WYNNE S. FURTH (State Bar No. 56397)
GRANT KOLLING (State Bar No. 99858)
CITY OF PALO ALTO
250 Hamilton Avenue
Palo Alto, CA 94301
Tel: (650) 329-2171
Fax: (650) 329-2646

G. LARRY ENGEL (State Bar No. 53484)
ROBERTO J. KAMPFNER (State Bar No. 179026)
JAMES E. TILL (State Bar No. 200464)
WHITE & CASE LLP
Three Embarcadero Center, Suite 2210
San Francisco, CA 94111
Tel: (415) 544-1100
Fax: (415) 544-0202

Special Counsel to Member of Official Committee of Unsecured Creditors, The City Of Palo Alto

50-275/323

UNITED STATES BANKRUPTCY COURT

NORTHERN DISTRICT OF CALIFORNIA

SAN FRANCISCO DIVISION

In re PACIFIC GAS & ELECTRIC COMPANY, a California corporation, Debtor. Tax I.D. No. 94-0742640	Case No. 01-30923 DM Chapter 11 **DECLARATION OF GRANT KOLLING IN SUPPORT OF MOTION OF THE CITY OF PALO ALTO FOR ORDER DIRECTING PAYMENT OF REASONABLE ATTORNEYS' FEES AND COSTS PURSUANT TO SECTION 503(b)(3)(D), 503(b)(3)(F) AND 503(b)(4) OF THE BANKRUPTCY CODE** Trial: Hearing: Time: Place: 235 Pine Street San Francisco, California

I, Grant Kolling, declare as follows:

1. I am a Senior Assistant City Attorney for The City of Palo Alto, a Chartered City and California municipal corporation, counsel of record for The City of Palo Alto, including its

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municipal (gas and electric) utility.

Background on The City of Palo Alto and Its Committee Services

2. As this Court is aware, this Chapter 11 Case is unusual. The interplay between the jurisdiction of the Bankruptcy Court, the Federal Energy Regulatory Commission ("FERC"), and the California Public Utilities Commission (the "CPUC") with respect to the assets, liabilities and operations of Pacific Gas and Electric Company ("PG&E" or the "Debtor") created special and unique challenges in timely developing a fair, feasible and confirmable plan of reorganization that could be expected to become effective within a reasonable amount of time. This is especially true in light of the solvent Debtor's unprecedented approach to achieve its ambitious, yet provocative goals, such as substantial freedom from State regulation of many of its business lines through a "plan of disaggregation" and other means (*i.e.*, what many described as a "regulatory jail break").

3. Throughout this case, The City of Palo Alto ("Palo Alto") has used its specialized knowledge and experience in the energy field and utility business to play a pivotal role in addressing complex issues implicated by PG&E's efforts to reorganize and emerge from bankruptcy. References in this Declaration to "Palo Alto" include its inside and outside counsel working on the matter, whose relevant efforts are known to the Court or described or incorporated herein. Because of the "test case" and unprecedented nature of the various plans of reorganization and amendments proposed by PG&E in this Court and advanced in related proceedings at FERC, the NRC and CPUC prior to the ultimate Settlement Plan (herein collectively described as the "PG&E Litigation Plan"), Palo Alto had to act through its lawyers primarily. Indeed, while we had utility executives and experts with whom to consult, complex and unsettled legal issues predominated in this case, requiring analysis and response by experienced lawyers in both bankruptcy law and utility/energy/governmental law, such as myself (as to the latter) and Larry Engel, a partner formerly at Brobeck, Phleger & Harrison, LLP and then at relevant times Morgan, Lewis & Bockius, LLP and now at White & Case, LLP.

4. Because of the unique nature of this case, the members of the Official Committee of Unsecured Creditors (the "Committee") were compelled to be extraordinarily active and to undertake numerous responsibilities and tasks not usually performed by creditors' committees, much less by individual members. I believe the broad range of complex issues prompted the U.S. Trustee to balance the Committee with carefully selected members representing the full range of creditor constituencies, including generators and QF parties, vendors, financial institutions and (for reasons described below) Palo Alto.

5. I believe that Palo Alto was selected, and its selection was justified, for the following reasons:

(a) Palo Alto, a top-rated municipal (gas and electric) utility in operation for more than a century, has special knowledge of (i) PG&E's assets, liabilities, contracts and businesses (past and present), (ii) applicable California and federal energy and utility laws and regulations, (iii) California governmental unit and agency concerns and dealings with PG&E, (iv) the California legislative process and the realities of effectively dealing with it, (v) investor-owned utility/municipal utility relations, (vi) the core issues about which Palo Alto expressed concern in its objections to the various plans of reorganization and amendments thereto filed in this case, (vii) the governmental and public policy and safety concerns raised by various California counties (the "Counties") in their Certain California Counties' Notice of Application and Application for Allowance and Payment of Compensation and Reimbursement of Expenses under Section 503(B)(3) and (4)(the "Counties Motion"), filed in this Court on or about March 15, 2004, and (viii) other critical matters;

(b) Because I believe that PG&E's audacious approach to its reorganization and to municipal utilities (and other similarly situated governmental agencies) in general exposed Palo Alto and others to the threat of serious harm during the entire case, Palo Alto was highly motivated to invest (and uniquely capable of investing) time and energy in the Committee's activities and in requiring the right kind of reorganization. Palo Alto was among the members regularly available to promptly act for, and in support of, the Committee.

Because Palo Alto had credibility with other members and Committee professionals, the Committee regularly requested or invited services of Palo Alto and solicited its input on a wide variety of projects and issues;

(c) The Committee found Palo Alto to be a useful "foil" and "tough cop" in dealing with PG&E, because (i) PG&E's provocative approach to the plan and many other issues engendered serious concern for many, and (ii) Palo Alto was correctly perceived as an unwilling target of PG&E's aggression, and who would have to resist such conduct. The Committee representatives on occasion appealed to PG&E for less provocative approaches to Palo Alto and the PG&E Litigation Plan. The Committee and others welcomed Palo Alto's primary efforts to educate PG&E to the mistakes inherent in litigation of the unchartered, legally questionable and politically ill-advised path to jurisdictional disaggregation of its assets and other controversial features of the PG&E Litigation Plan. Indeed, I believe that many, if not all, of the major creditor parties in the case perceived Palo Alto's responses to PG&E's conduct to be appropriate and conducive to the general efforts to attempt to moderate PG&E's positions with respect to many issues of common concern, especially since PG&E continuously insisted (incorrectly) that the PG&E Litigation Plan was the only possible plan, thus requiring objections to clear that plan out of the way for a better and more feasible plan;

(d) The Committee and other major parties recognized very early that Palo Alto's approach to PG&E's conduct was not contrary to their own interests. The reforms sought by Palo Alto in improvements to the various plans and objections to PG&E's other controversial actions (*e.g.*, unnecessarily harming QF's and other disputed or pass through creditors with meritorious claims in order to create further excess benefits for equity) advanced the interests of all creditors. Because Palo Alto's goal was to moderate PG&E's audacious approach, I believe that, until the Final Phase addressed below, other creditors did not perceive Palo Alto as an obstacle to their goals of prompt, full payment of their claims, but rather a help toward that goal, since the PG&E Litigation Plan needed to be superseded for progress to be made in the case; and

(e) The Committee represented the interests of both the creditors with undisputed claims who do not have a vested interest in a long-term relationship with PG&E, and other creditors (many of whose claims were disputed or passed through by PG&E) who are compelled by the nature of the energy business to maintain and on-going relationship with PG&E. Palo Alto served as a useful bridge for the Committee to those creditors in the latter category.

6. I have read and approved the Motion of the City of Palo Alto for an Order Directing Payment of Reasonable Attorneys' Fees and Costs Pursuant to Section 503(b)(3)(D) 503(b)(3)(F) and 503(b)(4) of the Bankruptcy Code (the "Palo Alto Motion"). I believe that the factual statements therein regarding the actions and positions of Palo Alto to be true and correct.

7. I have read the County Motion and, except as noted herein or in the Palo Alto Motion, I believe that Palo Alto also made the same kinds of contributions that were referred to in the County Motion with respect to governmental units' concerns and public policy and safety concerns, although to avoid duplication and to defer to the greater involvement of the Counties in such matters, Palo Alto left the details of the tax, nuclear decommissioning and environmental issues to the Counties. The work of Palo Alto on those public policy matters was less visible than that of the Counties for several reasons, including, in particular, (i) because most of the "backstage" work of the Committee was not revealed, including due to PG&E confidentiality agreements, and (ii) because in avoiding duplication at discovery, trial and arguments, Palo Alto followed the Counties in order and only occasionally perceived the need for follow up questions or arguments.

8. I have also read the Declaration of Philip S. Warden (the "Warden Declaration") In Support of the Application of Dynegy Power Marketing, Inc. For Payment of Administrative Expense for Its Substantial Contribution In Case (the "Dynegy Application"). The constructive actions of Dynegy described in the Warden Declaration, except for Dynegy's Class 6 settlement activities, were also taken or joined in by Palo Alto, and such contribution arguments made for the Dynegy Application are also applicable to Palo Alto

9. In the nearly three years after the Debtor filed its petition, the Committee as a whole or by its various subcommittees or working groups held approximately 100 in-person and telephonic meetings which Palo Alto attended. In addition to meetings of the Committee as a whole, the Committee created at least four subcommittees (Finance, Legislative/Regulatory, Litigation, and Plan Negotiation). Less formal working groups met and then reported to the full Committee. Moreover, there were literally thousands of telephone calls and e-mail messages exchanged between and among the Committee members and its professionals throughout the proceedings.

10. Because of its specialized knowledge, and relevant experience, Palo Alto was selected to chair the Legislative/Regulatory Subcommittee and to serve on both the Plan Negotiation and Finance Subcommittees. The Legislative/Regulatory, Plan Negotiation and Finance Subcommittees' members met in-person or by telephone frequently, especially during the first eighteen to twenty-four months. Additionally, because of the implausibility of PG&E's contention that the PG&E Litigation Plan was the only possible plan and a desire to understand the real alternatives, Palo Alto served on an informal subcommittee to evaluate the option of a sale of selected assets, including "Plan C" mentioned to the Court on occasion. The fact of such a "fallback" alternative was beneficial to creditors, so that they did not feel that they had no choice but to wait for the many years (at best) that would be required for any PG&E Litigation Plan to become effective, if ever. PG&E's zealous pursuit of the legally questionable and politically infeasible PG&E Litigation Plan created concerns for many creditors, which perceived PG&E's efforts as a potential, substantial barrier to emerging promptly from Chapter 11 with an effective lawful and fair plan. During this phase, some felt it was appropriate to initially consider sales of certain PG&E's assets at fair prices and on terms and conditions more economically favorable than that purportedly offered by the PG&E Litigation Plan. These parties and others considered the threat of such an alternative to be one of the few means of compelling PG&E to moderate its quixotic approach to reorganization.

11. In addition to its subcommittee services, Palo Alto performed other important

roles that supported the Committee's mission. For example, Palo Alto served as a liaison to California cities located in PG&E's service territory during their negotiations with PG&E in regard to new franchise agreements for PG&E's ETrans and GTrans entities. Further, Palo Alto, at the Committee's request, served as one of the Committee's representatives with respect to certain other matters that arose during the case, including legislative and governmental issues.

12. Because there was always so much to do on an urgent basis, including evaluating what PG&E was doing and proposing and PG&E's stated justifications, the Committee did far more than meet occasionally to discuss and ratify the actions of the Committee's professionals. Instead, there was an active, nonduplicative collaboration among the members and Committee professionals, in which members (often through counsel, since the legal issues predominated) developed ideas and reactions to share with the professionals and vice versa. But for such collaboration, many more Committee professionals would have been required at much greater expense. Because many of PG&E's approaches were not grounded on settled law and were certain to trigger litigation and other side-effects, it was important for the Committee and its professionals to hear a variety of perspectives and experiences from the members' inside and outside counsel, both to assure that the many issues were comprehensively addressed and also to make sure that the Committee and its professionals had independent data on the many activities in many different forums without either having to incur the expense of the Committee professionals monitoring everything of possible relevance or having to rely solely on PG&E's reports for information.

Phases of the PG&E Case

13. Palo Alto's contributions have varied during each phase of the case, which can be briefly described as follows.

(a) The "Negotiation Phase." During the initial phase of the case and until PG&E proposed the PG&E Litigation Plan (the "Negotiation Phase"), Palo Alto went to great efforts to avoid open and notorious disputes with PG&E. Palo Alto assisted the Committee in attempting to persuade PG&E to moderate its plan of reorganization and other dealings with

creditors, as well as attempting to reconcile the CPUC and the State with PG&E. During this Negotiation Phase, Palo Alto generally refrained from criticizing PG&E on the record, participating instead in the Committee's confidential negotiating process with PG&E to attempt to convince PG&E of more feasible and less contentious alternatives. Indeed, Palo Alto quietly endured what it perceived to be various PG&E acts of provocation in the hopes of achieving both a better plan and a peaceful reconciliation for itself and with respect to other governmental units. During this period, Palo Alto assisted in the negotiation of a temporary cessation of conflict regarding the Western Area Power Administration's ("WAPA") contract with PG&E. Unfortunately, even with the assistance of the Committee, Palo Alto could not dissuade or prevent PG&E from threatening to take or taking certain actions detrimental to Palo Alto's vital economic interests, such as (i) terminating the Interconnection Agreement on which Palo Alto depended for electric transmission under prejudicial circumstances, as described in the antitrust estimation proceedings, and (ii) attempting to substantially increase the gas transmission pricing to Palo Alto by reclassifying Palo Alto from a "noncore" industrial/wholesale type customer into a "core" consumer customer, as described in the Settlement Plan trial proceeding. (The CPUC ALJ eventually rejected that attempt to reclassify Palo Alto from its historical, "noncore" or wholesale gas transmission customer classification, with other large and industrial customers, to a new "core" or retail customer classification.)

(b) The "Plan Dispute Phase." Once PG&E filed its initial PG&E Litigation Plan, Palo Alto began its effort to improve that plan and the amended and subsequent plans which PG&E and then the CPUC, respectively, attempted to confirm (the "Plan Dispute Phase"). Because PG&E insisted on its PG&E Litigation Plan as the only plan it would consider, the path to a better and feasible plan required that the nonfeasible and divisive PG&E Litigation Plan be removed as an obstacle to a better and more feasible plan. Palo Alto also believes that its opposition improved each plan in ways that the plan proponents would not voluntarily accept without court-required reforms or clarifications. I believe that these improvements did not undermine the economics needed to pay creditors in full. They were

generally offered to minimize the incentives and ability of PG&E to abuse its monopoly power by economically harming municipal utilities and other continuing creditors in ways that would also be counterproductive for PG&E and its creditors in the long run. In my opinion, Palo Alto's effort to moderate PG&E's provocative approach, whether or not it could be cost-effectively proven to be tortious or wrongful, was in the best interest of creditors and, as demonstrated in practice, in the long-term best interest of PG&E and its creditors. Indeed, the ultimately confirmed Settlement Agreement (and, therefore, the Settlement Plan) included various of Palo Alto's recommendations and suggestions, and the Court's related rulings also protected creditors from some of the possible adverse interpretations of the Settlement Agreement and Plan.

(c) The "Final Phase." As a direct result of Palo Alto's opposition to the Proposed Settlement Agreement and related Settlement Plan, important reforms and clarifications were made by this Court and by the CPUC, and further risk to PG&E's continuing pass-through and disputed creditors were also reduced. Palo Alto appealed in an effort further to reduce such risks and threats to Palo Alto in the future, but, as expected, those activities have not interfered with the effectiveness of the Settlement Plan. Palo Alto is not requesting reimbursement for any post-confirmation expenses, even though I believe Palo Alto may achieve other long-term benefits for pass-through and disputed creditors through its continuing efforts post-confirmation, hopefully by settlement.

Palo Alto notes the following illustrative contributions for the benefit of creditors, especially those who are governmental units or otherwise have to continue to deal with PG&E:

(1) Although Palo Alto opposed some aspects of the CPUC/Committee Plan in order to induce reforms that the CPUC was disinclined to impose on PG&E, Palo Alto helped preserve the essential defense of the Reorganization Agreement (proposed by the CPUC) from PG&E's attacks. That unselfish Palo Alto action anticipated the foreseeable risk that PG&E might later be able to use (and did use against Palo Alto) the

Reorganization Agreement as a basis for the more challenging and problematic Proposed Settlement Agreement with the CPUC. Nevertheless, like the Committee, Palo Alto believed that the ultimately successful plan that Palo Alto aspired to help create would include such a Reorganization Agreement;

(2) While Palo Alto continued to object in order to achieve reforms, it also acted to save the CPUC/Committee Plan against PG&E's assault on the apparent weaknesses of the CPUC's case regarding the cram down of PG&E's equity, including a hole in the evidence that PG&E used to seek to defeat the plan. Palo Alto observed that the Committee's only possible rehabilitating witness, Tom Lumsden, had been unable to fully cover the CPUC/Committee's position, because of limitations in what he was permitted to address in the CPUC direct case. Because PG&E had "opened several doors" in its cross-examination, Palo Alto's separate cross-examination of Mr. Lumsden thereafter served to preserve the Plan from possible defeat by PG&E's vigorous opposition, thus preserving the plan's leverage as an alternative to the PG&E Litigation Plan and facilitating the ultimate settlement (i.e., that rescued the CPUC/Committee Plan, which became the foundation for an improved Settlement Plan thereafter);

(3) Palo Alto alone joined the Committee in advocating the final settlement process that culminated in the Settlement Plan. But for Palo Alto's effort to improve the PG&E Plan through settlement negotiations (ironically, PG&E then excluded Palo Alto and other objectors besides the CPUC from the negotiations), the PG&E Litigation Plan might have been confirmed, although it probably never would have become effective. That result would have been financially and otherwise detrimental for many interested parties, including the vast majority of creditors who did not want to wait years for an effective date. Moreover, Palo Alto's objections to the competing plans, and its success in compelling critical amendments to the competing plans, helped facilitate the settlement process that benefitted many interested parties (but not necessarily Palo Alto);

(4) Palo Alto's objections to the Settlement Agreement and

Settlement Plan resulted in several improvements to the Settlement Agreement and Settlement Plan (some were specified by this Court's rulings, others required by the CPUC itself), including provisions designed to narrow dangerous interpretations and clarify limitations of the adverse impacts of the Settlement Agreement and Settlement Plan. Even PG&E was compelled to offer some revised interpretations of its Settlement Agreement and Settlement Plan in response to Palo Alto's and others' principled challenges;

(5) Even though Palo Alto is not seeking reimbursement in this application for its costs incurred in the antitrust estimation proceeding, Palo Alto believes that its efforts have benefited creditors and others (i) by developing further evidence against the PG&E Litigation Plan, especially as to its electric transmission flaws and ETrans problems, (ii) by moderating the approach of PG&E to various disputes in multiple forums, and (iii) by reducing the ultimate risk of a regulatory, legislative and public relations backlash against PG&E. In this and other respects, Palo Alto's strong complaints about PG&E's conduct sometimes had the desired effect of moderating the threat of harms which PG&E sought to inflict on Palo Alto and other PG&E customers on whom Palo Alto depends (*e.g.*, Northern California Power Agency, Transmission Agency of Northern California, and WAPA.); and

(6) All of the clarifications and reforms in the Settlement Plan resulting from Palo Alto's objections, as well as from the earlier plans to which Palo Alto objected (many of which were carried forward into the Settlement Plan) are in the long-term best interest of creditors and PG&E. But for Palo Alto's objections and resulting attention to the issues, I believe that PG&E would have persisted in far more aggressive actions in ways that would have ultimately created a backlash, including greater regulatory and legislative restraints on PG&E. While Palo Alto continued, with the support of some creditors, to object vigorously to PG&E's aggressive conduct or tactics, other major creditors did not oppose Palo Alto's efforts in this regard as they knew from direct experience (or even mediation efforts on Palo Alto's behalf) how aggressive PG&E was toward municipal utilities like Palo Alto.

For the reasons stated above, Palo Alto believes that it has worked both quietly and effectively both behind the scenes and in the public litigation, playing a unique and important role in this case in its service on or for the Committee and making a substantial contribution to the success of this case. Palo Alto's efforts were not duplicative of the efforts of any other party in this case seeking such reimbursement now; moreover, Palo Alto has generally either been supportive of various Committee positions and activities or has been useful in achieving results that were beneficial, such as creating sufficient doubts about the PG&E Litigation Plan in order to make a better plan possible. In short, Palo Alto's efforts enabled the bankruptcy to move toward confirmation of a plan and helped to ensure the successful emergence of the Debtor intact as a vertically integrated entity – a result that would not have been as assured, but for Palo Alto's active and forceful participation.

Palo Alto Expense Data

14. Attached hereto are redacted invoices for the applicable services that Palo Alto employed from the same team of lawyers, first from Brobeck, Phleger & Harrison, LLP, and then from Morgan, Lewis & Bockius, LLP. No waiver of the attorney-client or work product privileges is intended by release of those invoices. While those lawyers performed more services than those for which Palo Alto requests reimbursement, I have excluded those that relate to Palo Alto's individual claim recovery efforts, including the antitrust estimation proceeding activities and efforts in other forums, even though Palo Alto could argue that those efforts had some general benefits for creditors, especially pass-through and disputed creditors, as well as enhancing the knowledge and evidence also used in the tasks for which Palo Alto seeks reimbursement. For example, the discovery and related work done by counsel for Palo Alto in connection with the antitrust estimation proceeding in this court and in the FERC proceedings for which no reimbursement was sought enhanced Palo Alto's ability to address the electric transmission problems at issue in the plans of reorganization. Similarly, Palo Alto's participation in the CPUC and NRC process for which no reimbursement is sought also enhanced Palo Alto's reimbursable efforts.

15. Although the Northern California Power Agency ("NCPA") also participated in the Chapter 11 case and its counsel and staff contributed value in collaboration with Palo Alto, the NCPA is not making a substantial contribution claim. To the extent that the Northern California Power Agency has contributed benefits to Palo Alto in order to support these efforts by Palo Alto for which reimbursement is sought by Palo Alto, Palo Alto is collecting all of the specified attorneys' fees and costs incurred by Palo Alto, and Palo Alto will satisfy whatever subrogation or other rights NCPA might have.

16. Palo Alto has incurred legal fees and expenses for which it seeks reimbursement in the amount of $1,901,913.48 during the Application Period, as well as substantial other legal fees and expenses with respect to the PG&E Chapter 11 case and related proceedings for which Palo Alto does not seek reimbursement here.

I declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge, information and belief.

Executed this 8th day of July, 2004 in San Francisco, California.

Grant Kolling