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UNITED STATES BANKRUPTCY COURT

CENTRAL DISTRICT OF CALIFORNIA

LOS ANGELES DIVISION

IN RE: COLOREP, INC., a California corporation, *et al.*, Debtors.	Case No. 2:13-bk-27689-WB Chapter 11 (Jointly Administered) **REPLY OF COLUMBIA GAS OF VIRGINIA, INC. TO DEBTORS' OMNIBUS RESPONSE [DOCKET NO. 147] TO OBJECTIONS FILED BY VIRGINIA ELECTRIC AND POWER COMPANY d/b/a DOMINION POWER [DOCKET NO. 72] AND COLUMBIA GAS OF VIRGINIA, INC. [DOCKET NO. 88] TO AMOUNT AND SCOPE OF ADEQUATE ASSURANCE THAT CERTAIN UTILITIES ARE ENTITLED TO UNDER BANKRUPTCY CODE SECTION 366** **Hearing Date** Date: August 28, 2013 Time: 10:00 a.m. Location: Courtroom 1475 255 East Temple Street Los Angeles, CA 90012

Columbia Gas of Virginia, Inc. ("Columbia"), by its undersigned counsel, hereby replies (this "Reply") to the Debtors' omnibus response [Doc. No. 147] (the "Response") to the objections of Virginia Electric and Power Company d/b/a Dominion Virginia Power [Doc. No. 72] and Columbia [Doc. No. 88] (the "Columbia Objection") to the Debtors' *Emergency Motion for Order: (I) Deeming Utilities Adequately Assured of Future Performance; and (II) Establishing Procedures for Determining Requests for Additional Assurance Pursuant to Bankruptcy Code Section 366; Memorandum of Points and Authorities; Declaration in Support Thereof* [Doc. No. 8] (the "Utilities Motion") and the corresponding Order [Doc. No. 54] (the "Utilities Order"), and in support hereof, respectfully states as follows:[1]

I.

INTRODUCTION

Columbia raised two issues in response to the relief requested in the Utilities Motion and granted in the Utilities Order: (i) whether the Debtors' proposed assurance of payment was "adequate" under section 366 of the Bankruptcy Code; and (ii) whether the injunction requested by the Debtors and imposed by the Utilities Order prohibiting Columbia from altering, refusing, discontinuing service to, or discriminating against the Debtors under *any* circumstances is authorized under the Bankruptcy Code. Through good faith negotiations, the first issue was resolved by agreement between the Debtors and Columbia. Specifically, the Debtors agreed to deliver to Columbia a cash deposit in the amount of $12,000.00 within five (5) days of any order on the Columbia Objection, which deposit shall constitute adequate assurance of payment under section 366 of the Bankruptcy Code. See Resp. at 6. Columbia respectfully requests that the Court approve this agreed-upon modification to the form and amount of assurance of payment to Columbia as part of any order on the Columbia Objection. The Debtors and Columbia were unable to resolve the second issue through negotiations, and accordingly, the remainder of this Reply focuses solely on the impropriety of the Debtors' desired injunction.

[1] Capitalized terms used but not defined in this Reply have the meanings given in the Columbia Objection.

II.

ARGUMENT

The Utilities Order improperly strips Columbia of its right to discontinue or refuse post-petition utility service to the Debtors based on any valid reason under applicable law other than commencement of this bankruptcy case and non-payment of pre-petition debts. Specifically, the Utilities Motion requested an order providing, and the Utilities Order provides, that "[t]he Debtors' utility service providers . . . are prohibited from altering, refusing, discontinuing service to, or discriminating against the Debtors." Utilities Order at ¶ 2. By its plain terms, the Utilities Order prohibits the Debtors' utility providers from discontinuing or refusing service under any circumstances. As set forth more fully below, this broad injunction contravenes Columbia's rights under section 366 of the Bankruptcy Code as interpreted by every court that has examined the issue and is not authorized by either sections 362 or 105 of the Bankruptcy Code. Accordingly, Columbia respectfully requests that the Court modify the Utilities Order to confirm Columbia's right to discontinue or refuse service to the Debtors for any valid reason under applicable law other than commencement of this bankruptcy case and non-payment of pre-petition debts.[2]

A. SECTION 366 OF THE BANKRUPTCY CODE PERMITS COLUMBIA TO DISCONTINUE OR REFUSE SERVICE TO THE DEBTORS FOR ANY VALID REASON UNDER APPLICABLE LAW OTHER THAN COMMENCEMENT OF THIS BANKRUPTCY CASE AND NON-PAYMENT OF PRE-PETITION DEBTS.

Section 366(a) of the Bankruptcy Code protects debtors from the discontinuance of utility service or other discrimination based upon commencement of a bankruptcy case and non-payment of pre-petition debts. This section provides in relevant part:

[2] The Debtors summarily assert in a footnote that the Columbia Objection was procedurally improper with respect to Columbia's challenge to the injunction, because the Utilities Order provided procedures only for objecting to the Court's "determination that the Debtors have provided adequate assurance." See Resp. at 5-6, n. 11. In light of the unique procedural posture of this contested matter, specifically, a hearing on the Utilities Motion being held upon four days' notice to Columbia without a reasonable opportunity to object and the entry of an order containing procedures for objecting to the relief granted therein within fourteen (14) days, Columbia believed a single responsive pleading was appropriate. To the extent the Court disagrees, Columbia respectfully requests that its request for modification of the injunction be deemed to be a motion for reconsideration under Fed. R. Civ. P. 60(b)(6), as made applicable to these proceedings by Fed. R. Bankr. P. 9024.

> a utility may not alter, refuse, or discontinue service to, or discriminate against, the trustee or the debtor solely on the basis of the commencement of a case under this title or that a debt owed by the debtor to such utility for service rendered before the order for relief was not paid when due.

11 U.S.C. § 366(a). Section 366(c) provides an exception to the general rule set forth in subsection (a) in chapter 11 cases. This subsection permits a utility to discontinue or refuse service solely because of the commencement of a bankruptcy case or the non-payment of pre-petition debts if the debtor fails to provide assurance of payment satisfactory to the utility. 11 U.S.C. § 366(c). These provisions are designed to "clarify the bankruptcy court's power to prevent a utility from using its termination power to enforce payment of pre-petition debts, as long as adequate security for payment of future bills is provided to the utility." Begley v. Philadelphia Elec. Co., 760 F.2d 46, 48 (3d Cir. 1985) (citing 2 COLLIER ON BANKRUPTCY at ¶¶ 366.01-.03 (15th Ed. 1984)).

Section 366 is silent as to a utility's right to discontinue or refuse service where adequate assurance is posted but applicable law permits the utility to discontinue or refuse service for a valid reason other than commencement of a bankruptcy case and non-payment of pre-petition debts (e.g., non-payment for post-petition services). On this point, the Debtors and Columbia agree. The Debtors and Columbia disagree, however, with respect to how Congress's silence should be interpreted.

Every court that has examined this issue has unanimously held that section 366 of the Bankruptcy Code implicitly allows utilities to discontinue or refuse service for any valid reason under applicable law other than commencement of a bankruptcy case and non-payment of pre-petition debts. See Robinson v. Mich. Consol. Gas Co., 918 F.2d 579, 588 (6th Cir. 1990) (it is "well-established" that a utility may terminate service upon debtor's failure to pay for post-petition services); Begley, 760 F.2d at 49; Jones v. Boston Gas Co. (In re Jones), 369 B.R. 745, 752 (1st Cir. B.A.P. 2007) (utility does not run afoul of automatic stay by terminating service based on debtor's failure to pay post-petition service); Weisel v. Dominion Peoples Gas Co. (In re Weisel), 428 B.R. 185, 188 (W.D. Pa. 2010) (a utility is permitted to unilaterally terminate gas service based on postpetition unpaid bills, without requirement of seeking leave of court or relief from stay); MFS

Telecom, Inc. v. Motorola Inc. (In re Conxus Commc'ns., Inc.), 262 B.R. 893, 899 (D. Del. 2001) (concluding that bankruptcy court erred in enjoining, under § 105, termination of utility service based upon post-petition default); Memphis Light, Gas & Water Div. v. Farley, 135 B.R. 292, 294 (W.D. Tenn. 1991); Johnson v. Philadelphia Elec. Co., 80 B.R. 30, 31 (E.D. Pa. 1987) (concluding that § 366(b) specifically allows a utility to terminate service for failure to pay post-petition services); Morris v. Detroit Edison (In re Morris), 66 B.R. 28, 29 (E.D. Mich. 1986); In re Spencer, 218 B.R. 290, 294 n. 5 (Bankr. W.D.N.Y. 1998) (utility may commence termination proceedings pursuant to state law if there is a post-petition delinquency); In re Webb, 38 B.R. 541, 544 (Bankr. E.D. Pa. 1984) ("a utility has the discretion to refuse service to any debtor for any reason which would validly constitute a ground for refusal if that debtor were not in bankruptcy, with the single exception of nonpayment for past services."). Based upon this significant body of case law:

> It is *well-established* that § 366 permits a utility to terminate service to a debtor or trustee who has posted adequate assurance but fails to make post-petition payments on the utility service, and may do so without seeking relief from the automatic stay as long as the utility follows its state law termination procedures.

In re Weisel, 428 B.R. at 188 (emphasis added); accord In re Jones, 369 B.R. at 749 ("courts have *routinely* allowed utilities to terminate service for post-petition delinquencies without obtaining relief from stay.") (emphasis added); see also 3 COLLIER ON BANKRUPTCY at ¶ 366.03[2] (16th Ed. 2013) ("The provision of adequate assurance does not prevent a utility from terminating service to the debtor or the estate if postpetition payments for utility services are not made."). The injunction requested by the Debtors and incorporated into the Utilities Order contravenes Columbia's rights under section 366 of the Bankruptcy Code and this "well-established" principle.

The Debtors dismiss the aforementioned authorities as a "small body of case law" and criticize each of these courts, which are spread across multiple jurisdictions, for "blindly" following the Third Circuit in Begley and failing to go into any "real analysis" of section 366 of the Bankruptcy Code. See Resp. at 18-19. The Debtors' criticism is misplaced, particularly where the Debtors did not, and cannot, cite a single case relating to termination of post-petition utility service to support their view. The Debtors' primary criticism of Begley and its progeny is that they fail to

reconcile the implied permission to discontinue or refuse service under section 366 with the inability of a non-debtor counterparty to unilaterally terminate an executory contract under section 362. For the reasons set forth below, these concepts can be reconciled, and they are not mutually exclusive.

B. SECTION 362 OF THE BANKRUPTCY CODE DOES NOT PROVIDE A STATUTORY BASIS TO ENJOIN COLUMBIA FROM DISCONTINUING POST-PETITION UTILITY SERVICE PURSUANT TO APPLICABLE LAW.

The Ninth Circuit has held repeatedly that section 362(a)(3) of the Bankruptcy Code, which stays "any act to obtain possession of property of the estate," prohibits non-debtor counterparties from unilaterally terminating an executory contract without seeking relief from the automatic stay. Carroll v. Tri-Growth Centre City, Ltd., 903 F.2d 1266, 1271 (9th Cir. 1990); Computer Commc'ns, Inc. v. Codex Corp. (In re Computer Commc'ns, Inc.), 824 F.2d 725, 728 (9th Cir. 1987); Minoco Group of Cos., Ltd. v. First State Underwriters Agency of New England Reinsurance Corp. (In re Minoco Group of Cos., Ltd.), 799 F.2d 517, 519 (9th Cir. 1986). These cases are predicated on the principle that, under section 541 of the Bankruptcy Code, a debtor's contracts become property of the estate upon the filing of a petition. See In re Computer Commc'ns, Inc., 824 F.2d at 729-30. The Debtors rely on section 362(a)(3) and this body of case law to support their desired injunction. However, the propriety of an injunction prohibiting the termination or cancellation of Columbia's *agreement* with the Debtors is not at issue here. Rather, the question is whether section 362(a)(3) of the Bankruptcy Code provides statutory authority for an injunction prohibiting Columbia from discontinuing or refusing *service* to the Debtors for any valid reason under applicable law other than commencement of this bankruptcy case and non-payment of prepetition debts. Neither the text of section 362(a)(3) nor the cases cited by the Debtors support such a broad injunction.

The injunction requested by the Debtors and incorporated in the Utilities Order does not merely prohibit the termination of an executory contract; it goes further by prohibiting Columbia from discontinuing or refusing service for any reason. This is an important distinction recognized in the Ninth Circuit. In In re Bobbitt, 174 B.R. 548 (Bankr. N.D. Cal. 1993), the debtors relied upon In

re Computer Communications to argue that a counterparty's termination of services under the parties' contract constituted an exercise of control over property of the estate and, consequently, a violation of the automatic stay. The Court explained that the holding of Computer Communications is clear: "*unilateral termination* of a contract by a creditor requires relief from the automatic stay." In re Bobbitt, 174 B.R. at 554 (emphasis in original). In Bobbitt, the counterparty did not terminate the contract; rather, the counterparty merely breached the contract by refusing to provide certain services. The Court was unable to find, nor could the debtors cite, any support for the proposition that "a creditor's mere breach of a contract requires relief from the automatic stay." Id. Ultimately, the Court held that the counterparty did not violate the automatic stay because the mere cancellation of services did not constitute a termination of the contract. Id.

In a more recent decision distinguishing between termination and breach of a contract, the Bankruptcy Appellate Panel of the Ninth Circuit remarked that "Congress clearly knew how to identify acts requiring relief from the stay, but did not include a provision staying . . . breaches of a contract." Benz v. DTRIC Ins. Co. (In re Benz), 368 B.R. 861, 865 (9th Cir. B.A.P. 2007). The Court continued by noting that "it stretches the plain meaning of section 362 to require a contracting party to obtain relief from the stay before refusing to perform under a contract." In re Benz, 368 B.R. at 865; see also In re Lucre, 339 B.R. 648, 660 (Bankr. W.D. Mich. 2006) ("it is illogical to contend that the non-debtor party's justifiable refusal to perform under an executory contract post-petition is somehow a violation of the automatic stay.").

Stretching the plain meaning of section 362 is exactly what the Debtors are requesting the Court do here. The Debtors want the Court to prohibit by injunction what section 362 does not stay automatically—the refusal of Columbia to perform under a services agreement where applicable non-bankruptcy law excuses its non-performance. See Horton v. Horton, 254 Va. 111, 204 (Va. 1997) (recognizing under Virginia law that material breach by one party to a contract excuses the other party to the contract from performing his contractual obligations). Contrary to the Debtors' assertions, neither section 362(a)(3) nor Computer Communications and its progeny support an injunction prohibiting a refusal to perform under an services agreement with a debtor. Such an

injunction is tantamount to involuntary servitude. Like the Court in In re Bobbitt, this Court should decline to expand the holding of Computer Communications to enjoin justifiable refusals to perform under a services agreement.

C. SECTION 105 OF THE BANKRUPTCY CODE DOES NOT PROVIDE A STATUTORY BASIS TO ENJOIN COLUMBIA FROM DISCONTINUING POST-PETITION UTILITY SERVICE PURSUANT TO APPLICABLE LAW.

Section 105(a) of the Bankruptcy Code authorizes bankruptcy courts to "issue any order, process, or judgment that is necessary or appropriate to carry out the provisions" of the Bankruptcy Code. 11 U.S.C. § 105(a). This section "merely authorizes the bankruptcy or district courts to issue orders required to implement the substantive provisions of the Code." In re Packers' Cold Storage, Inc., 64 B.R. 265, 267 (Bankr. C.D. Cal. 1986). It "does not create substantive rights otherwise unavailable, or grant the court an unrestricted license to do equity." Id. In other words, a bankruptcy court may exercise its powers under section 105(a) "only as a means to fulfill some specific Code provision." In re Saxman, 325 F.3d 1168, 1174-75 (9th Cir. 2003) (citing Norwest Bank Worthington v. Ahlers, 485 U.S. 197, 206, (1988) ("[W]hatever equitable powers remain in the bankruptcy court must and can only be exercised within the confines of the Bankruptcy Code.")).

Section 105(a) of the Bankruptcy Code does not provide a statutory basis to enjoin Columbia from discontinuing service because such injunction would contravene section 366 of the Bankruptcy Code and create substantive rights that are otherwise unavailable to the Debtors under the Bankruptcy Code. See MFS Telecom, Inc. v. Motorola Inc. (In re Conxus Commc'ns, Inc.), 262 B.R. 893, 899 (D. Del. 2001). The question presented in In re Conxus Commc'ns was whether the bankruptcy court erred in enjoining a utility under section 105 of the Bankruptcy Code from exercising its rights to terminate telecommunications services to the debtors. 262 B.R. at 899. Acknowledging the utility's right to terminate service to the debtors after a post-petition payment default under section 366, the Court found that it was error for the bankruptcy court to utilize section 105 to restrict the utility's rights while expanding the debtor's rights beyond the protection provided to them under section 366. Id. Not only is Columbia's right to refuse service supported by section

366, but an injunction prohibiting such right is unsupported by section 362. Consequently, the Debtors cannot argue legitimately that their desired injunction is a means to fulfill some specific provision of the Bankruptcy Code.

The Debtors argue that the injunction is necessary to "protect the integrity of the Debtors' estates" because of the substantial harm that will result from a termination of utility services at the Harrisonburg facility. This argument has been rejected by a number of courts. See, e.g., In re Conxus Commc'ns, 262 B.R. at 899 ("exigent circumstances" cited by debtors in support of an injunction did not justify a departure from the Bankruptcy Code); In re Lucre, 339 B.R. at 661. As an example, the Court in In re Lucre examined similar equitable arguments and rejected them, stating:

> Bankruptcy judges and practitioners alike are uneasy whenever a party advocates a position which, if accepted, would interfere with the debtor's ability to reorganize. After all, one of the objectives of Chapter 11 is to give the debtor some breathing space. In this instance, SBC's desire to withhold further services under the interconnection agreement jeopardizes not only Lucre's future but also other creditors' prospects of being repaid what they are owed. Consequently, there is the temptation to intervene in order to protect the integrity of the reorganization process. . . . [However,] Congress has not guaranteed all debtors success under Chapter 11. . . . All that Congress has done is to set up a system within which all debtors can try. Whether a particular debtor succeeds or not is a function of its ability to overcome its own unique circumstances sufficiently to take advantage of the tools Congress has provided. . . . [T]he fact that SMC is an impediment to Lucre does not mean that I should skew the system Congress has created in order to increase Lucre's chances.

Id. Moreover, even without an injunction, Columbia cannot simply terminate service on a whim. Columbia is a state-regulated entity. "Utilities cannot terminate service without following the procedures established by the regulating agencies, which procedures are intended to provide customers with the opportunity to pay arrears over time before facing termination." In re Jones, 369 B.R. at 749, n. 3. In short, the Debtors already are provided protections from termination of service under applicable state law that are deemed adequate by Columbia's regulating agency.

III.

CONCLUSION

WHEREFORE, Columbia respectfully requests that the Court enter an order (i) approving the agreement between the Debtors and Columbia that Debtors shall deliver to Columbia a $12,000.00 cash deposit within five (5) days of the date of any order on the Columbia Objection, which deposit shall be considered adequate assurance of payment under section 366 of the Bankruptcy Code, and (ii) modifying the Utilities Order to confirm Columbia's right to discontinue or refuse service to the Debtors for any valid reason under applicable law other than commencement of this bankruptcy case and non-payment of pre-petition debts, and (iii) granting such other and further relief as may be just and proper.

Dated: August 26, 2013

Respectfully submitted,

REED SMITH LLP

By: /s/ Christopher O. Rivas
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Attorneys for Columbia Gas of Virginia, Inc.

PROOF OF SERVICE OF DOCUMENT

I am over the age of 18 and not a party to this bankruptcy case or adversary proceeding. My business address is: Reed Smith LLP, 355 South Grand Avenue, Suite 2900, Los Angeles, CA 90071.

A true and correct copy of the foregoing document entitled (*specify*): **REPLY OF COLUMBIA GAS OF VIRGINIA, INC. TO DEBTORS' OMNIBUS RESPONSE [DOCKET NO. 147] TO OBJECTIONS FILED BY VIRGINIA ELECTRIC AND POWER COMPANY d/b/a DOMINION POWER [DOCKET NO. 72] AND COLUMBIA GAS OF VIRGINIA, INC. [DOCKET NO. 88] TO AMOUNT AND SCOPE OF ADEQUATE ASSURANCE THAT CERTAIN UTILITIES ARE ENTITLED TO UNDER BANKRUPTCY CODE SECTION 366** will be served or was served **(a)** on the judge in chambers in the form and manner required by LBR 5005-2(d); and **(b)** in the manner stated below:

1. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF)**: Pursuant to controlling General Orders and LBR, the foregoing document will be served by the court via NEF and hyperlink to the document. On (*date*) August 26, 2013, I checked the CM/ECF docket for this bankruptcy case or adversary proceeding and determined that the following persons are on the Electronic Mail Notice List to receive NEF transmission at the email addresses stated below:

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2. SERVED BY UNITED STATES MAIL:
On (*date*)_____, I served the following persons and/or entities at the last known addresses in this bankruptcy case or adversary proceeding by placing a true and correct copy thereof in a sealed envelope in the United States mail, first class, postage prepaid, and addressed as follows. Listing the judge here constitutes a declaration that mailing to the judge will be completed no later than 24 hours after the document is filed.

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3. SERVED BY PERSONAL DELIVERY, OVERNIGHT MAIL, FACSIMILE TRANSMISSION OR EMAIL (state method for each person or entity served): Pursuant to F.R.Civ.P. 5 and/or controlling LBR, on (*date*) August 26, 2013, I served the following persons and/or entities by personal delivery, overnight mail service, or (for those who consented in writing to such service method), by facsimile transmission and/or email as follows. Listing the judge here constitutes a declaration that personal delivery on, or overnight mail to, the judge will be completed no later than 24 hours after the document is filed.

Honorable Judge Sherry Bluebond
United States Bankruptcy Court
Central District of California
Edward R. Roybal Federal Building and Courthouse
255 E. Temple Street, Suite 1482 / Courtroom 1475
Los Angeles, CA 90012
[Via Messenger]

☐ Service information continued on attached page

I declare under penalty of perjury under the laws of the United States that the foregoing is true and correct.

August 26, 2013	Gilda Anderson	/s/ Gilda Anderson
Date	*Printed Name*	*Signature*

1. **TO BE SERVED BY THE COURT VIA NOTICE OF ELECTRONIC FILING (NEF)**

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