruptcy Code authorizes the Debtor to "enter into
21 transactions, including the sale or lease or property of the estate . . . and use property of the
22 estate in the ordinary course of business without notice or a hearing." 11 U.S.C. § 363(c)(1).
23 In light of the highly regulated nature of its industry, PG&E must abide by the rules of
24 multiple regulatory agencies, including FERC on those matters for which FERC is the
25 regulatory authority.

26 It is standard practice for FERC to approve utility rate changes on a preliminary
27 basis, subject to later review and possible subsequent refunds. See Jones Decl. ¶3.
28 Because PG&E is subject to FERC jurisdiction, it must abide by subsequent adjustments are

1 mandated by FERC. PG&E believes that these adjustments ordered and should be followed
2 in the ordinary course of its business and can be undertaken without notice or a hearing.

3
4 **B. PG&E Should Be Authorized To Pay The Refund Obligations Pursuant To**
5 **Section 363(b)(1) Of The Bankruptcy Code On The Basis That It Makes**
6 **Sound Business Sense To Pay These Categories Of Claims Pre-**
7 **Confirmation.**

8 If the refund payments are not within PG&E's ordinary course of business,
9 PG&E should be authorized to pay the two categories of refund obligations discussed above
10 pursuant to Section 363(b)(1) of the Bankruptcy Code, which provides that "[t]he trustee,
11 after notice and a hearing, may use, sell, or lease, other than in the ordinary course of
12 business, property of the estate." 11 U.S.C. §363(b)(1).

13 In determining whether to authorize a transaction under Section 363(b)(1), courts
14 require a debtor to show that a sound business purpose justifies such actions, applying the
15 business judgment test. See, e.g., Stephens Indus., Inc. v. McClung, 789 F.2d 386, 389-90
16 (6th Cir. 1986); Comm. of Equity Sec. Holders v. Lionel Corp. (In re Lionel Corp.), 722
17 F.2d 1063, 1071 (2d Cir. 1983); see also 3 Lawrence P. King, Collier on Bankruptcy
18 ¶363.02[1][g] (15th ed. rev. 1998).

19 The burden of establishing a valid business purpose for a transaction outside the
20 ordinary course of business falls upon the debtor. See In re Lionel Corp., 722 F.2d at 1066.
21 Once the debtor has articulated a rational business justification, however, a presumption
22 attaches that the decision was made "on an informed basis, in good faith and in the honest
23 belief that the action taken was in the best interest of the [debtor]." See, e.g., Official
24 Comm. of Subordinated Bondholders v. Integrated Res., Inc. (In re Integrated Res., Inc.),
25 147 B.R. 650, 656 (S.D.N.Y. 1992) (citing Smith v. Van Gorkom, 488 A.2d 858, 872 (Del.
26 1985)).

27 Here, sound business justifications exist for PG&E's pre-confirmation payment
28 of the refund obligations described above. Indeed, as a regulated electric utility, PG&E is
obligated to submit to FERC jurisdiction and obey FERC orders. Moreover, PG&E will be

1 able to resolve these three categories of obligations by effecting refunds totaling
2 approximately \$775,000 in total. PG&E is solvent and has the cash on hand to pay these
3 claims without prejudice to other creditors³.

4
5 **C. Payment Of The Refund Obligations Is Practical, "Legal And Factually**
6 **Inevitable," And In The Best Interests Of Creditors And The Estate; Thus**
7 **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. 2001).

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
17 Section 105 is "to assure the bankruptcy court's power to take whatever action is appropriate
18 or necessary in aid of the exercise of its jurisdiction." 2 Lawrence P. King, Collier on
19 Bankruptcy ¶105.01, at 105-5 to 105-6 (15th ed. rev. 2000); see, e.g., Crafts Precision Indus.,
20 Inc. 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 Comp. 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

26 ³The authorization sought by PG&E would also benefit the estate by reducing post-
27 petition interest costs and streamlining the claims resolution process, thereby allowing
28 PG&E to focus those resources involved in the claims process on larger, more complex
claims.

1 debtor-in-possession to pay pre-petition debt and to allow debtor to pay some creditors in
2 class without paying others without violating Bankruptcy Code, as a "rigid application of the
3 priorities of §507 would be inconsistent with the fundamental purpose of reorganization and
4 of the [Bankruptcy Code's] grant of equity powers to bankruptcy courts, which is to create a
5 flexible mechanism that will permit the greatest likelihood of survival of the debtor and
6 payment of creditors in full or at least proportionately"); see also In re Payless, 268 B.R. at
7 547. As discussed above, the payments PG&E seeks authority to make have sound business
8 justifications and are entirely appropriate.

9
10 IV.

11 CONCLUSION

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

15
16 DATED: April 23, 2003.

17 Respectfully,

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

20 By: 
21 WILLIAM J. LAFFERTY

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