

**Restructuring in the Rearview Mirror – a 10-Year Retrospective of California's
Doomed Experiment with Electric Deregulation. By The Energy Overseer**

**From Street Theater to Strict Protocols, PG&E's First Week in Court Goes
by the Numbers**

[The Pacific Gas & Electric Chapter 11 filing of April 6 represented the most important utility bankruptcy case in US history and ranked as the top corporate asset restructuring proceeding in 20 years. The politics of PG&E's decision to enter bankruptcy were simple: to try to escape some of the California Public Utilities Commission's attempts to assert power over nonutility assets, and to effect a business reorganization that would transfer key operations into federal jurisdiction.]

The biggest little show opening in town this week turned out to be Pacific Gas & Electric's Chapter 11 case, convened in Courtroom No. 22 of the US Bankruptcy Court, Northern District of California, with Judge Dennis Montali presiding [No. 01-30923-DM]. With scores of attorneys, reporters and consumer representatives trying to squeeze into the court, guards at the security check-in point joked that they were busier than a BART station and had timed the building's elevators to match arrival schedules at the nearby transit station in San Francisco's Financial District.

Judge Montali, a former Naval Reserve officer who saw active duty aboard two destroyers and then became an instructor at the Naval Reserve Officers Candidate School prior to his law career, is known to run a tight ship in the court. He proved it again this week.

The scene for Monday's opening session was enlivened by street protestors who tried to carry their demonstration into the courtroom. Activist Medea Benjamin evidently had not read Judge Montali's rules for courtroom decorum: "No member of the media or the public shall direct any queries to the judge, court staff or the parties while court is in session."

When Benjamin approached the bench and said she had an "open letter" to read, the judge cut her short and sent her back to a seat in the packed gallery. In other forums, such as meetings of the California Public Utilities Commission and this week's congressional field hearings in San Jose, Benjamin and other members of the Coalition for Public Power Now group pressed their protests to the point of being ejected from the hearing rooms. In this case, she followed the judge's stern admonition and sat down. He later allowed her to read the statement but told the activists that if they want a full explanation of the proceedings, they should hire an attorney.

The first order of business for the judge was to approve a series of motions by PG&E meant to keep money flowing for operations. On the day the utility filed for Chapter 11, April 6, Montali immediately endorsed expenditures of \$50 million for wages, benefits and bonuses to nonunion, nonexecutive

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management that PG&E CEO Bob Glynn approved the day before and another \$38 million in benefit obligations and taxes.

Though controversial, the payments were deemed necessary by PG&E to reward employees for past performance and to keep key staff aboard during what is expected to be a long, drawn out financial restructuring.

The judge also allowed PG&E access to money in operating accounts--subject to possible bank liens--and the use of existing business forms and letterhead without the required "debtor-in-possession" stamp. Montali said he felt the case was probably well enough known that anyone doing business with the utility would be aware of its status, and that forcing new forms would impose burdensome costs and be "extremely disruptive to daily business operations."

Among actions this week were a half-dozen interim orders approving PG&E motions: to use cash collateral pledged to natural gas suppliers to continue fuel purchases; to rely on collateral pledged to mortgage bondholders to maintain operations; and to return \$5.3 million in past security deposits for residential customers who paid up front for installations and line extensions. The motion also covers future refunds, estimated at \$1.7 million per month for households and \$1.8 million for business customers.

While Montali allowed these deposits to flow back to customers, he deferred on a motion to refund some \$286,000 to large commercial customers who had paid deposits on new interconnections. The total refund liability might be as much as \$250 million over time, and with so many utility debts outstanding to thousands of utility creditors, Montali reasoned, it did not make sense to take such a large pot of money off the table.

During a case management conference Thursday, Montali rejected petitions from four Central Valley cogenerators that wanted to be released from their qualifying facility contracts because they had not been paid. PG&E's attorney said that checks would be going out next week. Montali set aside the issue but warned he would hold hearings if PG&E does not pay as promised.

Through it all, the judge lived up to his reputation as an active overseer, strong on legal requirements and strict as to form, but not without a sense of humor. At one point, he professed an inability to see the future of natural gas prices and warned participants that solving the energy crisis single-handedly is beyond his judicial powers.

Outside the court, US trustee Linda Ekstrom Stanley this week cobbled together a creditors' committee to represent companies owed money by the utility from among a list of the 100 top unsecured creditors. Eleven firms and entities were included--although the court had received scores of requests for participation. Four financial institutions were named to the committee: Bank of

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New York, the single largest creditor with \$2.2 billion in the hole; BankAmerica, \$1.175 billion; US Bank, \$310 million; and Merrill Lynch, \$106 million.

The four power marketers and qualifying facility owners on the committee were Enron Corp., \$580 million; Dynegy Power Marketing, \$225 million; KES Kingsburg, \$182 million; and GWF Power Systems, \$62 million. The Davey Tree Expert Company, a longtime vegetation-control contractor for PG&E, was said to be owed \$9.6 million. Also on the committee will be representatives of the city of Palo Alto, with a \$200 million claim, and the state of Tennessee, which is out \$75 million--some \$25 million in employee retirement funds and \$50 million in general fund investments.

Left off the list were two California agencies, the Power Exchange--itself in Chapter 11--and the Independent System Operator. Though listed among the top five creditors in PG&E's filing, CalPX (\$1.96 billion) and Cal-ISO (\$1.228 billion) are largely pass-through agencies, with ultimate creditors such as the power marketers and energy producers given a higher priority on the committee. Also not directly participating will be Calpine Corporation, which had five generation subsidiaries on the top-20 list, owed more than \$200 million, according to PG&E's filing. Calpine has said PG&E's total debt to it is closer to \$275 million.

PG&E has claimed as much as \$9 billion in debt related to the difference between what it had to pay for power and what it could collect in rates. As part of the April 6 bankruptcy petition, the utility spelled out its cash-flow crunch. Besides a monthly power debt expected to reach \$600 million following a recent CPUC rate order, PG&E has defaulted on \$873 million in commercial bond liabilities. As of March 29, PG&E had \$2.6 billion in cash.

"If the company were current with all payments to its creditors (including \$938 million balance of its bank loans) its cash position would be negative \$1.8 billion," the utility said. Another \$1.5 billion in payments to gas suppliers, Cal-ISO and QFs is due at the end of April, with at least another \$1.4 billion in long-term debt that will come due at the end of the year. "In sum," PG&E said, it "does not have the cash on hand to pay its obligations, it cannot borrow the cash to do so, and it anticipates that the obligations it continues to incur will grow faster than the revenues it anticipates it will receive."

The most contentious issue raised during the first week of proceedings is a key legal conflict between the regulatory authority of the CPUC and the power of the bankruptcy judge over past revenues. In a motion filed April 9, PG&E asked Judge Montali to stay the CPUC's recent rate order, in which utilities were told to recalculate restructuring transition cost accounts and to offset stranded-cost collections since 1998 against the high costs of generation procurement since last summer [D01-03-082].

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While PG&E and Southern California Edison had argued that they completed stranded-cost collections last August, thus ending the rate freeze and putting ratepayers on the hook for energy costs, the CPUC ruling refused to accept the argument. Instead, according to PG&E, the order would result in a recalculation that puts past recovery amounts at risk and means the rate freeze will run its full statutory term, through March 2002. PG&E told the court this would "prevent PG&E from recovering billions [of dollars] in accumulated revenue shortfalls" in its transition revenue account. The utility contends the CPUC order is illegal, and it asked the court to enjoin compliance with the order, especially regarding an April 11 deadline for the utility to provide a new accounting that reflects the CPUC's determinations.

Rather than take up the matter as scheduled Wednesday afternoon, Judge Montali gave PG&E and the CPUC time to work out a compromise. Though he took consideration of a temporary restraining order off the calendar, Montali has set the issue for review on May 14.

On May 9, the judge will take up final hearings on cash-control issues and on collateral-use matters **[Arthur O'Donnell]**.

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