Wall Street Could Make $1 Billion Off PG&E’s Bankruptcy – and Ratepayers Are on the Hook

KQED

PG&E’s bankruptcy is making some people very rich.
Since the utility filed for Chapter 11 protection in January, lawyers and consultants have made a staggering $217 million. Big banks have netted $114 million in financing fees — and that number could top $1 billion by the time the company exits bankruptcy next year.
Others are reaping the bankruptcy windfall, too.
A handful of hedge funds stand to make billions because they own nearly one-fifth of PG&E’s stock and bought up more than half of the wildfire insurance claims against the company — meaning they are basically on both sides of the negotiating table in court.
And stock prices are fluctuating wildly based on the latest twists and turns in the bankruptcy case, providing speculators the opportunity to make huge short-term returns.
Bankruptcy is big business for Wall Street, and PG&E’s Chapter 11 case is no different — except in this situation, utility ratepayers are the ones who will likely be picking up the bulk of the tab.
“PG&E’s sole source of revenue, the only way they earn money, is from ratepayer bills,” said Mark Toney, president of the ratepayer advocacy group TURN. “PG&E filed for bankruptcy voluntarily … PG&E didn’t have to go into bankruptcy. They did it for their financial advantage and to try to stick their shareholder costs to the ratepayers.”
Bankruptcy, he charged, is a “strategy of Wall Street to extract the maximum amount of cash from California ratepayers.”
PG&E disputes that characterization, noting through a spokeswoman that a state law passed earlier this year requires the utility’s exit plan from bankruptcy to be “neutral, to ratepayers, on average” and that shareholders will pay for the costs of the Chapter 11 case.
But Gov. Gavin Newsom has raised concerns as well.
Late Friday, in a letter to PG&E executives, Newsom rejected the utility’s current proposal for exiting bankruptcy, saying it doesn’t do enough to ensure that the company will emerge stronger and better

able to provide safe, reliable power. He wrote that PG&E's proposal depends too much on borrowing money, and he wants more accountability — including a plan for essentially handing control of the company over to the state or another third party if it fails to meet the state's requirements.

Professor Jared Ellias of UC Hastings College of the Law, an expert in bankruptcy law who has been following PG&E's case closely, agreed that customers are the ones who will foot most of the bill for this bankruptcy — and that PG&E's current plan for the future wouldn't transform the utility.

"As a ratepayer, it can be strange to watch all of these investors making money off PG&E while feeling kind of helpless, because chances are our rates are going to go up in the years to come," he said.

"This company isn't leaving bankruptcy with a solution to its business problems," Ellias added. "So I think as a ratepayer, it's really easy to be cynical" about how the process benefits investors, banks, lawyers and other consultants.

Facing billions of dollars in legal claims from wildfire victims and demands from the governor, state officials and a federal court to dramatically improve its safety performance, there's no doubt that PG&E would have had to spend at least some of the money it's now shelling out in bankruptcy.

But there are major costs that the company wouldn't be incurring if it hadn't filed for bankruptcy, according to court filings and regulatory records reviewed by KQED News.

Ellias said there's an entire industry dedicated to helping shepherd big companies through bankruptcy.

"There are a large number of professionals who are highly skilled, who specialize in helping companies like PG&E and their creditors deal with their problems. They are very, very skilled professionals … but they're also incredibly expensive. And so when a company runs into financial trouble, they tend to have to spend a lot of money on lawyers and consultants and investment bankers to try to get a handle on what's going on," he said.

But there are doubts over whether the company will in fact emerge from the bankruptcy proceedings stronger, with less debt and better able to serve the 16 million residents who depend on it for power — even though the purpose of Chapter 11 is for a reorganized company to exit the process more financially stable.

"Normally when a company leaves bankruptcy, they've convinced the judge that whatever their business problems were prior to entering into bankruptcy, they've solved those problems," Ellias said. "They've chosen to use the bankruptcy process to try to manage the fire victims' claims, … and to try to settle those claims. And that's the main thing they're going to accomplish in bankruptcy."

But the new PG&E won't have solved its most pressing challenge: How to stop causing devastating wildfires.

“They’re not leaving bankruptcy with a lot of ammunition in the tank to deal with the problems that are going to come to them in the years ahead,” Ellias said.

“When they leave, they’re not going to be all that different than the PG&E that filed for Chapter 11 in January.”

The Business of Bankruptcy

There are many ways in which investors, lawyers and consultants are making money off PG&E’s bankruptcy. Some are straightforward, such as the money being paid out to attorneys, investment advisers and accounting firms.

Others are more nebulous and difficult to quantify — like the profits still being made from stock trades and the enormous sums that hedge funds stand to earn by essentially playing both sides of the case.

And some are largely unknown, such as the fees being paid to banks that have agreed to finance future loans to the company, the terms of which are generally kept secret.

Here’s what KQED found after reviewing court filings and other records.

Fees and Expenses: ‘Among the Most Expensive Bankruptcy Cases Ever’

The biggest ticket items so far are the fees and expenses charged to PG&E by lawyers, accountants, investment bankers and other consultants: According to a KQED review of court records, that bill totals at least $217,771,932.16 so far. That number encompasses all the fees and expenses filed with the bankruptcy court to date, generally covering the period from January through September, with some including October.

And it’s a bill that will only climb. U.S. Trustee Andrew Vara, the government watchdog overseeing PG&E’s case, wrote in a recent court filing that the professional fees in this case “are likely to rank eventually among the most expensive bankruptcy cases ever filed.”

Under bankruptcy law, the company filing for Chapter 11 must pay for not only their own attorneys and consultants, but also for those representing the groups to whom the company owes money.

This means that in addition to their own lawyers, PG&E has been billed more than $26 million in attorney fees and expenses between January and October by the group representing wildfire victims; $21.5 million by financial advisers working for PG&E’s secured creditors; and nearly $18 million by the law firm charged with representing unsecured creditors — groups that PG&E owes money to that don’t have collateral.

“Everybody who is considered a creditor, someone that PG&E owes money to, gets a seat at the table and they get their lawyer fees, all of the expert fees reimbursed,” said Toney, the ratepayer advocate.

“So we’re talking about the hedge funds are getting reimbursed. We’re talking about the wildfire

claimants, the insurance companies. … The only party not being represented is ratepayers."
All the Company's Lawyers
The seven law firms assisting PG&E in the bankruptcy have billed the company more than $125 million this year.
By far the biggest of those bills comes from Cravath, Swaine & Moore, PG&E's lead attorneys for wildfire-related tort issues. The firm has billed more than $71 million in fees and expenses since the bankruptcy case was filed, including more than $13 million in September alone.
Another firm, Munger, Tolles & Olson, represents PG&E before regulators and on wildfire liability issues. For the first 10 months of this year, the firm has billed nearly $20 million in legal fees and more than $250,000 in expenses. That includes $3.97 million in fees and expenses in October alone. Lawyers at the firm charge between $400 and $1,400 an hour; and expenses include $19,230.59 in hotel charges in October.
And Weil, Gotshal & Manges, PG&E's main bankruptcy attorneys, billed more than $23 million in fees and expenses through September.
Vara, the federal trustee overseeing the case, has questioned whether all the expenses are justified. In a September filing, he wrote he had found "$4 million in improper, excessive, or otherwise objectionable fees and expenses" and said the first round of fee applications "reflect numerous instances of questionable billing judgment and overstaffing."
He cited internal meetings and conference calls involving 22 attorneys from the same firm; "numerous instances of large numbers of attorneys billing" for the same hearing; "implausibly high numbers of billable hours" by one lawyer in a single day — including one case in which a person billed for 24 hours in one day; and meals and transportation expenses charged to PG&E even when no case was done for the utility that day.
The bankruptcy judge eventually approved all the charges.
In a written statement, PG&E told KQED News that the company has "retained expert advisors to help guide us through the complex Chapter 11 process – and help shape the business for the future – so that the company can remain focused on serving customers, enhancing our wildfire safety efforts, and working together with our stakeholders to create a more sustainable foundation for the delivery of safe, reliable and affordable service in the years ahead."
Financing Fees: Paying a Premium for Bankruptcy Loans
The other direct way PG&E is paying Wall Street is through borrowing money. The interest and fees associated with those loans could top $1 billion, even if the company doesn't actually tap all the cash it's

qualified to borrow.
When a company like PG&E files for bankruptcy, it must secure financing to carry it through the court proceedings. Those loans leapfrog to the head of the line, meaning they are guaranteed to be paid back ahead of other debt.
Then, the company must set up exit financing to help ensure a smooth transition out of bankruptcy.
In this case, PG&E secured $5.5 billion in financing at the beginning of the bankruptcy from 10 large institutions: J.P. Morgan Securities, Merrill Lynch, Pierce, Fenner & Smith, Barclays Bank, Citibank, BNP Paribas Securities, Credit Suisse Loan Funding, Goldman Sachs Bank USA, MUFG Union Bank and Wells Fargo Securities.
So far this year, according to SEC filings, those loans have netted the banks $114 million in financing fees.
Ellias says studies have shown bankruptcy financing carries higher costs.
“In some ways it’s kind of like a penalty, where you did a poor job managing your business and now you can get this loan that is more expensive than what you should have had to pay,” he said.
Less clear still is how much PG&E will pay for its next round of financing, though one estimate pegs the number at $1 billion.
In an Oct. 23 court filing, PG&E wrote that it plans to use $14 billion in equity commitment and has lined up $34 billion in bridge loans if it needs to draw on them for its exit financing.
The company wrote in the filing that it does not currently anticipate having to draw on those bridge loans. But attorneys for wildfire victims pointed out in a court filing that even if the company doesn’t need the loans, it will still have to pay steep financing fees.
“The fees for this unnecessary financing could exceed $1 billion,” lawyer David J. Richardson, of the Baker & Hostetler firm, wrote in objecting to PG&E’s plan.
Toney said this all shows who the bankruptcy’s biggest winners will be.
“Bankruptcy is a windfall for Wall Street. It’s a windfall for banks,” he said, noting that PG&E’s first bankruptcy ended up costing around $700 million — and that this one stands to be much more expensive.
But a PG&E spokeswoman said that the new financing would actually save ratepayers up to $200 million a year by allowing the company to refinance existing, higher interest rate debt with debt at lower interest rates — a change that would save ratepayers money.
Hedge Funds Playing Both Sides
But perhaps no one stands to make as much as the 10 hedge funds that are playing both sides of PG&E’s

bankruptcy and wildfire liability crisis.
Those 10 companies have bought into the company as stockholders. At the same time, they've bought billions of dollars' worth of insurance company claims against the utility arising from the 2017 and 2018 wildfires.
Here's how that works: After a utility-caused wildfire, insurance companies pay customers for the damage they've suffered, then go after PG&E to recover the money they've paid out . But since the process can be long and drawn out — especially during a bankruptcy proceeding — the insurers are willing to sell their claims at a loss.
"If you're an insurance company, you're in the business of mitigating losses and minimizing risks," said Ellias. "So when this company ran into financial trouble and then filed for bankruptcy, you had the option of selling your claim to hedge funds who would give you cash and then you could walk away from this situation … So you're willing to part with your claims at a discount because you didn't want to spend the next year taking on the risk of a bankruptcy filing and dealing with PG&E."
According to the Wall Street Journal, Boston-based hedge fund Baupost Group has purchased at least $6 billion of its $7.4 billion in subrogation claims for around 30 to 35 cents on the dollar — meaning it could make hundreds of millions of dollars under an $11 billion insurance settlement proposed as part of the bankruptcy case.
Baupost also owns 24.5 million shares of PG&E stock, giving it an ownership stake in the company of about 4.6%. The shares have fluctuated wildly this year, but Baupost's payout from the insurance settlement would more than make up for any losses the company has suffered on its stock holdings.
Critics often refer to firms that trade in these types of distressed assets as "investment vultures." Many of the shares were bought at bargain basement prices around the time PG&E filed for bankruptcy.

The fact that hedge funds stand to profit in this situation doesn't sit right with Amy Bach, executive director of United Policyholders, which advocates for insurance consumers.
"It doesn't seem right that investors should be able to profit from a dynamic that they didn't have any role in in the first place," she said, noting that the original insurance companies, not hedge funds, took the risk to insure the consumers.
But Bach said the complicated nature of these investments raises another concern: Whether the entry of more parties, like the hedge funds, into the bankruptcy proceedings has made the case more expensive.
"It's just taking way longer than it should have because of the complexity of all these parties being involved, because there are so many hands that want to get into the pot," she said.

Indiana University associate law professor Pamela Foohey said it's not necessarily a bad thing that hedge funds are essentially on multiple sides of the negotiating table at once — they may have more of an interest in shaping an outcome to the bankruptcy that benefits all parties.

"In large bankruptcies, there are repeat players simply because the entire financial industry in this country and most of the world is so compressed," she added.

Stocks: For Investors, Volatility Means Opportunity

Of course, while all this maneuvering is happening in bankruptcy court, PG&E remains a publicly traded company — giving aggressive investors opportunities to make money on its fluctuating stock prices.

"A lot of hedge funds look for volatility when they're trading, they're looking for assets that are moving around so they can buy them and sell them and buy them and sell them and make other bets on the price of the stock," Ellias said. "So a boring public utility with stock is just kind of stable. That's not that interesting necessarily to a hedge fund that's trying to make a lot of money. They need volatility so they can trade. And this company has certainly supplied plenty of volatility."

PG&E shares have ping-ponged wildly over the past several years, from a high of $70 a share before the 2017 fires down to around $6 a share when the company filed for bankruptcy. In October, amid uncertainty in the bankruptcy case and news that PG&E lines had sparked another fire, shares plunged again to around $3.80 a share — but now sit around $10 a share.

Those low numbers may sound bad — but volatility means opportunity. For example, in April the Wall Street Journal reported that three hedge funds had bought about 10 percent of PG&E's stock when it was at a record low, right after bankruptcy; if they had sold back then, they would have made around $700 million. Two of those — Abrams Capital Management and Redwood Capital Management LLC — also own those subrogation claims against the company.

Foohey said the interest in PG&E's stock could also be seen as a good thing for ratepayers.

"The fact that there is an active trading market in the stock suggests that someone out there thinks the stock is worth something, which means they think the company … has the ability to be restructured," she said.

Any strength in the stock and share price stands to benefit wildfire victims, too — part of the $13.5 billion settlement reached in early December calls for survivors to receive 20 percent of the company's shares as part of the broader payout.

That was also stellar news for current shareholders, Ellias said, who have been fighting with bondholders in court over who will control the company once it exits Chapter 11.

"For the current shareholders of the company who are really just fighting to stay in control and to still keep some part of their ownership share of this company after bankruptcy, this is a huge win," Ellias said. "Huge win. I mean, the shares have been really trading up on this news. This is exciting news for the shareholders."

Among those shareholders: Abrams and Baupost, the companies that are also making money off the insurance settlement.

This story was updated on Dec. 18 to reflect statements provided by PG&E.