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9 UNITED STATES BANKRUPTCY COURT
10 NORTHERN DISTRICT OF CALIFORNIA
11 SAN FRANCISCO DIVISION

12 In re

13 PACIFIC GAS AND ELECTRIC COMPANY,
14 a California corporation,

15 Debtor.

16 Federal I.D. No. 94-0742640
17

Case No. 01-30923 DM

Chapter 11 Case

Date: September 26, 2003

Time: 10:30 a.m.

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

Judge: Hon. Dennis Montali

18 DECLARATION OF JOSEPH SAUVAGE IN SUPPORT OF MOTION FOR
19 AUTHORITY TO ENTER INTO CERTAIN HEDGING TRANSACTIONS IN
20 CONNECTION WITH FINANCING UNDER PROPOSED PLAN OF
21 REORGANIZATION, AND TO INCUR SECURED DEBT RELATED THERETO

22 1. I am a Managing Director of Lehman Brothers Inc., an affiliate of Lehman
23 Brothers Special Financing Inc. ("LBSF"), which is a proposed counterparty with respect to the
24 Interest Rate Hedges that Pacific Gas and Electric Company, the debtor in the above-captioned
25 bankruptcy case ("PG&E"), seeks authority to enter into pursuant to PG&E's Motion For Authority
26 To Enter Into Certain Hedging Transactions In Connection With Financing Under Proposed Plan Of
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1 Reorganization, And To Incur Secured Debt Related Thereto (the "Motion").¹ I make this
2 declaration (this "Declaration") in support of the Motion in support of a finding that LBSF has acted
3 in "good faith," as such term is defined in Section 364(e) of the Bankruptcy Code, in entering into
4 Interest Rate Hedges and Hedge Agreement with PG&E as described in the Motion. This
5 Declaration is based on my personal knowledge (except as to any matters stated on information and
6 belief, and as to such matters, I am informed and believe they are true) and upon my review of the
7 Motion. If called as a witness, I could and would testify competently to the facts stated herein.
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9 2. Lehman Brothers Inc., an affiliate of LBSF, and certain other affiliates of LBSF
10 (collectively, "Lehman"), have provided and may in the future provide investment banking services
11 to PG&E Corporation (the "Corporation") and various affiliates, including acting as a financial
12 advisor to the Corporation during this bankruptcy case.
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14 3. Lehman has held and may in the future hold debt and/or equity securities issued
15 by PG&E, the Corporation, and/or various affiliates.
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17 4. Because of the magnitude of PG&E's Chapter 11 case and the relatively large
18 number of parties in interest, it is impractical, if not impossible, for Lehman to represent that it has
19 disclosed all of its relationships with all of the parties in interest herein; it should be assumed that
20 Lehman has or may in the future have substantial commercial relationships with numerous parties in
21 interest in this case that engage in transactions in the financial markets.
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23 5. LBSF has extensive experience in arranging and engaging in hedging
24 transactions, including transactions of the type defined as "Interest Rate Hedges" in the Motion.

25 Based on such experience, LBSF is prepared to enter into Interest Rate Hedges and Hedge
26 Agreements with PG&E, even though LBSF is not aware of any substantially similar precedent for
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28 ¹ Unless otherwise defined herein, capitalized terms used herein shall have the meanings ascribed to such terms in the Motion.

1 the particular Interest Rate Hedges contemplated pursuant to the Motion in view of PG&E's status
2 as a Chapter 11 debtor.

3 6. LBSF has conducted extensive, arms-length negotiations with PG&E regarding
4 the Interest Rate Hedges and the prospective Hedge Agreements, and the final Hedge Agreements
5 that result will be the product of such arms-length negotiations. LBSF and PG&E have been
6 represented by separate counsel in connection with such negotiations.
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8 7. In its capacity as a financial advisor to the Corporation and as a financial
9 institution experienced in interest rate hedge transactions, Lehman believes that any investment-
10 grade-rated financial institution proposed to be a counterparty to any Interest Rate Hedge with
11 PG&E will require (acting on a commercially reasonable basis), as a condition to entering into any
12 Hedge Agreement(s) with PG&E and as a term of such Hedge Agreement(s), the bankruptcy-related
13 terms described in the Motion, including, without limitation, (i) that if PG&E requires a
14 counterparty to post collateral to secure PG&E's credit exposure to such counterparty above
15 negotiated threshold levels, PG&E too will be required to post collateral to secure the counterparty's
16 exposure to PG&E and that PG&E will be required to post such collateral on a priming basis under
17 Bankruptcy Code Section 364(d), and (ii) that the counterparty has immediate and self-executing
18 relief from the automatic stay of Bankruptcy Code Section 362(a) to enforce its rights and remedies
19 under the Hedge Agreement(s) it enters into with PG&E. Lehman believes that the bankruptcy-
20 related provisions that will be included in the Hedge Agreements as described in the Motion are fair
21 and reasonable based upon the benchmarks and standards for financing transactions with Chapter 11
22 debtors, and that comparable terms would be required by other institutional counterparties if PG&E
23 entered into substantially similar hedge transactions with other institutional counterparties.
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8. Lehman has made and will make no payment promise or undertaking to any officer or director of PG&E, the Corporation or any of their affiliates as a *quid pro quo* for entering into any Interest Rate Hedges or Hedge Agreements.

I declare under penalty of perjury under the laws of the United States of America that the foregoing is true and correct. Executed this 29th day of August, 2003 in New York, New York.

JOSEPH SAUVAGE