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Hearing Date: February 21, 2008 at 10:00 a.m.
Objection Deadline: Monday, February 11, 2008

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF NEW YORK

In re:	)	**Chapter 11**
	)	
Quebecor World (USA) Inc., et al.,	)	**Case No. 08-10152 (JMP)**
	)	**Jointly Administered**
	)	
Debtors.	)	**Honorable James M. Peck**
	)	

OBJECTION OF CERTAIN UTILITY COMPANIES TO MOTION OF THE DEBTORS FOR INTERIM ORDER DETERMINING ADEQUATE ASSURANCE OF PAYMENT FOR FUTURE UTILITY SERVICES AND/OR RELIEF PROVIDED TO DEBTORS UNDER INTERIM ORDER UNDER 11 U.S.C. §§ 105(a) AND 366 DETERMINING ADEQUATE ASSURANCE OF PAYMENT FOR FUTURE UTILITY SERVICES

Consolidated Edison Company Of New York, Inc. ("ConEd"), Duke Energy Ohio, Inc. ("DEO"), Duke Energy Carolinas, LLC ("DEC"), New York State Electric and Gas Corporation ("NYSEG"), The Commonwealth Edison Company ("ComEd"), PECO Energy Company

("PECO"), Piedmont Natural Gas Company ("PNG"), and Virginia Electric and Power Company, d/b/a Dominion Virginia Power ("DVP") (collectively, the "Utilities"), by their undersigned counsel, object to the *Motion Of The Debtors For Interim Order Determining Adequate Assurance Of Payment For Future Utility Services* And/Or Relief Provided To Debtors Under *Interim Order Under 11 U.S.C. §§ 105(a) And 366 Determining Adequate Assurance Of Payment For Future Utility Services* (the "Utility Motion" and the "Interim Order"), and set forth the following:

Introduction

Despite the fact that Congress amended Section 366 of the Bankruptcy Code to reverse the prior practice of many bankruptcy courts making an initial determination of adequate assurance of payment on motions heard on an *ex parte* basis at the commencement of the bankruptcy proceeding, these and other debtors, have been filing motions at the outset of their bankruptcy proceedings seeking specifically to avoid the provisions and requirements set forth in the amended Section 366 for the provision of adequate assurance of payment to utilities. Section 366, as amended, requires a debtor to provide utilities with adequate assurance of payment that is satisfactory to the utility within thirty (30) days of the Petition Date. If a debtor believes the amount of the utility's request needs to be modified, the debtor can file a Motion with the Court seeking to modify the utility's request (a "Modification Motion"). Moreover, if the debtor acts promptly, it can file and schedule the Modification Motion to be heard before the thirty-day period expires. Thus, in addition to failing to provide their utilities with adequate assurance of payment as required by Section 366 of the Bankruptcy Code, the Debtors are seeking to escape the statutory requirements in Section 366(c)(3) which provides that in order to modify the Utilities' request for adequate assurance of payment the Debtors must: (1) file an appropriate

pleading seeking to modify the request; and, (2) present evidence why the Court should consider the Debtors' request to modify the deposit amount requested herein by the Utilities.[1] The Debtors were not even aware of the Utilities' requests for adequate assurance of payment when they filed the Utility Motion, so it is clear that the Utility Motion is not a Modification Motion required by Section 366(c)(3). Accordingly, the Court should deny the Utility Motion and require the Debtors to comply with the requirements of Section 366.

Further, instead of contacting their utility companies,[2] as identified on Exhibit B attached to the Utility Motion, and/or waiting to receive deposit requests and following the requirements and procedures set forth in Section 366, the Debtors ignored, and ask this Court to ignore, the plain language and the express requirements of Section 366 by filing an *ex parte* Motion. Under the Utility Motion, the Debtors request that this Court, without evidence, supporting documentation or input from the Utilities to establish that Debtors': (i) offer to tender security deposits in an amount equal to the Debtors' calculation of the cost of two weeks of utility service based upon a historical average over the past twelve months (the "Deposit"), presumably January 2007 through December 2007 although Debtors do not attach any invoices to the Utility Motion; and (ii) purported ability to timely pay its utilities for all post-petition obligations based upon Debtors' proposed post-petition credit facility, constitute adequate assurance of payment. In addition, Debtors offer the Deposit only to the utilities who request the Deposit in writing and provided that such utility does not already hold a deposit equal to or greater than two (2) weeks of utility services.

[1] The deposit requests from the Utilities that are set forth in this Objection are the deposit amounts that the Utilities' governing regulatory bodies have determined as the appropriate amounts that the Utilities can request from their customers.

[2] In the Utility Motion, Debtors fail to address why performing this statutory obligation imposed an insurmountable

Almost everything requested by the Debtors in the Utility Motion is contrary to the express requirements of Section 366 of the Bankruptcy Code, as amended, and should be rejected by this Court. Simply put, if these and other debtors would just follow the express provisions of Section 366(c), and merely contact their utility providers to ascertain their requests for adequate assurance of future payment before filing an *ex parte* motion with the Court, it is likely that many adequate assurance demands could be resolved without the need for any Court involvement. However, these and other debtors are continually forcing utilities to needlessly incur legal fees and respond to these improper first-day utility motions. Such a practice by these and other debtors not only violates the express provisions of Section 366(c), but also results in the waste of judicial resources, and needless attorneys' fees being incurred by the Debtors' estates and by the utilities.

In addition to completely ignoring the Utilities' rights under Section 366, the proposed two-week deposit is an inadequate amount to secure the Utilities' provision of post-petition accounts to the Debtors. The Utilities bill the accounts in arrears on a monthly basis. Accordingly, there is no rational basis as to why one-half of one-month's service could even begin to cover the payment of the Utilities' post-petition invoices. Moreover, Debtors' methodology fails to take into account steadily rising energy and gas prices due to changes in market conditions well beyond the control of the Utilities and whether any of the twelve months contain off-peak billing compared to other months of the year wherein more utility service is consumed by Debtors. Therefore, the Utilities request that the Court deny the Utility Motion and require the Debtors to comply with the requirements of Section 366.

Finally, the Debtors' purported ability to pay for post-petition utility services in the

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and unduly burdensome task and strain upon the Debtors and the Debtors' resources.

ordinary course of business through access to DIP financing as a complement to Debtors' offer to provide a two-week security deposit is nothing more than a pre-BAPCPA argument cast in a new light. The availability of an administrative expense priority constituting adequate assurance of future payment is now expressly rejected under Section 366(c). In addition, Debtors' refusal to provide any adequate assurance of payment to any utility already holding a pre-petition security deposit equal to or greater than the amount of the Deposit offered by Debtors is unduly prejudicial, is in derogation of Section 366(c)(4) and must not be tolerated by this Court.

In this case the Utilities' deposit requests are based on: (1) the uncertainty as to whether any post-petition financing will be sufficient to pay for all post-petition utility services to the Debtors; (2) the billing exposure created by the Utilities' respective state law tariffs and/or regulations; and, (3) amounts that the applicable state regulatory commissions, which are neutral third-party entities, permit the Utilities to request.

For all of the foregoing reasons and for the reasons that follow, the Utilities request that this Court deny the Utility Motion and through the Final Order on the Utility Motion require that the Debtors provide the Utilities with security deposits according to the amounts set forth herein.

Procedural Facts

1. On January 21, 2008 (the "Petition Date"), Quebecor World (USA) Inc. ("QWUSA") and fifty-two (52) related entities (collectively, the "Debtors") commenced their cases (the "Bankruptcy Cases") in this Court by filing petitions for bankruptcy relief under Chapter 11 of Title 11 of the United States Code, 11 U.S.C §§ 101 *et seq*. (the "Bankruptcy Code"). The Debtors continue to operate their businesses and manage their properties as debtors in possession pursuant to Bankruptcy Code sections 1107(a) and 1108.

2. The Debtors' cases pending before this Court are being jointly administered.

3. On January 20, 2008, the Debtors' corporate parent, Quebecor World, Inc. ("QWI") as well as each one of the aforementioned Debtors also commenced a proceeding before the Superior Court, Commercial Division, for the Judicial District of Montreal (the "Canadian Court") for a plan of compromise or arrangement (the "Canadian Proceeding") under the Canadian Companies' Creditors Arrangement Act ("CCAA"). According to the Debtors, each one of the Debtors was joined in the Canadian Proceeding so that every Debtor could receive the protection of a stay under the CCAA as well as the automatic stay as provided under Section 362 of the Bankruptcy Code.

The Utility Motion

4. On January 22, 2008, one day after the Petition Date, the Debtors filed the Utility Motion.

5. In the Utility Motion, the Debtors allege that they pay their utility companies approximately $10 million per month for services rendered. Utility Motion at ¶ 28.

6. The Debtors further claim that the Utilities are already afforded adequate assurance of future payment because of the Debtors' intention to fully pay all postpetition obligations for utility service in a timely manner. Further, Debtors allege that through their borrowings under their proposed DIP facility, the Debtors will have ample cash available to pay for all of their postpetition utility obligations. Utility Motion at ¶ 31.

7. Through the Utility Motion, however, the Debtors seek to avoid the procedural and substantive requirements of Section 366 of the Bankruptcy Code. Instead of responding to adequate assurance requests of the Debtors' utility companies, the Debtors have instead elected to file the Utility Motion and seek procedures and deposit amounts that fail to provide the Utilities with adequate assurance of payment as required by Section 366 of the Bankruptcy

Code.

8. Specifically, in the Utility Motion, the Debtors propose to provide a security deposit equal to two-weeks of utility service based upon the Debtors' calculated historical average of these costs during the past twelve months, presumably January 1, 2007, through December 31, 2007, although the Debtors do not specify the time period nor attach any invoices reflecting the amounts that Debtors actually paid during this period (the "Adequate Assurance Deposit"). Utility Motion at ¶ 32.

9. Debtors, however, further propose paying the Adequate Assurance Deposit only upon certain conditions. The Adequate Assurance Deposit will be paid only to those utilities who actually request it from the Debtors in writing and only if the requesting utility does not already hold a deposit equal to or greater than two-weeks of utility services and that utility is not currently receiving advance prepayments for utility services from the Debtors. Moreover, the Debtors insist that any utility that makes and accepts such a request for the Adequate Assurance Deposit shall be deemed to have stipulated that the Adequate Assurance Deposit satisfies Debtors' obligations under Section 366 of the Bankruptcy Code and to have waived any future rights to receive additional adequate assurance during the pendency of the Bankruptcy Cases. In the meantime, of course, the Utilities' continue to provide ongoing services to the Debtors. Utility Motion at ¶ 32.

10. The Debtors then propose that Adequate Assurance Procedures be made available to any utility seeking additional assurances of payment from the Debtors for the provision of post-petition utility services (the "Adequate Assurance Procedures"). Utility Motion at ¶ 34.

11. Pursuant to the Adequate Assurance Procedures, any request for additional adequate assurance must be submitted to Debtors and to Debtors counsel and must: (i) be made

in writing; (ii) set forth the location for which utility services are provided; (iii) include a summary of the Debtors' payment history relevant to the affected account(s), including any security deposits; and (iv) set forth why the utility provider believes the proposed adequate assurance is not sufficient adequate assurance of future payment (an "Additional Adequate Assurance Request"). Utility Motion at ¶ 34(b) & (c). As Section 366(c) provides that the absence of prepetition security is statutorily irrelevant, the Utilities are at a loss as to why such items would be required in such a request. Moreover, as Section 366(c) specifically provides that it is the Debtors' burden to provide the Utilities with adequate assurance of payment that is satisfactory to the Utilities, the requirement that the Utilities set forth why the Debtors' worthless and unsubstantiated two-week Adequate Assurance Deposit is not sufficient is contrary to the requirements of Section 366(c).

12. In addition, upon receipt of any Additional Adequate Assurance Request, the Debtors shall have the greater of (i) fourteen (14) days from the receipt of such Additional Adequate Assurance Request or (ii) thirty (30) days from the Petition Date to consider and negotiate with the utility resolution of the Additional Adequate Assurance Request (the "Resolution Period"). Utility Motion at ¶ 34(d).

13. The Debtors, in their discretion, may either resolve the Additional Adequate Assurance Request by mutual agreement and may pay the amount of the Additional Adequate Assurance Request if the Debtors believe that such Additional Adequate Assurance Request is reasonable. Utility Motion at ¶ 34(e).

14. If, however, the Debtors determine that the Additional Adequate Assurance Request is not reasonable and they are unable to resolve the additional amount requested with the utility provider during the Resolution Period, then the Debtors will request a hearing before

the Court to determine the adequacy of assurances of payment pursuant to Section 366(c)(3) of the Bankruptcy Code (the "Determination Hearing"). Utility Motion at ¶ 34(f).

15. Finally, pending resolution of the Additional Adequate Assurance Request at any such Determination Hearing, the utility who submitted the Additional Adequate Assurance Request is restrained from discontinuing, altering or refusing service to the Debtors on account of any objections to the proposed adequate assurance. Utility Motion at ¶ 34(g).

16. Debtors also include in the Utility Motion an "opt out" provision whereupon any utility provider who objects to the Adequate Assurance Procedures must file an objection to the procedures (a "Procedure Objection") so that it is actually received by Debtors' counsel within twenty (20) days of entry of the Interim Order. Utility Motion at ¶ 35(a).

17. Similar to the procedures for submitting an Additional Adequate Assurance Request, the Procedure Objection must: (i) be made in writing; (ii) set forth the location for which utility services are provided; (iii) include a summary of the Debtors' payment history relevant to the affected account(s), including any security deposits; (iv) set forth why the utility provider believes the proposed adequate assurance is not sufficient adequate assurance of future payment; and, (v) set forth why the utility provider believes it should be exempted from the Adequate Assurance Procedures. Utility Motion at ¶ 35(b). As indicated herein, the Procedure Objection addresses only the Adequate Assurance Procedures which pertain to any Additional Adequate Assurance Request. It is therefore unclear whether the Procedure Objection is also intended to apply to those utilities who object to the Adequate Assurance Deposit.

18. The Debtors, in their discretion, may either resolve the Procedure Objection by mutual agreement and may in connection with such agreement pay the utility additional adequate assurance if the Debtors believe that such additional adequate assurance is reasonable. Utility

Motion at ¶ 35(c).

19. If, on the other hand, the Debtors determine that the Procedure Objection is not reasonable and are unable to resolve the matter with the utility, then the Procedure Objection shall be heard at the final hearing. Utility Motion at ¶ 35(d).

20. Finally, all utility providers who do not timely file a Procedure Objection are deemed to have consented to the Adequate Assurance Procedures and are bound by those terms. Their only alternative at that point is to submit an Additional Assurance Request pursuant to the Adequate Assurance Procedures and said utilities shall be "enjoined from ceasing performance" pending any Determination Hearing that may be conducted pursuant to the Adequate Assurance Procedures. Utility Motion at ¶ 35(e).

21. On January 23, 2008, the Court held an *ex parte* hearing on the Utility Motion and thereupon entered the Interim Order that, *inter alia*, set the final hearing on the Utility Motion for February 21, 2008, for the purpose of resolving any Procedure Objections.

Facts Regarding the Debtors Which Support the Utilities' Request For Adequate Assurance of Payment

22. The Debtors collectively operate the second largest commercial printing business in the United States. *Declaration of Jeremy Roberts Pursuant to Local Bankruptcy Rule 1007-2 And In Support Of The Debtors' Petitions And First Day Motions* ¶ 7 (hereinafter "Roberts Declaration at ¶ __").

23. QWI is the corporate parent of the Debtors having been incorporated on February 23, 1989, pursuant to the Canada Business Corporations Act. QWI is a public company with shares listed on the Toronto Stock Exchange and the New York Stock Exchange with its registered and principal office located in the City of Montreal in the Province of Quebec Canada.

QWI, together with the Debtors and all of QWI's debtor and non-debtor subsidiaries and affiliates are referred to in the Roberts Declaration as QW World. Roberts Declaration at ¶ 7.

24. QWI's principal United States subsidiary, Debtor QWUSA, is a wholly-owned subsidiary of Debtor Quebecor Printing Holding Company ("QPHC"). QPHC is a direct and wholly-owned subsidiary of QWI. As the corporate parent of QW World's United States subsidiaries, QWUSA oversees the Debtors' cash management, operations, employee matters and other areas. In addition, QWUSA is a party to certain of QW World's pre-petition financing agreements. Roberts Declaration at ¶ 8.

Debtors' Existing Debt

25. For the year ending December 31, 2006, QW World's operations in the United States made-up approximately 62% of overall revenue. Roberts Declaration at ¶ 10.

26. Prior to the Petition Date, Debtors funded their operational and capital expenditures through revolving credit facilities in the aggregate amount of $750 million based upon an amended and restated credit agreement dated December 15, 2005, among QWI and QWUSA, as borrowers, and sixteen (16) financial institutions including Royal Bank of Canada, also serving as administrative agent for the lenders, to which QPHC intervened as a guarantor (the "Bank Syndicate Agreement"). The credit facility under the Bank Syndicate Agreement matures in January 2009 unless extended for additional one-year periods in accordance with the terms and conditions of the Bank Syndicate Agreement. Roberts Declaration at ¶ 23.

27. The Bank Syndicate Agreement is guaranteed and secured by the "Bank Security" consisting of (i) unlimited guaranties from certain of the Debtors dated on or about October 26, 2007, (ii) shares of certain Debtors owned and pledged by certain other Debtors, (iii) security on all real and personal property of Debtor QW Memphis with some exclusion, and, (iv) security on

all inventory of QWI located in Canada, dated October 26, 2007. Roberts Declaration at ¶ 24.

28. The aggregate amount of debt secured under both the Bank Syndicate Agreement and the Equipment Financing Agreement is $170 million. Roberts Declaration at ¶ 25.

29. As of January 11, 2008, the aggregate amount of indebtedness outstanding under the Bank Syndicate Agreement was approximately $735 million, of which approximately $135 million is secured. Roberts Declaration at ¶ 26.

30. Debtors are also indebted under an Equipment Financing Facility, pursuant to a credit agreement dated January 13, 2006, as amended, among QWI, as borrower, QWUSA, as guarantor, Societe Generale (Canada) as lender and provides for an equipment financing credit facility in the aggregate amount and United States equivalent, as of January 15, 2008, of $202,571,926.00. Roberts Declaration at ¶ 27.

31. The Equipment Financing Agreement is guaranteed and secured on a *pari passu* basis by the same collateral as the lenders under the Bank Syndicate Agreement. Roberts Declaration at ¶ 28.

32. As of January 11, 2008, the aggregate amount of indebtedness outstanding under the Equipment Financing Agreement was approximately $155 million, of which approximately $35 million is secured. Roberts Declaration at ¶ 30.

33. Certain of the Debtors and QWI are obligors under various Note Issuances. According to Jeremy Roberts, the Note Issuances are pre-petition indentures providing for the issuance of senior notes due post-petition. The total aggregate amount outstanding under all of these Note Issuances is approximately $1,451,300,000.00. Roberts Declaration at ¶ 31.

34. QWI and certain of the Debtors are parties to an accounts receivable facility. Under this facility, QWI and certain of the Debtors sell their Canadian and United States

receivables on a revolving basis to Quebecor World Finance, Inc. ("QWF"). QWF, in turn, sells the receivables, pursuant to an amended and restated receivables sale agreement dated as of September 24, 1999, as amended and restated as of December 22, 1999, as further amended (the "RSA"), to various party purchasers and ABN Amro Bank N.V., as agent ("ABN"). Pursuant to the RSA, ABN holds a first priority lien on all of the Debtors' and QWI's accounts receivable purchased by QWF under the Canadian and United States receivables purchase agreements. The Canadian receivables program was rolled into the United States receivables program on or about October 24, 2007, and as of December 31, 2007, the aggregate amount outstanding on account of the Debtors' accounts receivable subject to the RSA was approximately $428 million. Roberts Declaration at ¶ 33.

35. As of the Petition Date, Debtors have outstanding obligations to various Trade Vendors in the aggregate amount of approximately $120 million. Roberts Declaration at ¶ 34.

Events Leading To the Debtors' Chapter 11 Filing

36. In 2005, on a consolidated basis, QWI recorded a $162.6 million loss. QWI's consolidated revenues were $6.34 billion for 2004 decreasing to $6.28 billion in 2005 and decreasing again in 2006 to $6.09 billion. Roberts Declaration at ¶ 41.

37. During the first two quarters of 2007, QWI's net losses from continuing operations totaled approximately $59.2 million and QWI reported an operating loss of $315 million for the third quarter of 2007. Roberts Declaration at ¶ 42.

38. As of September 30, 2007, QWI's consolidated revenues were $4.17 billion, a 6.7% decrease from the same period during 2006. Roberts Declaration at ¶ 43.

39. The decrease in revenues is attributed to lower paper sales as well as reduced volume caused primarily by temporary restructuring dislocations and plant closures and price

pressures. Roberts Declaration at ¶ 43.

40. Prior to the Petition Date, QWI and the Debtors attempted unsuccessfully several measures to improve their balance sheets both by raising capital and selling assets but experienced instead a withdrawn refinancing plan and failed sale of its European operations. In addition, QWI and Debtors have downsized and closed various facilities, completed sales and leaseback transactions, and redeemed or repurchased various senior notes. Roberts Declaration at ¶¶ 45-48.

41. The Debtors' efforts to raise funds proved unsuccessful. Prior to the Petition Date, the lenders under the Bank Syndicate Agreement informed the Debtors that they would not provide any further advances under the bank facility beyond those currently permitted. Roberts Declaration at ¶ 50.

42. With year end covenant defaults looming under the Bank Syndicate Agreement, the Debtors and QWI were able to obtain a waiver from the lenders and from the sponsors of its North American securitization program, subject to the satisfaction of certain conditions and refinancing milestones, including the acquisition of $125 million in new financing by January 15, 2008. The Debtors and QWI, however, were unsuccessful with achieving these conditions and milestones imposed by the bank syndicate lenders. Roberts Declaration at ¶ 50.

43. Debtors are currently facing a severe liquidity crisis. Roberts Declaration at ¶ 51.

44. Debtors have less than $50 million available under the Bank Syndicate Agreement with estimated cash flow projections indicating that Debtors will require $225 million just to satisfy their obligations through January 2008. Roberts Declaration at ¶ 51.

45. QWI currently has aggregate outstanding trade payables of approximately $526.7 million of which $120 million are attributable to the Debtors; in addition to ongoing ordinary

course payments, QWI was also contractually obligated to render debt payments of approximately $19.5 million by January 15, 2008, which remains unpaid, and has only rendered partial payments of the total $10 million due for pension obligations. Roberts Declaration at ¶ 51.

46. QWI and the Debtors are without sufficient liquid resources to pay their obligations that are both currently due or expected to become due in January 2008. Roberts Declaration at ¶ 53.

47. As indicated above, the lenders will not advance any further credit beyond the amount permitted under the Bank Syndicate Agreement, suppliers are demanding cash terms and certain customers are threatening to no longer do business with QWI and the Debtors unless letters of credit or other security are provided. Roberts Declaration at ¶ 53.

48. Accordingly, Debtors filed their bankruptcy petitions with the intention of conducting significant restructurings, including discontinuation of certain business segments and a reduction of the Debtors' debt obligations. Roberts Declaration at ¶ 54.

Post-Petition Financing

49. On January 22, 2008, Debtors filed a motion (the "DIP Motion") to obtain post-petition secured financing on an interim basis with authority to immediately borrow under the DIP facility, on a joint and several basis with QWI, an aggregate principal or face amount of $750,000,000.00. DIP Motion at ¶ 50; Interim Order Approving the DIP Motion at ¶ 4.

50. On January 23, 2008, the Court entered an Interim Order approving the relief requested under the DIP Motion.

51. As part of its factual findings regarding the DIP financing, the Court noted that the DIP financing is vital to the Debtors' ability to preserve and maintain their going concern

value. Interim Order Approving the DIP Motion at ¶ 3(d).

52. If approved on a final basis, the DIP facility would provide QWI and the Debtors, on a joint and several basis, with post-petition secured credit of up to one billion dollars ($1,000,000,000.00). Interim Order Approving the DIP Motion at ¶¶ (a) and (i).

53. Of the initial $750 million advanced under the DIP facility, Debtors represent that approximately $416.8 million will be used to repurchase the existing North American accounts receivable securitization under the RSA. The remaining $333 million will be used for working capital and general corporate purposes and to pay fees incurred in relation to the DIP facility, the Bankruptcy Cases, and the purchase of the Receivables Portfolio. Roberts Declaration at ¶ 147.

54. Other than the foregoing and upon information and belief, to date, Debtors have neither submitted to the Court nor made available to their creditors a Budget specifying their postpetition obligations or their projected disbursements necessary to pay for those expenses.

55. As collateral for the DIP facility, the secured DIP creditors received DIP liens, as more fully described and set forth in paragraph 6 of the Interim Order Approving the DIP Motion. In addition, the Administrative Agent, on behalf of the secured DIP creditors, pursuant to Section 364(c)(1) of the Bankruptcy Code, has received a superpriority claim with priority over any and all administrative expenses other than the carve-out provision for payment of professional fees. Interim Order Approving the DIP Motion at ¶ 7.

56. Under the Interim Order, the Court approved a carve-out provision in the amount of $20,000,000 to secure the payment of unpaid fees and expenses for professionals retained by the Debtors, including counsel for the Debtors, or any Creditors' Committee as well as an additional $250,000 for the payment of fees and expenses of a chapter 7 trustee upon the conversion of the Bankruptcy Cases. Interim Order Approving the DIP Motion at ¶ 16.

57. The Court has set a final hearing on the DIP Motion for on March 6, 2008.

Facts Concerning the Utilities

58. Each of the Utilities provided the Debtors with prepetition utility service and continues to provide the Debtors with uninterrupted post-petition utility service.

59. Under the Utilities' billing cycles, the Debtors receive approximately one-month of utility service before the Utility issues a bill for such service. Once a bill is issued, the Debtors have approximately fifteen (15) to thirty (30) days to pay the applicable bill. If the Debtors fail to timely pay the bill, a past due notice is issued and a late fee is subsequently imposed on the account. If the Debtors fail to pay the bill after the issuance of the past due notice, the Utilities issue a notice that informs the Debtors that they must cure the arrearage within a certain period of time or their services will be disconnected. Accordingly, under the Utilities' billing cycles, the Debtors could receive two (2) to three (3) months of unpaid service before their service could be terminated for a post-petition payment default.

60. Subject to a reservation of the Utilities' rights to supplement their post-petition deposit requests if additional accounts belonging to the Debtors are subsequently identified, the Utilities' post-petition deposit requests are currently as follows:

Utility	**Estimated Prepetiton Debt**	**Number of Accounts**	**Deposit Request**
ConEd	($363.43)	1	$9,675.00 (2 months)
DEO	n/a	1	$10,345.00 (2 months)
DEC	n/a	1	$5,580.00 (2 months)
NYSEG	$71,847.70	2	$182,575.00 (2 months)
ComEd	$82,408.70	9	$334,714.00 (4 months)
PECO	$46,030.00	4	$39,014.00 (2 months)
PNG	n/a	3	$32,750.00 (2 months)
DVP	$182,200	2	$332,009.00 (2 months)

61. DVP maintained a letter of credit on the Debtors' prepetition

accounts in the amount of $331,938.00.

62. NYSEG maintained security deposits on the Debtors' prepetition accounts in the total amount of $85,000.

63. The Debtors have a third party supplier, Sempra, that provides the electric and gas commodity transported by ComEd. In the event that the Debtors require gas and/or electric commodity from ComEd, the requested deposit would increase.

Discussion

A. THE DEBTORS' PROPOSED ADEQUATE ASSURANCE OF PAYMENT PROCEDURES VIOLATE THE EXPRESS PROVISIONS OF SECTION 366 AND SHOULD BE REJECTED BY THE COURT.

Sections 366(b) and (c) of the Bankruptcy Code, in pertinent part, provide:

(b) Such utility may alter, refuse, or discontinue service if neither the trustee nor the Debtors, within 20 days after the date of the order for relief, furnishes adequate assurance of payment, in the form of a deposit or other security, for service after such date.

(c)(1)(A) For purposes of this subsection, the term "assurance of payment" means

(i) a cash deposit;
(ii) a letter of credit;
(iii) a certificate of deposit;
(iv) a surety bond;
(v) a prepayment of utility consumption; or
(vi) another form of security that is mutually agreed upon between the utility and the Debtors or the trustee.

(B) For purposes of this subsection an administrative expense priority shall not constitute an assurance of payment,

(2) Subject to paragraphs (3) and (4), with respect to a case filed under chapter 11, a utility referred to in subsection (a) may alter, refuse, or discontinue utility service, if during the 30-day period beginning on the date of the filing of the petition, the utility does not receive from the Debtors or the trustee adequate assurance of payment for utility service that is satisfactory to the utility;

(3)(A) On request of a party in interest and after notice and a hearing, the court may order modification of the amount of an assurance of payment under paragraph (2).

(B) In making a determination under this paragraph whether an assurance of payment is adequate, the court may not consider

(i) the absence of security before the date of the filing of the petition;

(ii) the payment by the Debtors of charges for utility service in a timely manner before the date of the filing of the petition; or

(iii) the availability of an administrative expense priority.

(4) Notwithstanding any other provision of law, with respect to a case subject to this subsection, a utility may recover or set off against a security deposit provided to the utility by the Debtors before the date of the filing of the petition without notice or order of the court.

11 U.S.C. §366.

1. THE COURT SHOULD DENY DEBTORS' MOTION BECAUSE THE DEBTORS FAILED TO: (1) FOLLOW THE PROVISIONS OF SECTION 366(c)(3); AND (2) PROVIDE ANY BASIS FOR MODIFYING THE UTILITIES' DEPOSIT REQUESTS.

The procedure under Section 366(c) is for the debtor to provide a utility with adequate assurance of payment that is satisfactory to the utility within thirty (30) days of the petition date. If the debtor believes that the adequate assurance of payment requested by the utility needs to be modified, then the debtor can file a motion and have the court determine whether the amount of the utility's request should be modified. The Utility Motion, which seeks to establish adequate assurance of payment, not modify existing requests, is not in compliance with Section 366(c)(3). Accordingly, this Court should deny the Utility Motion and require the Debtors to comply with the requirements of Section 366(c)(3) of the Bankruptcy Code

In addition to failing to follow the requirements of Section 366, the Utility Motion, also fails to address why this Court should modify the Utilities' requests for adequate assurance of payment deposits set forth in paragraph 60 above (the "Requests").

Under Section 366(c), the Debtors have the burden of proof as to whether the Utilities' adequate assurance of payment requests should be modified. *See In re Stagecoach Enterprises, Inc.***,** 1 B.R. 732, 734 (Bankr. M.D.Fla. 1979) (holding that the debtor, as the petitioning party at a Section 366 hearing, bears the burden of proof). Debtors, however, offer the Court no evidence to explain how or why the amount of the Requests should be modified. Indeed, the Debtors never even address the matter in the Utility Motion because Debtors failed to: (1) contact the Utilities concerning their Requests; and (2) make any attempt to determine whether the Requests for adequate assurance needed to be modified. Accordingly, the Court should deny the relief requested by Debtors in the Utility Motion and require the Debtors to comply with the requirements of Section 366(c) with respect to the Utilities.

Through the Utility Motion, Debtors attempt to avoid their obligations and the burden of proof under Section 366(c). The fact that the Debtors have offered to pay the Utilities a two-week deposit is simply not relevant. Moreover, the Debtors' reliance upon their supposed ability to pay future utility services in the ordinary course of business, which as evidenced by this Objection is dubious at best, is nothing more than the promise of an allowed administrative expense in violation of Section 366(c)(1)(B). Accordingly, because the Debtors failed to comply with the requirements of Section 366(c)(3) by filing a modification motion and fail to set forth any reason why the Requests should be modified in the Utility Motion, the Utility Motion should be denied, and the Debtors should be required to immediately pay the Utilities their Requests.

2. THE COURT SHOULD REJECT THE PROCEDURES THAT ATTEMPT TO ADD TIME CONSUMING AND BURDENSOME REQUIREMENTS THAT ARE NOT FOUND IN SECTION 366.

In addition to Debtors' failure under the Utility Motion to abide by the requirements of Section 366(c), the Debtors also seek entry of an order from the Court permitting procedures

designed to make the adequate assurance of payment process more time consuming and burdensome to the Utilities while Debtors simultaneously continue to enjoy uninterrupted, continuous utility services from the Utilities. For example, even though Section 366 now defines assurance of payment, it contains no provisions requiring utilities to make demands for adequate assurance within certain time periods nor does it establish requirements for the content of any such request.

Despite the foregoing, Debtors require their utilities to first request the two-week deposit before Debtors will pay it, but even with a request, Debtors will only pay the deposit to those utilities who satisfy Debtors' criteria: (1) the requesting utility does not already hold a deposit equal to or greater than two-weeks of utility services (This would exclude NYSEG and DVP); and, (2) the requesting utility is not currently receiving advance prepayments for utility services from the Debtors. In addition, Debtors require that any request for additional adequate assurance must be submitted to Debtors and to Debtors' counsel and must: (i) be made in writing; (ii) set forth the location for which utility services are provided; (iii) include a summary of the Debtors' payment history relevant to the affected account(s), including any security deposits; and (iv) set forth why the utility provider believes the proposed adequate assurance is not sufficient adequate assurance of future payment. Further, any utility who objects to these Adequate Assurance Procedures must file a Procedure Objection so that it is actually received by Debtors' counsel within twenty (20) days of entry of the Interim Order (the "Procedure Objection Deadline"). Similar to the procedures for submitting an Additional Adequate Assurance Request, the Procedure Objection must: (i) be made in writing; (ii) set forth the location for which utility services are provided; (iii) include a summary of the Debtors' payment history relevant to the affected account(s), including any security deposits; (iv) set forth why the utility provider

believes the proposed adequate assurance is not sufficient adequate assurance of future payment;

and, (v) set forth why the utility provider believes it should be exempted from the Adequate Assurance Procedures.

Debtors' proposal to only provide the Adequate Assurance Deposit to those utilities who satisfy Debtors' arbitrary criteria of not already holding a deposit equal to or greater than two-weeks of utility services and who do not currently receive advance prepayments for utility services from the Debtors simply has no statutory basis under Section 366 and must not be tolerated by this Court. Indeed, under Section 366(c)(4), a utility is permitted without notice or order of the court to liquidate pre-petition deposits for purposes of set off against unpaid pre-petition debts. Thus, Debtors' attempt to prejudice a utility, such as DVP and NYSEG, by refusing to provide said utility with an adequate assurance deposit because of a deposit already held by the utility is preposterous.

Moreover, information regarding security deposits or other security held by a utility, which the Utilities are being required to provide to the Debtors as procedures imposed under the Interim Order, are statutorily irrelevant pursuant to Section 366(c)(3)(B). Section 366(c)(3)(B) expressly provides:

> (B) In making a determination under this paragraph whether an assurance of payment is adequate, the court may not consider
>
> (i) the absence of security before the date of the filing of the petition;
>
> (ii) the payment by the debtor of charges for utility service in a timely manner before the date of the filing of the petition; or
>
> (iii) the availability of an administrative expense priority.

Furthermore, the Debtors presumably have access to the same account information as the Utilities. The Debtors are merely seeking to impose these requirements and procedures upon the

Utilities to dissuade the Utilities from making requests for adequate assurance of payment pursuant to Section 366 of the Bankruptcy Code. Simply put, such burdensome procedures are not contained in Section 366 and should not be granted by this Court. Additionally, Debtors' proposed procedure, which attempts to shift and place the burden upon the Utilities to explain to the Debtors why the Utilities believe that the Debtors' Adequate Assurance Deposit is not sufficient adequate assurance of future payment defies every conceivable interpretation of Section 366(c)(2).

Rather than attempting to contact the Utilities to determine their requests for adequate assurance, Debtors elected to present this Court with an *ex parte* motion providing for adequate assurance in a form and in an amount that is satisfactory to the Debtors – a position clearly in violation of the express provisions of Section 366(c)(2). The Utilities recognize that on the one hand it may not have been possible for the Debtors to consult with all of their utilities listed on Exhibit B to the Utility Motion within the thirty (30) day period set forth in Section 366(c). If that is in fact the case, then the Debtors should have proceeded with a Motion stating that they were unable to comply with the requirements of Section 366(c) and ask the Court for relief in that regard and then provide their utilities with an opportunity to address and/or to oppose the foregoing relief. In this case, however, the Utilities are not being provided with sufficient adequate assurance of payment under Debtors' Utility Motion and/or the Interim Order, much less payment of adequate assurance that is satisfactory to the Utilities.

3. THE COURT SHOULD ORDER THE DEBTORS TO PROVIDE THE ADEQUATE ASSURANCE OF PAYMENT REQUESTED BY THE UTILITIES PURSUANT TO SECTION 366 OF THE BANKRUPTCY CODE.

Section 366(c) was amended to overturn decisions such as *Virginia Electric and Power*

Company v. Caldor, Inc., 117 F.3d 646 (2d Cir. 1997), that held that an administrative expense, without more, could constitute adequate assurance of payment in certain cases. Section 366(c)(1)(A) specifically defines the forms that assurance of payment may take as:

> (i) a cash deposit;
> (ii) a letter of credit;
> (iii) a certificate of deposit;
> (iv) a surety bond;
> (v) a prepayment of utility consumption; or
> (vi) another form of security that is mutually agreed upon between the utility and the debtor or the trustee.

A determination of adequate assurance is within the court's discretion, and is made on a case-by-case basis, subject to the new requirements of Section 366(c). *See In re Utica Floor Maintenance, Inc.*, 25 B.R. 1010, 1016 (Bankr. N.D.N.Y. 1982); *In re Cunha*, 1 B.R. 330, 332-33 (Bankr. E.D. Va. 1979). Section 366 of the Bankruptcy Code was enacted to balance a debtor's need for utility services from a provider that holds a monopoly on such services, with the need of the utility to ensure for itself and its rate payers that it receives payment for providing these essential services. *See In re Hanratty*, 907 F.2d 1418, 1424 (3d Cir. 1990). The deposit or other security "should bear a reasonable relationship to expected or anticipated utility consumption by a debtor." *In re Coastal Dry Dock & Repair Corp.*, 62 B.R. 879, 883 (Bankr. E.D.N.Y. 1986). In making such a determination, it is appropriate for the Court to consider "the length of time necessary for the utility to effect termination once one billing cycle is missed." *In re Begley*, 760 F.2d 46, 49 (3d Cir. 1985). Based on the Debtors' anticipated utility consumption, the minimum period of time the Debtors could receive service from the Utilities before termination of service for non-payment of bills is approximately two (2) months. Accordingly, the two-month deposits requested by the Utilities are reasonable. *See In re Stagecoach*, 1 B.R. at 735-36 (holding that a two month deposit is appropriate where the debtor

could receive sixty (60) days of service before termination of services because of the utilities' billing cycle.); *see also In the Matter of Robmac, Inc.*, 8 B.R. 1, 3-4 (Bankr. N.D. Ga. 1979).

As set forth above, the Requests are based on: (1) the Utilities' billing exposure created by respective state law tariffs and/or regulations (the "Tariffs"); and, (2) amounts that applicable public service commissions, which are neutral third-party entities, permit the Utilities to request from its customers. Although the Utilities recognize that this Court is not bound by the Tariffs, the Tariffs are extremely relevant information of a determination made by an independent entity on the appropriate amount of security that should be paid to the Utilities.

In contrast, the Debtors do not provide an objective much less an evidentiary basis for their proposed adequate assurance in the form of two-weeks cash deposits. Furthermore, the Debtors assert that the Utilities are already afforded adequate assurance of future payment because of the Debtors' intention to fully pay all postpetition obligations for utility service in a timely manner. Debtors allege that through their borrowings under their proposed DIP facility the Debtors will have ample cash available to pay for all of their postpetition utility obligations. Utility Motion at ¶ 31. The Debtors' reliance, however, upon their purported ability to pay for future utility service under the DIP facility is merely an offer to pay an administrative expense cast in a new light and for that reason is statutorily irrelevant under Section 366. Section 366(c)(3)(B)(iii) specifically provides that in making a determination under Section 366, a court may not consider the availability of an administrative expense priority. Furthermore, a restatement of the provisions under Section 503 of the Bankruptcy Code is not a form of adequate assurance being "provided" by the Debtors to their Utilities. Section 503 stands on its own and is already available to the Utilities regardless of Debtors' attempt to offer an administrative expense priority as adequate assurance of future payment. Moveover, as

indicated above, any administrative expense claim that the Utilities may have against the Debtors is subject to the superpriority claim of the secured DIP creditors and the carve-out provided to the Debtors' professionals.

Debtors' liquidity problems and financing crisis are severe. Recognizing that the Debtors financial situation is dire, Debtors counsel has ensured that the payment of Debtors' counsel and other professionals post-petition fees are secured through a $20,000,000 carve-out in the Debtors' proposed DIP financing. The foregoing security is in addition to the $939,053.09 retainer held by Debtors' counsel as of the Petition Date and the Debtors' payment of pre-petition attorneys' fees totaling nearly $2.5 million. Debtors' Application to Employ and Retain Arnold & Porter, LLC, As Attorneys For The Debtors at ¶ 37. If insiders with information on the Debtors' finances, such as Debtors' counsel, believe such security is necessary to secure the payment of their fees, certainly the Utilities should receive post-petition security to secure the payment of their post-petition invoices.

As declared by Jeremy Roberts and as further evidenced by the DIP financing arrangement, Debtors' debt service is extensive while at the same time Debtors' quarterly losses have steadily increased for the past three or four years. Mr. Roberts indicated that Debtors, pre-petition, had no source of operating capital other than approximately $50 million available under their pre-petition lending facility with estimated cash flow projections indicating that Debtors will require $225 million just to satisfy their obligations through January 2008. Further, just before the Petition Date, under their pre-petition lending facility, the Debtors were indebted in the aggregate amount of $735 million. As evidenced by the Interim Order Approving the DIP Motion, Debtors' borrowings and further debts continue to deepen. Debtors are to receive immediately availability for post-petition secured funding in the principal amount of $750

million with ultimate DIP financing up to $1 billion pending the Court's final approval of the DIP Motion. Strikingly, however, Debtors are incurring this enormous debt without providing their creditors with any budget to account for the disbursements that will be made by way of their post-petition borrowings. Finally, Jeremy Roberts remarked about the Debtors' failed attempts prepetition to sell their European assets and that as part of the Debtors' restructuring in these Bankruptcy Cases, the Debtors intended to sell assets and downsize plants or close them altogether. The Court made as part of its findings in approving the DIP Motion that the Debtors required the DIP financing to maintain their value as a going concern. Given the high price that would most likely have to be paid to purchase the Debtors' assets in a bankruptcy sale, given the superpriority claim of the secured DIP creditors and the Debtors' pre-petition maximized debt-load, there is no guarantee and great cause for concern by the Utilities that any post-petition sale of the Debtors' assets will not provide proceeds sufficient to pay for the Debtors' other administrative expenses.

Accordingly, not only have the Debtors failed to satisfy their statutory burden under Section 366 as to why the Requests should be modified, but Debtors have also failed to demonstrate why their alternative adequate assurance of payment proposal provided under the Utility Motion should be accepted by the Utilities and approved by the Court, especially if as Debtors assert, their average monthly utility costs are approximately $10 million. Hence, for these reasons and for all of the foregoing reasons, the Court should deny the Utility Motion and require the Debtors to immediately pay the Utilities the adequate assurance deposit amounts requested herein.

WHEREFORE, and for the foregoing reasons, the Utilities respectfully request that this Court enter an order:

(I) Denying the Utility Motion;

(II) Awarding the Utilities post-petition adequate assurance of payment pursuant to Section 366 in an amount equal to the Requests; and

(III) Providing such other and further relief as the Court deems just and appropriate.

Dated: Uniondale, New York
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