UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF OHIO
EASTERN DIVISION

In re:	: **Case No. 06-51848**
	: **(Jointly Administered)**
CEP HOLDINGS, LLC, *et. al.*,	:
	: **Chapter 11**
Debtors.	:
	: **Honorable Marilyn Shea-Stonum**

PROCEDURES OBJECTION OF CERTAIN UTILITY COMPANIES TO MOTION OF DEBTORS AND DEBTORS IN POSSESSION, PURSUANT TO SECTION 366 OF THE BANKRUPTCY CODE, FOR INTERIM AND FINAL ORDERS: (A) PROHIBITING UTILITIES FROM ALTERING, REFUSING OR DISCONTINUING SERVICES TO, OR DISCRIMINATING AGAINST, THE DEBTORS ON ACCOUNT OF PREPETITION INVOICES; (B) DETERMINING THAT THE UTILITIES ARE ADEQUATELY ASSURED OF FUTURE PAYMENT; (C) ESTABLISHING PROCEDURES FOR DETERMINING REQUESTS FOR ADDITIONAL ASSURANCE; AND (D) PERMITTING UTILITY COMPANIES TO OPT OUT OF THE PROCEDURES ESTABLISHED HEREIN

American Electric Power ("AEP"), Carolina Power & Light, d/b/a Progress Energy Carolinas ("CPL"), Exelon Energy Company ("Exelon") and Dominion East Ohio ("DEO") (collectively, the "Utilities"), by counsel, object to the *Motion of Debtors and Debtors In Possession, Pursuant To Section 366 of the Bankruptcy Code, For Interim and Final Orders: (A) Prohibiting Utilities From Altering, Refusing or Discontinuing Services To, or Discriminating Against, the Debtors On Account of Prepetition Invoices; (B) Determining That the Utilities Are Adequately Assured Of Future Payment; (C) Establishing Procedures For Determining Requests For Additional Assurance; and (D) Permitting Utility Companies To Opt Out of the Procedures Established Herein* (the "Utility Motion"), and set forth the following:

Procedural Facts

1. On September 20, 2006 (the "Petition Date"), the Debtors commenced their cases

under Chapter 11 of title 11 of the United States Code (the "Bankruptcy Code") that are now pending with this Court. 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 are being jointly administered.

3. On the Petition Date, the Debtors filed the Utility Motion.

4. Through the Utility Motion, the Debtors propose to provide as adequate assurance of future payment, a deposit equal to two weeks of utility service based on the historical average utility costs over the past 12 months, to any utility company that requests such a deposit in writing within thirty days after the Petition Date (the "Proposed Utility Deposit"). The Debtors do not propose to provide the Proposed Utility Deposit to any utility that already holds a pre-petition deposit equal to or greater than the proposed two week deposit, or provide a two week deposit to any utility that is paid in advance for services. If a utility requests and accepts the Proposed Utility Deposit, then such a utility will have waived any right to seek additional adequate assurance of future payment during the course of the Debtors' chapter 11 cases. The Debtors further propose that any utility that does not submit a written request accepting the Proposed Utility Deposit by the request deadline, or does not file a Procedures Objection to opt out of the Adequate Assurance Procedures sought by the Debtors, shall be deemed to have adequate assurance of future payment. Utility Motion at ¶ 26.

4. The Debtors' rely upon their anticipated access to sufficient DIP financing to pay for future utility service to justify their two week deposit offer. Utility Motion at ¶ 25. The Debtors claim that their estimated aggregate average monthly utility obligations total approximately $486,039.40. Utility Motion at ¶ 23.

5. On September 27, 2006, the Court, on an *ex parte* basis, entered the *Interim Order and Proposed Final Order, Pursuant To Section 366 of the Bankruptcy Code: (A) Prohibiting Utilities From Altering, Refusing or Discontinuing Services To, or Discriminating Against, the Debtors On Account of Prepetition Invoices; (B) Determining That the Utilities Are Adequately Assured Of Future Payment; (C) Establishing Procedures For Determining Requests For Additional Assurance; and (D) Permitting Utility Companies To Opt Out of the Procedures Established Herein* (the "Interim Utility Order").

6. The Interim Utility Order provides that a final hearing on the Utility Motion is scheduled for October 17, 2006 at 9:30 a.m., with objections to the Debtors' proposed adequate assurance procedures to be filed by and served by October 12, 2006 (15 days after entry of the Interim Utility Order).

Facts Regarding the Debtors Which Support
<u>the Utilities' Request For Adequate Assurance of Payment</u>

7. The Debtors manufacture rubber and plastic products for the OEM automotive market. *Affidavit of Joseph Mallak In Support of Chapter 11 Petitions and First Day Motions* at ¶ 7 (hereinafter "Mallak Aff. at ¶ __").

8. The Debtors contend that they, as well as other automotive suppliers, have faced a series of unanticipated operational and market challenges that have adversely affected their operations and cash flows, which have impaired both the Debtors' suppliers and customers which in turn have severely affected the Debtors' operations and businesses. Mallak Aff. at ¶ 12.

9. Regarding the Debtors' suppliers, the Debtors claim that the September 2005

hurricanes in the Gulf Coast region disproportionately damaged manufacturers who rely on plastic resins, and that shortly after the hurricanes, the Debtors began experiencing sharp cost increases in their principal raw materials (plastic resins) which increases were attributable to interrupted refining capacity. The Debtors claim that they have continued to experience significantly higher costs for raw materials resulting from the magnified rise in the price of crude oil and natural gas. Mallak Aff. at ¶ 13.

10. Regarding the Debtors' customers, the Debtors claim that they have been unsuccessful in recovering much of the increases in raw materials costs from their customers through price increases because of the structure of the American automotive industry which makes it difficult for manufacturers such as the Debtors to pass rising material costs on to customers. The Debtors further claim that although the Debtors have expended substantial effort in attempting to source cheaper alternatives (such as recycled materials and alternative formulations) for the substitution of higher cost materials, the Debtors' customers have delayed approving such material substitutions. The Debtors claim that although they are now starting to experience success in receiving approvals of the material substitutions, the damage to the Debtors' liquidity is irreversible outside the protections of the Bankruptcy Code. Mallak Aff. at ¶ 14.

11. The Debtors contend that in addition to increased material costs, the general instability of the industry has directly harmed the Debtors' liquidity. The Debtors assert that they have been impaired by the bankruptcy filing of several large OEM's, including Delphi Corporation, the Debtors' second largest customer. The bankruptcy filing of Delphi in October 2005 alone resulted in a cash loss to the Debtors of nearly $1.7 million based on the Debtors'

unpaid prepetition claim in that case. Mallak Aff. at ¶ 15.

12. In addition to bankruptcy filings in the industry, the Debtors' general credit downgrade allegedly led to delays and increasingly delinquent customer payments for approved tooling programs. Mallak Aff. at ¶ 16.

13. The Debtors also claim that they have also experienced excess capacity at their plants due to decisions by their customers. Mallak Aff. at ¶ 17.

14. Faced with a severe liquidity crisis, the Debtors contend that they had no choice but to commence theses bankruptcy cases as the only means of preserving the Debtors as going concerns. Mallak Aff. at ¶ 19.

15. The Debtors' goal is to stabilize their business operations and financial situation and sell their assets. Mallak Aff. at ¶ 20.

Debtors' Motion For Postpetition Financing

16. On the Petition Date, the Debtors filed their *Motion of the Debtors and Debtors In Possession For Emergency Order Authorizing Debtors To: (A) Use Cash Collateral On An Emergency Basis; (B) Incur Postpetition Debt On An Emergency Basis; (C) Grant Adequate Protection and Provide Security and Other Relief To Wachovia Capital Finance Corporation (Central); and (D) Grant Certain Related Relief* (the "Financing Motion").

17. Through the Financing Motion, the Debtors sought Court approval to obtain up to $30,880,000 of DIP financing on an emergency basis. Financing Motion at ¶ 24.e.

18. The Debtors propose to use the DIP financing in accordance with a budget attached to an emergency financing order. Financing Motion at ¶ 24.f.

19. On September 25, 2006, the Court entered the *Emergency Order* regarding the

Financing Motion (the "Emergency Financing Order"). In the Emergency Order, the Court stated that is was not in a position to make affirmative findings of fact, but that it accepts the Debtors' Proposed Emergency Order as the binding agreement of the signatories thereto. Through the Proposed Emergency Order, the Debtors can obtain aggregate post-petition debt totaling $30,880,000 to fund a 90 day sale process.

20. The 90 day DIP Budget attached to the Proposed Emergency Order does not even reflect the Debtors' anticipated utility costs. The DIP Budget assumes cure payments in arrears for utilities, leases, logistics and temporary services in the amount of $1 million. It, however, is not clear what is meant by cure costs. Are the cure costs as described in the DIP Budget costs to assume and assign special rate utility contracts or are they the costs to pay for anticipated, post-petition utility usage? As the Debtors claim to use nearly $500,000 in utility services each month, the $1 million figure would not be sufficient to pay the $1.5 million the Debtors would be expected to use in the 3-month sale process or additional periods if the sale does not close within 90 days. (DIP Budget at p. 3).

The Sale Motion

21. On October 4, 2006, the Debtors filed their *Motion For Order (A) Granting Authority For the Sale of Assets Pursuant To § 363(b); (B) Approving the Assumption and Assignment of Certain Executory Contracts and Unexpired Leases In Connection With Such Sale and Determining and Adjudicating Cure Amounts With Respect To Such Contracts and Leases Pursuant To § 365; (C) Establishing Bidding Procedures; (D) Setting Date For Auction and Hearing On Approval Of Sale Of Assets; and (E) Approving Form Of Notice* (the "Sale Motion").

22. Through the Sale Motion, the Debtors are seeking Court authority to sell certain facilities as going concerns ("Sale Facilities"), and to close other facilities ("Closing Facilities"). Sale Motion at ¶¶ 8, 9.

23. It is unclear when the Closing Facilities will be liquidated by an auctioneer.

24 Regarding the Sale Facilities, the Debtors have agreed with the Lender to obtain Court approval no later than December 1, 2006 to close a sale transaction no later than December 19, 2006. Sale Motion at ¶ 15.

25. The Debtors propose to conduct the auction for the Sale Facilities on November 29, 2006, with a Sale Hearing to be held on November 30, 2006. Sale Motion at ¶¶ 21, 27.

26. The Sale Motion further provides that the Debtors reserve the right to designate a "Stalking Horse Purchaser" with respect to any or all of the Sale Facilities. Sale Motion at ¶ 26.

27. The Sale Motion further provides that the Debtors will serve a proposed cure notice on all non-debtor counterparties to executory contracts and unexpired leases which may be assumed by the Debtors and assigned to a purchaser of a Sale Facility within 30 days of the filing of the Sale Motion. Sale Motion at ¶ 30.

28. In the event that the Debtors are authorized to close certain Closing Facilities, or sell certain Sale Facilities, in order to allow the Utilities to obtain access to the applicable meter to transfer service to the applicable landlord on the applicable assumption date, the Debtors should be required to provide the Utilities with at least the same advance notice of lease rejections that the landlords will ultimately be receiving in order to ensure that the Utilities are able to dispatch an employee to the applicable location, in particular those locations where

access is difficult.

<u>Motion to Convert Debtors' Chapter 11 Cases to Chapter 7 Cases</u>

29. On September 21, 2006, the Official Committee of Pre-Petition Trade Creditors (the "Trade Committee") filed its *Motion To Convert the Debtors' Chapter 11 Cases To Chapter 7 Cases Pursuant To 11 U.S.C. § 1112(b)* ("Motion To Convert").

30. The Trade Committee seeks to convert the Debtors' chapter 11 cases to chapter 7 cases because (i) the Debtors operate to benefit only General Motors Corporation, Visteon Corporation and Delphi Corporation (collectively, the "Customers") by a costly scheme intended to maximize the inventory build for the Customers regardless of the impact upon other parties in interest, and (ii) the losses resulting from the Debtors' express plan to augment the Customers' inventory, coupled with the Debtors' express intent not to attempt a rehabilitation of the Debtors' operations, constitutes "cause" for conversion.

31. The Trade Committee contends that the following information concerning the Debtors is important to the Court's consideration of whether the Debtors' Chapter 11 bankruptcies should be converted to a Chapter 7 liquidation:

> a. The Debtors failed to operate profitably or at "break-even" in any month since the acquisition of the Debtors' facilities by The Reserve Group in August 2005 and December 2005, respectively;
>
> b. The Debtors have already obtained concessions from their Customers in the form of "immediate pay" of accounts receivable due from the Customers, resulting in a significant paydown of obligations to Wachovia – yet the Debtors still had and continue to have insufficient liquidity to operate in the ordinary course of business in the absence of incurring additional secured debt;
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> c. As a result of the Debtors' "cash burn" and the inability to generate sufficient cash flow to permit operations in the ordinary course, the Customers were required to fund approximately $2.9 million in pre-bankruptcy loans on a junior participating basis in the Wachovia revolving credit facilities to provide the

Debtors sufficient availability to sustain even the most basic operations;

d. Based upon the Trade Committee's analysis of documentation provided to it by the Debtors and other independent sources, the Trade Committee forecasts that the Debtors will lose no less than $1 million on a monthly basis from operations through the foreseeable future;

e. The operating losses of the Debtors in chapter 11 will continue to be funded either through cash infusions or junior secured and superiority loans from the Customers or some combination of the two (if so permitted by the Court), with all such loans resulting in immediate and substantial harm to the interests of general unsecured creditors;

f. The Proposed Interim DIP Order is a mechanism for which the Customers can cause the Debtors to build the Customers' inventory, regardless of the impact on the Debtors' estates and then effectuate the closings of the Debtors' facilities if the Customers have no further use for those facilities;

g. The Proposed Interim DIP Order provides the Customers, non-fiduciaries to these bankruptcy estates, with the sole discretion to elect which of the Debtors' facilities will be promptly liquidated and which will be sold on any orderly basis;

h. Throughout the Proposed Interim DIP Order, in many instances the unsecured creditors will bear the brunt of the costs associated with the build of parts banks at various facilities for the benefit of the Customers as a result of further post-petition participation in the Wachovia facilities;

i. The Proposed Interim DIP Order proposes to have a Chapter 11 Trustee appointed in the event the Debtors fail to maintain production for bank builds requested by the Customers; and

j. The Proposed Interim DIP Order provides that in the Customers' pursuit to augment their inventory at the cost of the bankruptcy estates, their professional fees ($450,000) will be paid from estate proceeds.

Motion to Convert at ¶ 15.

32. A hearing on the Motion to Convert is scheduled for October 10, 2006.

Facts Concerning the Utilities

33. Each of the Utilities provided the Debtors with prepetition utility service and have continued to provide the Debtors with post-petition utility service.fn1

34. 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 15 to 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 service will be disconnected. Accordingly, under the Utilities' billing cycles, the Debtors could receive 2 to 2 1/2 months of unpaid service before their service could be terminated for a post-petition payment default.

35. 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' estimated pre-petition losses and the post-petition deposit requests are currently as follows:

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1 In accordance with DEO's General Sales Service tariff, DEO began providing the Debtors with gas utility service effective August 1, 2006 for the Carlisle Engineer Products facility located at 15332 Old State Road, Middlefield, Ohio, because the Debtors prior gas supplier, Constellation Energy, notified DEO on June 26, 2006 that Constellation Energy would no longer supply gas to that facility effective August 1, 2006.

Utility	No. of Accounts	Pre-Petition Debt	Deposit Request
AEP	1	$10,944.64fn2	$86,475 (two-month)
CPL	1	$12,466.61	$23,021 (two-month)
DEO	1	$5,769.10	$59,500 (two-month)
Exelon	1	$151.29	$8,200 (two-month)

36. DEO maintained a pre-petition deposit in the amount of $3,500 on the Debtors' pre-petition accounts that was applied to the Debtors' pre-petition debt pursuant to 366(c)(4). The foregoing deposit was based on the fact that prior to August 1, 2006, Dominion merely provided the Debtors with transport services. Effective August 1, 2006, Dominion became obligated to provide the Debtors with supply as well because the Debtors' prior gas supplier, Constellation NewEnergy Gas Division, dropped the Debtors as a customer.

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 debtor, 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;

2 AEP applied the pre-petition deposit, plus accrued interest, which totaled $56,990.68, against the Debtors' pre-petition debt of $67,935.32 to arrive at the $10,944.64 total set forth in this chart.

(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.

(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 debtor 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 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.

(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 debtor before the date of the filing of the petition without notice or order of the court.

1. The Debtors' Attempt To Deny Post-Petition Security To Utilities That Held Pre-Petition Security Should Be Denied.

In paragraph 26 of the Utility Motion, the Debtors propose to exclude utilities that held pre-petition security from obtaining post-petition security because the Debtors assert that their pre-petition security should be considered their post-petition security. The foregoing proposal is without merit. As an initial matter, Section 366(c)(4) provides that a utility can recover or set off its pre-petition deposit against pre-petition amounts owed by the Debtors to the utility. Pursuant to Section 366(c)(4), AEP and DEO have already recouped their pre-petition security against their pre-petition losses and are still owed

money from the Debtors for pre-petition utility service. Accordingly, the pre-petition deposits held by AEP and DEO cannot be used to secure the post-petition accounts because they no longer exist.

Moreover, since Section 366(c)(3)(B)(i) provides that the absence of pre-petition security cannot be considered in determining post-petition security, it is absurd that the existence of pre-petition security should serve to deny a utility from obtaining post-petition security.

If the Debtors were pre-paying for pre-petition utility service and have agreed to continue to do so post-petition, that is an acceptable form of adequate assurance of payment pursuant to Section 366. The mere fact that the Debtors were paying for pre-petition service in advance, however, is not relevant to the post-petition adequate assurance of payment determination unless the Debtors have agreed to continue the advance payments post-petition. Therefore, the Court should deny the Utility Motion to the extent it attempts to deprive Utilities from post-petition security based on their pre-petition security.

2. The Debtors' Attempt To Extend The 20 and 30-Day Provisions Of Section 366 Should Be Rejected.

As set forth above, Section 366(b) of the Bankruptcy Code establishes a procedure whereby a debtor is to provide a utility with adequate assurance of payment, in the form of a deposit or other security within the first 20 days of the bankruptcy proceeding. If the debtor fails to provide the utility with adequate assurance of payment that the utility believes is satisfactory within the first 30 days of the bankruptcy

proceeding, Section 366(c)(2) expressly provides that the utility is entitled to alter, refuse or discontinue service to the debtor.fn3. Despite the foregoing, the Debtors have sought in the Utility Motion procedures that would extend the 20 and 30-day periods of Sections 366(b) and (c).

Under the procedures sought by the Debtors in the Utility Motion, a utility that does not believe the Debtors' two-week deposit offer is sufficient, must make a request for adequate assurance of payment no later than 30 days after the Petition Date that is in compliance with the procedures set forth in ¶ 5(a) and (b) of the Interim Utility Order.

Additionally, under the Debtors' proposed procedures, the Debtors have the greater of (i) 14 days from the receipt of such additional assurance request or (ii) 30 days from the Petition Date (the "Resolution Period") to negotiate with such utility company requesting additional adequate assurance. Interim Utility Order at ¶ 5(c). If the Debtors determine that an Additional Assurance Request is not reasonable fn3, and are not able to resolve such request during the Resolution Period, the Debtors will request during or immediately after the Resolution Period, a Determination Hearing pursuant to section 366(c)(3)(A). Interim Utility Order at ¶ 5(e). Hence, the Debtors are seeking to obtain an extension of the 20 and 30-day periods of Section 366 if a utility makes a request for adequate assurance in accordance the burdensome requirements of the Debtors' proposed procedures. There is no need for all of these procedures. The Debtors either need to provide the Utilities with acceptable adequate assurance of payment within 30 days of the Petition Date or, as set forth in subsection 3 below, file a proper Motion seeking to

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3 Section 366(c)(2) provides that the utility, not the debtor, is the entity that is to decide whether the proposed adequate assurance of payment is satisfactory.

modify the adequate assurance of payment provided to the Utilities.

3. 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 seeking to avoid the time limitations established by Section 366, the Debtors also seek procedures designed to make the adequate assurance of payment process more time consuming and burdensome. 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, the proposed procedures set forth in the Utility Motion require utilities who object to the adequate assurance procedures to file and serve a Procedure Objection which is actually received by the Debtors within 15 days of entry of the Interim Order (by October 12, 2006), and which includes (i) the location(s) for which utility services are provided and the relevant account number(s), (ii) a description of any deposits, prepayments or other security currently held by the objecting utility company, (iii) an explanation as to why the objecting utility company believes that the proposed two week deposit is not sufficient adequate assurance of future payment, and (iv) an identification and explanation of the utility company's proposed adequate assurance demand. Interim Utility Order at ¶ 6(b). Information regarding prepetition payment history, security deposits or other security held by a utility, which the utilities would be required to provide to the Debtors as part of an Adequate Assurance Request under the proposed procedures in the Utility Motion are statutorily irrelevant pursuant to Sections 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.

Moreover, 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.

4. The Court Should Reject The Debtors' Proposed Adequate Assurance Procedures That Contravene The Express Provisions of Section 366 Which Requires a Debtor To Provide A Utility With Adequate Assurance As Demanded By the Utility, And If The Debtor Believes That The Deposit Should Be Modified, The Debtor Must File A Motion To Modify The Adequate Assurance Deposit Paid To The Utility.

Section 366(b) expressly provides that a debtor must provide a utility with adequate assurance of payment that the utility believes is satisfactory within the first 30 days of the bankruptcy proceeding. Section 366(c)(3)(a) (3)(A) further provides:

> 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).

Accordingly, the proper procedure under Section 366 is for a debtor to provide a utility with adequate assurance of payment requested by the utility within 30 days of the bankruptcy proceeding, and if the debtor wants a modification of the amount of adequate assurance of payment that it has provided to the utility, then the debtor must file a motion

to modify the deposit it has paid to the utility. Simply put, a debtor must first pay the requested deposit amount, and then file a motion to modify the paid deposit. *See In re Lucre, Inc.,* 333 B.R. 151 (Bankr. W.D. Mich. 2005) (holding that a debtor has no recourse to modify the adequate assurance payment that a utility is demanding until the debtor actually accepts and pays the adequate assurance that the utility proposes); *In re Stagecoach Enterprises, Inc.*, 1 B.R. 732 (Bankr. M.D. Fla. 1979) (holding that under Section 366, the utility itself has the initial right to set the amount of the deposit or other adequate assurance that it requires for the payment of utility service, and that the debtor can apply to the court for a modification of whatever amount the utility deems necessary to provide adequate assurance of payment). Additionally, the debtor has the burden of proof as to whether its requested adequate assurance modification is justified. *Id.* at 734 (holding that the debtor, as the petitioning party at a Section 366 hearing, bears the burden of proof).

B. THE COURT SHOULD ORDER THE DEBTORS TO PROVIDE THE ADEQUATE ASSURANCE OF PAYMENT REQUESTED HEREIN 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 security deposits requested by the Utilities are reasonable. See In re Stagecoach, 1 B.R. 732, 735-36 (Bankr. M.D. Fla. 1979) (two month deposit is appropriate where the debtor could receive 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 Utilities' deposit requests are based on: (1) their billing exposure created by respective state law tariffs and/or regulations; and (2) amounts that their respective state regulatory commission, which is a neutral third-party entity, permits them to request. Although the Utilities recognize that this Court is not bound by the regulations/tariffs of the applicable state governmental entity that establishes the deposit amounts that the Utilities can request from their customers, it is 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 addition, the Utilities' deposit requests are based upon: (a) the Debtors' admittedly severe liquidity issues as reflected above and the failure of the Debtors to include utility expenses in their 3-month DIP Budget; (b) the uncertainty as to whether the proceeds from the sales will be sufficient to cover secured and administrative expense claims; and (c) the lack of details regarding the proposed closing of certain Closing Facilities, or the sale of certain Sale Facilities, such as (i) the actual closing dates, (ii) how the Utilities will be notified when the Debtors no longer require service from the Utilities, and (iii) whether the Utilities be given access to properties to obtain final meter readings. Moreover, the Debtors' meaningless two week deposit offer does not even cover a one monthly billing cycle of the Utilities. Accordingly, there are several rational and objective bases upon which the Utilities' request for adequate assurance of payment is made.

In contrast, the Debtors do not provide an objective basis for their two week

deposit offer. Moreover, if a utility does not serve an Additional Adequate Assurance Request by within 30 days of the Petition Date that is not in compliance with the procedures set forth in ¶ 5(a) and (b) of the Interim Utility Order, or does not file a Procedures Objection within 15 days of entry of the Interim Utility Order it waives its right to seek additional adequate assurance of payment pursuant to Section 366. Interim Utility Order at ¶ 4. Furthermore, the Debtors rely upon their anticipated access to sufficient DIP financing to pay for future utility service to justify their two week deposit offer. (*See* Utility Motion at ¶ 25). 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.

WHEREFORE, the Utilities respectfully request that this Court enter an order:

(I) Vacating the Interim Utility Order;

(II) Awarding the Utilities the post-petition adequate assurances of payment they have requested from the Debtors herein; and

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

Dated: October 11, 2006

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CERTIFICATE OF SERVICE

I hereby certify that on this day of October 11, 2006, I caused a true and correct copy of the foregoing *Objection* to be served on the following individuals as follows:

Via Email Transmission To:

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Carl D. Rafoth, Esq.

SUPPLEMENTAL CERTIFICATE OF SERVICE

I hereby certify that on this 11th day of October 2006 I caused a true and correct copy of the foregoing *Objection* to be served upon the following individuals as follows and as required by this Court's September 28, 2006 GENERAL ORDER ONE pertaining to certain case management procedures:

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