

**Restructuring in the Rearview Mirror – a 10-Year Retrospective of California’s
Doomed Experiment with Electric Deregulation.
Courtroom 22 Coverage of the PG&E Bankruptcy**

Stakes Increase in PG&E Bankruptcy as Administrative Claims Are Filed

The state of California put something very special on the line in the Pacific Gas & Electric bankruptcy proceeding--its sovereign immunity from federal court jurisdiction. This week, the state decided to risk opening itself up to second-guessing by the court in order to collect \$179 million in energy payments said to be owed to the Department of Water Resources through June 30. The figure may be revised after forthcoming settlements of expenses incurred by the California Independent System Operator on behalf of DWR and the utilities.

Data filed with the court show that DWR on June 12 billed PG&E for \$531 million in energy purchases between January 17 and June 1, not including some Cal-ISO imbalance energy expenses.

Another state claim for as much as \$230 million will be filed by the October 3 deadline for administrative claims, said attorney general Bill Lockyer this week. That is what the state estimates PG&E owes to a variety of state agencies for everything from taxes to environmental mitigation costs.

The filing of claims could be the first step in a much more extensive intervention in the PG&E Chapter 11 case than the state has been willing to risk to date. So far, it has been to the state’s advantage to claim immunity from federal jurisdiction, which has kept Judge Dennis Montali wary of trying to assert jurisdiction over certain matters in the proceeding, particularly the application of California Public Utilities Commission orders on possible termination of PG&E’s rate freeze and ratemaking accounting.

There is a major jurisdictional tiff looming with regard to PG&E’s recently proposed plan of reorganization, however. Statements from Governor Gray Davis last week indicate that the state intends to fight PG&E’s proposed transfer of generation and transmission assets out of the state-regulated utility as part of a restructuring effort.

AG Lockyer this week said his office “will fight efforts by the utility to use the federal bankruptcy court to raid the pockets of taxpayers.” Lockyer added, “We are also looking closely at the PG&E reorganization plan because of the serious concern that the utility is seeking to evade further scrutiny by the California Public Utilities Commission and is seeking to avoid state laws that apply to their transfer of funds.”

The attorney general was referring to ABx1-6, which forbids disposal of utility generation assets until at least 2006 and requires the CPUC to maintain ratemaking authority over utility power generation.

The PG&E plan clearly intends to sidestep state law but asks the bankruptcy court to authorize a transfer of assets that would result in putting nuclear units and hydro assets under federal jurisdiction.

The transfer price, \$4.5 billion in cash and new debt issues, roughly corresponds to the valuations that PG&E has tried unsuccessfully to get the CPUC to accept in its continuing effort to end the statutory rate freeze.

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While consumer advocates call the transfer theft, PG&E Corporation chief executive officer Robert Glynn this week told a Dow Jones reporter, “Consumers don’t own those assets and they never have.” Glynn also said that there is no sale of the assets involved. “All the asset values are owned ultimately by the shareholders of PG&E Corp. And at the end of the day, all of the asset values will still be owned by the shareholders of PG&E.” He asserted PG&E’s position that the bankruptcy court may supercede state laws in order to effect a reorganization plan that satisfies recognized creditors.

Separately, Lockyer’s office recently filed a limited intervention in the PG&E case in order to promote the state’s interest in hundreds of millions of dollars’ worth of block-forward contracts that Governor Davis had commandeered from the California Power Exchange last winter. Lockyer’s office on September 10 moved for a waiver of PG&E’s immunity from legal challenges during bankruptcy. Noting several pending challenges to the state’s takeover of the contracts, Lockyer’s attorneys said they want to try to consolidate the various cases but need to clear such actions with the courts handling the PG&E and CalPX Chapter 11 proceedings.

The legal lines blurred even further last week, following a US Ninth Circuit Court of Appeals determination that Davis’ seizure of the contracts violates federal authority and power sellers’ rights.

The change in market prices turned those contracts into something of a liability. Because CalPX is itself in bankruptcy, it could not even squeeze a benefit from the contracts. Sellers would probably rather the DWR continue buying the power at contract prices than look for new buyers in a depressed market. Probably the biggest value to the contracts will be in setting a market valuation for CalPX’s compensation claim against the state as it tries to settle out with its creditors.

On September 26, state controller and chair of the Franchise Tax Board Kathleen Connell announced that the board had filed its own claim against PG&E for \$22 million in taxes owed the state. The board said the claim amount is based on an audit for the years 1994, 1995, 1997 and 1999.

California was not the only entity filing claims related to DWR power sales, though some companies filed claims for zero in order to exercise rights in the event of changes to Cal-ISO settlements. The first batch of claims made by marketers this week covered the April 6-April 30 period.

Williams Energy Marketing and affiliated companies are seeking \$39 million. Duke Energy claimed \$414,400 for its Oakland peaking units and zero for operations at Moss Landing and Morro Bay. Similarly, Reliant Energy entered a zero claim for April in order to preserve its rights. Williams had previously filed a claim for up to \$591 million in prebankruptcy energy deliveries **[Arthur O’Donnell]**.

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