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**UNITED STATES BANKRUPTCY COURT  
SOUTHERN DISTRICT OF NEW YORK**

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In re: )  
 )  
 ) Chapter 11  
Calpine Corporation, et al., )  
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 ) Case No. 05-\_\_\_\_ (\_\_\_\_)  
Debtors. ) Jointly Administered  
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**MOTION FOR ORDER UNDER 11 U.S.C. §§ 105, 362 AND 541 AND FED. R. BANKR.  
P. 3002 ESTABLISHING NOTIFICATION AND HEARING PROCEDURES  
FOR TRADING IN EQUITY SECURITIES**

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The above-captioned debtors (collectively, the “Debtors”) hereby move the Court (the “Motion”) for the entry of an order, substantially in the form attached hereto as **Exhibit A**, under 11 U.S.C. §§ 105, 362 and 541 and Fed. R. Bank. P. 3002 (the “Order”) (a) establishing notice and hearing procedures that must be satisfied before certain transfers of equity securities of Calpine Corporation (“Calpine”) or of any beneficial interest therein are deemed effective and (b) allowing for a hearing with respect to the prospective application of such procedures if the officially appointed committee of unsecured creditors (the “Creditors’ Committee”) makes a timely objection.<sup>1</sup>

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<sup>1</sup> The facts and circumstances supporting this Motion are set forth in the Declaration of Eric Pryor (the “Pryor Declaration”) annexed to the Motion as **Exhibit F**.

## **Jurisdiction**

1. The Court has jurisdiction over this matter pursuant to 28 U.S.C. § 1334. This matter is a core proceeding within the meaning of 28 U.S.C. § 157(b)(2).
2. Venue is proper pursuant to 28 U.S.C. §§ 1408 and 1409.
3. The statutory predicates for the relief requested herein are sections 105, 362 and 541 of the Bankruptcy Code, 11 U.S.C. §§ 101-1330 (the “Bankruptcy Code”) and Rule 3002 of the Federal Rules of Bankruptcy Procedure (the “Bankruptcy Rules”).

## **Background**

4. On the date hereof (the “Petition Date”), the Debtors filed their voluntary petitions for relief (the “Chapter 11 Cases”) under chapter 11 of the Bankruptcy Code. The Debtors are operating their businesses and managing their properties as debtors in possession pursuant to §§ 1107(a) and 1108 of the Bankruptcy Code.

5. Calpine, together with its direct and indirect subsidiaries (collectively, the “Company”), is involved in the development, construction, ownership and operation of power generation facilities and the sale of electricity and its by-product, thermal energy, primarily in the form of steam, predominantly in North America. It operates the largest fleet of natural gas-fired power plants in North America, and supplies approximately 3.5% of the electricity consumed in the United States, where the Company has ownership interests in, and operates, gas-fired power generation and cogeneration facilities, pipelines, geothermal steam fields and geothermal power generation facilities.

6. The Company owns, leases and operates 92 power plants in 21 states in the United States and three provinces in Canada. The Company also has interests in an additional five plants under active construction, including an interest in a natural gas-fired facility in Mexico. The Company markets electricity produced by its generating facilities to utilities and other third party purchasers while thermal energy produced by the gas-fired power cogeneration

facilities is sold primarily to industrial users. The Company offers to third parties energy procurement, liquidation and risk management services, combustion turbine component parts, engineering, and repair and maintenance services.

7. The Company is headquartered in San Jose, California, and employs approximately 3,302 people, of whom approximately 65 are represented by collective bargaining agreements.

8. The Company was founded in 1984 to manage energy projects and provide consulting services to power generators. The Company acquired its first megawatt in 1989 and completed its initial public offering in 1996. Since that time, the Company has ambitiously pursued its goal of acquiring and developing the energy industry's leading fleet of efficient, clean and reliable power generation facilities. To that end, between 2001 and 2004, the Company more than doubled the number of its power plants and can presently deliver more than 26,000 megawatts of electricity, with approximately 2,000 megawatts under active construction, or enough power altogether for approximately 28 million households.

9. The advanced technologies and cleaner fuel sources employed by the Company operate at significantly lower heat rates (a measure of efficiency), allowing for reduced fuel costs and strong competitive advantages, assuming free market-based competition. Within its major markets, the Company also seeks to locate its natural gas-fired plants in clusters, or "systems", to gain operational and supply-chain efficiencies.

10. One of the hallmarks of the Company's business model is its commitment to environmental responsibility. By focusing on the construction of modern, natural gas-fired and geothermal power plants – which emit significantly less carbon monoxide and other toxic substances than coal-fired facilities – the Company believes it currently has the largest, cleanest and most fuel-efficient fleet of power plants in the industry. The majority of the Company's

plants use “combined cycle” generation; *i.e.*, natural gas-fired combustion turbines and steam turbines that operate in tandem to generate power. This process requires up to 40% less fuel than older technologies and has a much lower environmental impact. The Company is also one of the world’s largest (if not the largest) producers of renewable and clean geothermal power, a natural energy source that burns no fossil fuels and thus has only negligible air emissions. Located in northern California at The Geysers, the Company has more than 350 active production wells providing steam that is piped into turbines to generate electricity.

11. Among the Company’s principal subsidiaries and affiliates are Calpine Energy Services, L.P., which offers to third parties energy procurement, liquidation and risk management services; Calpine Turbine Services, which sells combustion turbine component parts and repair and maintenance services;<sup>2</sup> Calpine Power Services, Inc., which provides engineering, procurement, construction management, commissioning and operations and management services; and Calpine Construct, which develops and builds new power facilities.

12. Before the Petition Date, Calpine’s common stock traded on the New York Stock Exchange (the “NYSE”) under the ticker symbol “CPN.” On December 6, 2005, the NYSE suspended trading in Calpine’s common stock and subsequently delisted it from the exchange. On December 7, 2005, the Equity Securities began trading on the over-the-counter market under the symbol “CPNL.PK.” As of November 8, 2005, Calpine had 569,382,412 shares issued and outstanding.

### **The United States Electricity Market**

13. The energy generation industry is one of the largest segments of the United States economy. Until recently, electricity providers consisted of relatively few utility monopolies

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<sup>2</sup> Calpine Turbine Services in turn includes Power Systems Mfg., LLC, in Jupiter, Florida, Thomassen Turbine Systems America, Inc. and Thomassen Turbine Systems B.V., in the Netherlands.

operating aged, inefficient, expensive and high-pollution facilities. But various industry trends, including deregulation, have introduced greater competition into energy markets. Most significantly, for the past decade, at the deregulated wholesale level, electric power generators have been able to sell directly to public utilities, municipalities and electric cooperatives.

14. The majority of United States power plants are coal-fired or nuclear, although most new power plants are fueled by natural gas. Future environmental protection initiatives could force many of the oldest and dirtiest coal plants to install costly emission control devices or close. Accordingly, the industry trend is likely to continue to be construction of cleaner and more efficient natural gas-fired facilities.

15. The Company's business model seeks to capitalize on these industry movements towards greater competition and cleaner fuel sources. But although the overall consumption rate of electricity continues to grow, the recent completion of many natural gas-fired combustion turbine projects has led to a sharp increase in power supplies and excess capacity in many of the Company's markets. During 2005, the Company operated at an average baseload capacity factor of approximately 45% through November. At the same time, the presently high cost of natural gas has made the operation of natural gas-fired plants more expensive. The combination of these two factors – an oversupply of electricity and the expensive price of natural gas fuel – has caused severe liquidity challenges for many of the power providers in the United States electricity markets, including the Company.

#### **Summary of Prepetition Indebtedness**

16. As set forth in the form 10-K filed by the Company on March 31, 2005, as of December 31, 2004, the Company's total consolidated funded debt was approximately \$18.0 billion, consisting of secured construction/project financing, capital lease obligations, senior notes and institutional term loans, convertible senior notes, preferred interests, trust preferred securities, secured and unsecured notes payable and borrowings under lines of credit. Moreover,

as of the Petition Date, the Company had accumulated approximately \$3.9 billion of net operating loss carryforwards and other tax credits.

### **Events Leading to the Chapter 11 Cases**

17. As noted above, the Company more than doubled its installed capacity between 2001 and 2004. This rapid expansion was funded primarily by incurring additional debt. Obligations to service this debt, coupled with challenging market conditions for electricity providers generally and in certain regional markets for the Company specifically, as well as other recent setbacks faced by the Company, have precipitated these Chapter 11 Cases.

18. The cost of natural gas – needed to fuel the Company’s fleet of mostly natural gas-fired combustion plants – has risen to a historically high level while the cost of coal is relatively much lower. This persisting imbalance places the Company at a severe disadvantage as compared to its competitors that operate coal-fired facilities. The effect was exacerbated when the Company sold substantially all of its remaining oil and natural gas reserves in July 2005. Prior to the sale, the Company’s cost to produce natural gas was significantly lower than natural gas prices in recent years and the sale left the Company in an unhedged, short fixed-price gas position.

19. In addition, excess capacity in the energy market resulted in the Company running at an average baseload capacity factor during the past year of approximately 45%. This has resulted in lower revenues than the Company is capable of generating were it to run at optimal capacity levels. Excess capacity in the energy market (including due to the continued operation of coal-burning facilities) over the past several years has also resulted in a sustained period of low spark spreads (the difference between the cost of fuel and electricity revenues), particularly in the Southeast as well as in certain other markets in which the Company operates. Furthermore, certain contract constraints and other obligations prevent the Company from shutting down facilities that are not generating sufficient power to cover costs.

20. One reason for the presently high cost of natural gas is constrained supplies from traditional drilling programs relative to demand. Although the high prices have led to initiatives to develop alternative supply options such as liquid natural gas or coal gasification, such alternative sources of fuel are not currently available to the Company. So long as the price of natural gas remains high (or increases further), and the Company does not have access to significant sources of alternative fuel supplies, the Company will be adversely affected.

21. The inconsistent transition to deregulated energy markets in North America exposes the Company to varying competitive pressures. In deregulated, highly competitive markets, the Company's natural gas-fired or geothermal merchant capacity competes directly with all other sources of electricity, such as nuclear, coal, oil or gas-fired. In highly regulated, uncompetitive markets, however, a local utility relies largely on its own supply to satisfy its own demand before buying competitively provided power. It is a sizable challenge for the Company to operate within and among these varying environments.

22. The Company relied heavily on debt financing to fund its rapid growth. Satisfying its obligations under its indebtedness, while funding anticipated capital expenditures and working capital requirements during what has been a period of low average baseload capacity factors and depressed spark spreads has left the Company with liquidity shortfalls. Accordingly, the Company launched a strategic initiative to reduce debt in May 2005 that included the possible sale or monetization of certain of the Company's assets. But covenant restrictions in the Company's debt (and certain equity) instruments preclude the Company from undertaking certain of these transactions or restrict the use of proceeds therefrom. Thus, the Company has been prevented from raising the necessary money to fund its debt service and operational needs or, even if such transactions could be completed, using the proceeds to reduce its debt.

23. A number of recent setbacks to the Company's liquidity position culminated in the filing of the Chapter 11 Cases. Most significantly, the Company's use of certain asset sale proceeds to purchase fuel for its power plants resulted in litigation with the trustees representing the holders of the Company's First- and Second-Lien Notes, who alleged that the use of the asset sale proceeds violated the terms of the indentures governing those Notes. Within the last month, the Delaware Chancery Court ruled that the Company's fuel purchases violated those indentures and ordered the Company to repay into a collateral account \$313 million plus interest by January 22, 2006. The Company appealed this decision but, on December 16, 2005, the Delaware Supreme Court affirmed the decision of the Chancery Court requiring that those funds be repaid. The prospect of having to satisfy such a sizable judgment in such a short period of time – along with the other factors described above – have made it necessary for the Company to commence reorganization cases under the Bankruptcy Code.

#### **The Debtors' Net Operating Losses and Tax Credits**

24. The Debtors have recently incurred, and are currently incurring, significant net operating losses ("NOLs"). By this Motion, the Debtors seek authorization to protect and preserve their valuable tax attributes, including NOL carryforwards of at least \$3.8 billion and other tax credits, consisting primarily of energy and other business credits, of at least \$46 million ("Tax Credits" and, together with the NOLs, "Tax Attributes") by establishing, pursuant to sections 105(a), 362(a)(3) and 541 of the Bankruptcy Code, notice and hearing procedures regarding the trading of Calpine equity securities that must be complied with before such trades or transfers become effective. If no trading restrictions are imposed by this Court, such trading or transfers could severely limit or even eliminate the Debtors' ability to use their Tax Attributes, a valuable asset of the Debtors' estates, and could lead to major negative consequences for the Debtors, their estates and the overall reorganization process.

25. As set forth in greater detail in the Motion and stated in the Pryor Declaration, the Tax Attributes are of significant value to the Debtors and their estates because, as explained in greater detail below, the Debtors can carry forward their NOLs to offset their future taxable income for up to 20 taxable years, thereby reducing their future aggregate tax obligations<sup>3</sup> and freeing up funds to meet working capital requirements and service debt. Such NOLs may also be utilized by the Debtors to offset any taxable income generated by transactions completed during the Chapter 11 Cases.

26. Specifically, unrestricted trading of Calpine equity securities could adversely affect the Debtors' Tax Attributes if (a) too many 5% or greater blocks of equity securities are created or (b) too many shares are added to or sold from such blocks such that, together with previous trading by 5% shareholders during the preceding three-year period, an ownership change within the meaning of section 382 of the Internal Revenue Code of 1986 (as amended, the "IRC") is triggered prior to emergence and outside the context of a confirmed chapter 11 plan of reorganization.

### **Relief Requested**

27. To preserve to the fullest extent possible the flexibility to craft a plan of reorganization that maximizes the use of their Tax Attributes, the Debtors seek limited relief that will enable them to closely monitor certain transfers of Calpine equity securities so as to be in a position to act expeditiously to prevent such transfers, if necessary, with the purpose of preserving the Tax Attributes. Thus, the Debtors request that this Court enter an order immediately, thereby preserving the status quo in this regard and, to the extent necessary, allow

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<sup>3</sup> See 26 U.S.C. § 172.

for a hearing with respect to the prospective application of such procedures if the Creditors' Committee makes a timely objection.

28. The ability of a company to use its NOLs and certain other tax attributes to reduce future taxes is subject to certain limitations contained in 26 U.S.C. § 382 ("Section 382"). As a general matter, if a corporation undergoes a change of ownership, Section 382 limits the corporation's ability to use its NOLs and certain other tax attributes to offset future income. Under Section 382, a change of ownership occurs where the percentage of a company's equity held by one or more 5% shareholders increases by more than 50 percentage points over the lowest percentage of stock owned by such shareholders at any time during a three year rolling testing period.

29. The general purpose of Section 382 is to prevent a company with taxable income from reducing its tax obligations by acquiring control of a company with built-in tax losses. To achieve this objective, Section 382 limits the amount of taxable income that can be offset by a pre-change loss to the long-term tax exempt bond rate (as published by the Treasury) as of the change-of-control date multiplied by the value of the stock of the loss corporation immediately before the ownership change. Built-in losses recognized during the five-year period after the change date are subject to similar annual limitations.

30. By establishing procedures for continuously monitoring the trading of equity securities, the Debtors can preserve their ability to seek substantive relief at the appropriate time, particularly if it appears that additional trading may jeopardize the use of their Tax Attributes. Accordingly, the Debtors request that this Court enter an order establishing the following procedures and allow for a hearing with respect to the prospective application of such procedures if the Creditors' Committee makes a timely objection:

(a) Procedure for Trading in Equity Securities

(i) Any person or entity who currently is or becomes a Substantial Shareholder (as such term is defined in paragraph (v) below) must file with the Court, and serve upon the Debtors and counsel to the Debtors, a notice of such status, in the form attached hereto as **Exhibit B**, on or before the later of (A) 40 days after the effective date of the notice of entry of the Order or (B) 10 days after becoming a Substantial Shareholder.

(ii) Prior to effectuating any transfer of equity securities (including options to acquire stock, as defined in paragraph (v) below) that would result in an increase in the amount of common stock of Calpine beneficially owned by a Substantial Shareholder or would result in a person or entity becoming a Substantial Shareholder, such Substantial Shareholder must file with the Court, and serve on the Debtors and attorneys for the Debtors, an advance written notice in the form attached hereto as **Exhibit C**,<sup>4</sup> of the intended transfer of equity securities.

(iii) Prior to effectuating any transfer of equity securities (including options to acquire stock) that would result in a decrease in the amount of common stock of Calpine beneficially owned by a Substantial Shareholder or would result in a person or entity's ceasing to be a Substantial Shareholder, such Substantial Shareholder must file with the Court, and serve on the Debtors and attorneys for the Debtors, an advance written notice, in the form attached hereto as **Exhibit D**,<sup>5</sup> of the intended transfer of equity securities.

(iv) The Debtors would have 30 calendar days after receipt of a Notice of Proposed Transfer to file with this Court and serve on such Substantial Shareholder an objection

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<sup>4</sup> A notice in the form of **Exhibit C** is hereinafter referred to as a "Notice of Intent to Purchase, Acquire or Otherwise Accumulate."

<sup>5</sup> A notice in the form of **Exhibit D** (as described below) is hereinafter referred to as a "Notice of Intent to Sell, Trade or Otherwise Transfer" (and, together with a Notice of Intent to Purchase, Acquire or Accumulate, is collectively referred to as a "Notice of Proposed Transfer").

to any proposed transfer of equity securities described in the Notice of Proposed Transfer on the grounds that such transfer might adversely affect the Debtors' ability to utilize their Tax Attributes. If the Debtors file an objection, such transaction would not be effective unless approved by a final and nonappealable order of this Court. If the Debtors do not object within such 30-day period, such transaction could proceed solely as set forth in the Notice of Proposed Transfer. Further transactions within the scope of this paragraph must be the subject of additional notices as set forth herein, with an additional 30-day waiting period.

(v) For purposes of this Motion and the Order: (A) a "Substantial Shareholder" is any person or entity which beneficially owns at least 25,600,000 shares (representing approximately 4.5% of all issued and outstanding shares<sup>6</sup>) of the common stock of Calpine, (B) "beneficial ownership" of equity securities includes direct and indirect ownership (a holding company would be considered to beneficially own all shares owned or acquired by its subsidiaries), ownership by such holder's family members and persons acting in concert with such holder to make a coordinated acquisition of stock, and ownership of shares which such holder has an option to acquire, and (C) an "option" to acquire stock includes any contingent purchase, warrant, convertible debt, put, stock subject to risk of forfeiture, contract to acquire stock, or similar interest, regardless of whether it is contingent or otherwise not currently exercisable.

(b) Debtors' Right to Waive

(i) The Debtors may waive, in writing and in their sole and absolute discretion, any and all restrictions, stays and notification procedures contained in this Motion or in any order entered with respect hereto.

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<sup>6</sup> Based on 569,382,412 shares of common stock of Calpine outstanding as of November 8, 2005.

## **Basis for Relief**

### **A. The Significance of the Debtors' Tax Attributes**

31. As of the Petition Date, the Debtors had NOLs of at least \$3.8 billion and other tax credits of at least \$46 million. These Tax Attributes could translate into potential future tax savings for the Debtors of approximately \$1.5 billion, based on a combined federal and state income tax rate of approximately 40%.

32. Sections 39(a), 59(e), 172(b) and 904(c) of the IRC permit corporations to carry forward Tax Attributes to offset future taxable income and tax liability, thereby significantly improving such corporations' cash position in the future. Thus, the Debtors' Tax Attributes are a valuable asset of the estates whose availability will facilitate the Debtors' successful reorganization and serve to improve creditor recoveries. The Debtors' ability to use their Tax Attributes, however, could be severely limited under sections 382 and 383 of the IRC as a result of the trading and accumulation of Calpine equity securities prior to the consummation of a plan of reorganization.

### **B. The Provisions of IRC § 382**

33. Section 382 of the IRC limits the amount of taxable income that can be offset by a corporation's NOLs in taxable years (or portion thereof) following an ownership change.<sup>7</sup> Generally, an "ownership change" occurs if the percentage (by value) of the stock of a corporation owned by one or more 5% shareholders has increased by more than 50 percentage points over the lowest percentage of stock owned by such shareholders at any time during the

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<sup>7</sup> Similarly, section 383 of the IRC limits the amount of tax liability that can be offset by Tax Credits following an ownership change.

three-year testing period ending on the date of the ownership change.<sup>8</sup> For example, an ownership change would occur in the following situation:

An individual (“U”) owns 50.1% of the stock of corporation XYZ (“X”). U sells her 50.1 % interest to another individual (“B”), who owns 5% of XYZ’s stock. Under IRC § 382, an ownership change has occurred because B’s interest in XYZ has increased more than 50 percentage points (from 5% to 55.1%) during the testing period. The same result would follow even if B owned no XYZ stock prior to the transaction with U because B both becomes a 5% shareholder and increases his ownership by more than 50% percentage points during the testing period.

34. When an ownership change occurs, IRC § 382 limits the amount of a corporation’s income that may be offset by its “pre-change losses” to an annual amount equal to the value of the corporation prior to the ownership change multiplied by the long-term tax exempt rate. See IRC § 382(b). “Pre-change losses” would include (i) NOLs and (ii) any net unrealized built-in loss (as defined in IRC § 382(h)(3)). IRC § 383 limits the amount of tax liability that may be offset by “pre-change tax credits” to the liability attributable to the amount of income that could have been offset by pre-change losses but was not so offset. “Pre-change tax credits” would include Tax Credits. This formulaic limitation under IRC § 382 and § 383 can severely restrict the ability to use “pre-change losses” and “pre-change tax attributes” because the value of the stock of a distressed company may be quite low. By way of illustration, if the Debtors were to undergo an ownership change today, they would be permitted to offset with pre-change losses no more than approximately \$6.9 million of their income in each post-

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<sup>8</sup> In general, under IRC § 382(g)(4)(A), all stockholders who individually hold less than 5% of the stock of a company are deemed to be a single 5% stockholder throughout the three-year testing period, and transfers between such shareholders are disregarded for purposes of determining whether an ownership change has occurred (the “public group rule”). Thus, so long as 50% or more of the stock is owned by less than 5% stockholders throughout the three-year testing period, there will be no change of control under IRC § 382. Accordingly, the Debtors do not seek to impose the requested notice and hearing procedures on trading by stockholders holding less than 4.5% of Calpine stock; provided, however, that such stockholders do not have an intent to accumulate a 4.5% or greater block of stock or add or sell shares to or from such a block.

change tax year, which amount is the current market capitalization of Calpine (approximately \$156 million, as of December 19, 2005) multiplied by 4.40% (the approximate long-term tax exempt rate for December 2005). Taxable income in excess of this amount would generally be taxable to the Debtors at a combined federal and state income tax rate of approximately 35%.

35. The problem facing the Debtors, which this Motion seeks to resolve, is that if too many equity holders transfer their equity interests prior to the effective date of a plan of reorganization, such transfers may trigger an ownership change. The Debtors need the ability to monitor, and possibly object to, changes in ownership of Calpine equity securities to preserve flexibility in operating their business during the pendency of the Chapter 11 Cases, in crafting a plan of reorganization and, finally, in maximizing their ability to reduce federal income taxes by offsetting their post-reorganization income with the Tax Attributes.

**C. The Requested Relief Is Narrowly Tailored**

36. The requested relief does not bar all Calpine stock trading. Moreover, the requested relief does not prohibit the trading in the Debtors' claims. At this early juncture, the Debtors seek to establish procedures only to monitor those types of stock trading that would pose a serious risk under the IRC § 382 ownership change test, so as to preserve the Debtors' ability to seek substantive relief if it appears that a proposed trade will jeopardize the use of their Tax Attributes. The procedures requested by the Debtors in this Motion would permit most stock and all claims trading to continue, subject only to Bankruptcy Rule 3002 and applicable securities, corporate and other laws.

**D. The Requested Relief Is Necessary to Avoid Irreparable Harm to the Debtors**

37. Once a Tax Attribute is limited under IRC § 382, its use is limited forever, and once an equity interest is transferred, it cannot be undone. The relief sought herein is necessary to avoid an irrevocable loss of the Tax Attributes and the irreparable harm that would be caused

by unrestricted trading in Calpine equity securities and the Debtors' resulting inability to offset taxable income with their Tax Attributes.

38. Absent granting the relief requested herein, the Debtors would be irreparably harmed by the mere filing of this Motion. If the Debtors filed this Motion in accordance with the usual notice procedures set forth in the Bankruptcy Rules, the Debtors believe it is likely that a flurry of trading in Calpine stock would immediately follow. Parties holding Calpine stock might rush to transfer such stock before the restrictions on such trading are imposed by this Court. Such trading would put the Tax Attributes in jeopardy, as described above, and would therefore be counterproductive to the Debtors' objectives in seeking this relief. Accordingly, the Debtors request that the procedures described herein be approved and that a hearing be allowed with respect to such procedures if the Creditors' Committee makes a timely objection.

**E. Provisions of the Proposed Order**

39. Following entry of the Order, the Debtors propose to send a notice in substantially the form attached hereto as **Exhibit E** (the "Notice of Order") to (a) the Office of the United States Trustee; (b) any committee appointed under section 1102 of the Bankruptcy Code; (c) counsel for the agents under the prepetition and postpetition credit facilities; (d) the Debtors' 80 largest unsecured creditors; (e) the transfer agents for any class of common stock of Calpine; (f) the Securities and Exchange Commission; and (g) the Internal Revenue Service. Upon receipt of the Notice of Order, any transfer agent for any stock of Calpine would be required to send such Notice of Order to all holders of Calpine stock in excess of 25,600,000 shares registered with such transfer agent; provided, however, that, if any transfer agent provides the Debtors with the name and addresses of all holders of such stock, the Debtors would be required to deliver the Notice of Order to such holders. Any such registered holder would be required, in turn, to provide such Notice of Order to any holder for whose account such registered holder holds such stock in excess of 7,000,000 shares, and so on down the chain of ownership. Additionally, any

person or entity or broker or agent acting on their behalf who sells 5,000,000 shares of common stock of Calpine (or an option with respect thereto) to another person or entity would be required to provide a copy of the Notice of Order authorizing such procedures to such purchaser or any broker or agent acting on their behalf of such stock. Finally, the Debtors will promptly publish the Notice of Order in *The Wall Street Journal*, *The Financial Times* (U.S. edition) and *San Jose Mercury News*.

40. The entry of the Order shall be final; provided, however, that (a) within 10 days after the Creditors' Committee has been formed and retained counsel, the Creditors' Committee may object (an "Objection") to the prospective application of the Order from and after the date of such Objection, and (b) pending such hearing, this Order shall remain in full force and effect. If an Objection is timely filed by the Creditors' Committee, (a) a hearing will be held at the United States Bankruptcy Court for the Southern District of New York, Alexander Hamilton Custom House, One Bowling Green, New York, New York 10004-1408, at the next regularly scheduled omnibus hearing in these cases, which will be at date and time to be established by this Court and (b) further notice will be served on order of the Court; provided, however, that if an Objection is timely filed and such Objection is resolved prior to a hearing on such Objection in a manner that does not require a revision of the Order, then the Notice of Order will be sent, as further provided in paragraph 23 below.

41. The Debtors propose that, if no Objection is timely filed and served or if an Objection is timely filed and such Objection is resolved prior to hearing on such Objection in a manner that does not require a revision of the Order, the Debtors will send the Notice of Order to (a) the Office of the United States Trustee; (b) any statutory committee appointed in the Chapter 11 Cases; (c) attorneys for the agents under the prepetition and postpetition credit facilities; (d) the Debtors' 80 largest unsecured creditors; (e) the indenture trustees or transfer agents for any

class of common stock of Calpine or any bonds or debentures of the Debtors; (f) all parties who file notices of transfers of claims under Bankruptcy Rule 3001; (g) all known creditors; (h) the Securities and Exchange Commission; and (i) the Internal Revenue Service. Upon receipt of the Notice of Order, any transfer agent for any stock of Calpine will be required to send such Notice of Order to all holders of such stock registered with such transfer agent; provided, however, that if any transfer agent provides the Debtors with the name and addresses of all holders of such stock, the Debtors would be required to deliver the Notice of Order to such holders. Any such registered holder must, in turn, provide such Notice of Order to any holder for whose account such registered holder holds such stock, and so on down the chain of ownership. Additionally, any person or entity or broker or agent acting on their behalf who sells 5,000,000 shares of common stock of Calpine (or an option with respect thereto) to another person or entity must provide a copy of the Notice of Order authorizing such procedures to such purchaser or any broker or agent acting on their behalf.

42. Unless otherwise ordered by this Court, at least once every three months during the Chapter 11 Cases, all transfer agents for any stock of Calpine would be required to send the Notice of Order to all holders of such stock in excess of 7,000,000 shares registered with such transfer agent; provided, however, that if any transfer agent provides the Debtors with the name and addresses of all holders of such stock, the Debtors shall deliver the Notice of Order to such holders. Any such registered holder must, in turn, provide such Notice of Order to any holder for whose account such registered holder holds such stock in excess of 7,000,000 shares, and so on down the chain of ownership.

43. The foregoing notice procedures satisfy due process and the strictures of Bankruptcy Rule 9014 by providing the relevant counterparties with a notice and an opportunity to object and attend a hearing. See, e.g., In re Colo. Mountain Cellars, Inc., 226 B.R. 244, 246

(D. Colo. 1998) (noting that hearing is not required to satisfy Bankruptcy Rule 9014). Further, the proposed notice procedures protect the due process rights of the parties-in-interest without unnecessarily exposing the Debtors' estates to unwanted administrative expenses.

**F. NOLs Are Property of a Debtor's Estate and Are Entitled to Court Protection**

44. Courts have uniformly held that a debtor's NOLs constitute property of the estate under section 541 of the Bankruptcy Code and, as such, courts have the authority to implement certain protective measures to preserve the NOLs. The seminal case articulating this rule is In re Prudential Lines, Inc., 107 B.R. 832 (Bankr. S.D.N.Y. 1989), aff'd, 119 B.R. 430 (S.D.N.Y. 1990), aff'd, 928 F.2d 565 (2d Cir. 1991), cert. denied 502 U.S. 821 (1991). In Prudential Lines, the Bankruptcy Court for the Southern District of New York enjoined a parent corporation from taking a worthless stock deduction with respect to its wholly-owned debtor subsidiary on the grounds that allowing the parent to do so would destroy its debtor-subsidiary's NOLs. In issuing the injunction, the court held that "debtor's potential ability to utilize NOLs is property of an estate," 107 B.R. at 838, and that "the taking or a worthless stock deduction is an exercise of control over a debtor's NOLs," 107 B.R. at 842, and thus was properly subject to the automatic stay provisions of section 362 of the Bankruptcy Code. See also In re White Metal Rolling & Stamping Corp., 222 B.R. 417, 424 (Bankr. S.D.N.Y. 1998) ("it is beyond peradventure that NOL carrybacks and carryovers are property of the estate of the loss corporation that generated them"); In re Southeast Banking Corp., Case No. 91-14561-BKC (PGH) (Bankr. S.D. Fla. July 21, 1994) (debtor's interest in their NOLs "constitutes property of the estate within the scope of 11 U.S.C. Section 541(a)(i) and is entitled to the protection of the automatic stay"); In re Phar-Mor, Inc., 152 B.R. 924 (Bankr. N.D. Ohio 1993) ("the sale of stock is prohibited by § 362(a)(3) as an exercise of control over the NOL, which is property of the estate"); In re Grossman's, Inc., Case No. 97-695 (PJW) (Bankr. D. Del. Oct. 9, 1997) (debtors' NOL carryforwards are property of debtors' estates protected by the automatic stay provisions of the Bankruptcy Code). Since

the Debtors' NOLs are property of their estates, this Court has the authority under section 362 of the Bankruptcy Code to enforce the automatic stay by restricting the transfer of claims against and equity securities in the Debtors that could jeopardize the existence of this valuable asset.

**G. Tax Credits Are Property of a Debtor's Estate and Are Entitled to Court Protection**

45. Similar to NOLs, the Tax Credits are valuable assets of the Debtors' estate. The Tax Credits, like NOLs, may be used by the Debtors to offset future income and reduce future federal income taxes. Accordingly, the Tax Credits constitute property of the Debtors' estates under section 541 of the Bankruptcy Code and should be given the same protective treatment as NOLs. As with NOLs, this Court has the authority under section 362 of the Bankruptcy Code to enforce the automatic stay by restricting the transfer of Calpine equity securities, which transfers could reduce this valuable asset. Courts have granted relief similar to that sought herein with respect to non-NOL tax credits in other cases. See, e.g., In re Delta Air Lines, Inc., Case No. 05-17923 (PCB) (Bankr. S.D.N.Y. Sept. 16, 2005) (finding that NOL and tax credit carryforwards are property of the Debtors' estate and approving notification procedures and restrictions on certain transfers of claims against and interests in the debtors on an interim basis to protect, inter alia, \$346 million in non-NOL tax credits).

**H. Bankruptcy Courts Have Granted the Relief Requested in the Motion**

46. Courts have routinely restricted or enjoined transfers of equity securities or claims, or issued other injunctive relief to protect a debtor against the possible loss of its NOL carryforwards. See, e.g., In re Delta Air Lines, Inc., Case No. 05-17923 (PCB) (Bankr. S.D.N.Y. Sept. 16, 2005) (approving notification procedures and restrictions on certain transfers of claims against and equity interests in the debtors on an interim basis); In re Northwest Airlines Corp., Case No. 05-17930 (ALG) (Bankr. S.D.N.Y. Sept. 15, 2005) (approving notification procedures and restrictions on certain transfers of claims against and equity interests in the debtors on an

interim basis); In re US Airways, Inc., Case No. 04-13819 (SSM) (Bankr. E.D. Va. Apr. 1, 2005) (approving notification procedures and restrictions on certain transfers of claims against and equity interests in debtors); In re WHX Corp., Case No. 05-11444 (ALG) (Bankr. S.D.N.Y. March 31, 2005) (debtor provided 10 days to object to proposed transfers of claims or equity securities by substantial claimholders and shareholders); In re WorldCom, Inc., Case No. 02-13533 (AJG) (Bankr. S.D.N.Y. March 5, 2003) (approving notification procedures and restrictions on certain transfers of claims against and equity interests in debtors); In re W.R. Grace & Co., Case No. 01-01139 (JKF) (Bankr. D. Del. Jan. 24, 2005) (approving notification procedures and restrictions on certain transfers of equity interests in the debtors); In re UAL Corp., Case No. 02-B-48191 (EW) (Bankr. N.D. Ill. Dec. 30, 2002) (approving, on an interim basis, notification procedures and restrictions on certain transfers of equity interests in the debtors); In re Adelphia Comm. Corp., Case No. 02-41729 (REG) (Bankr. S.D.N.Y. Sept. 27, 2002) (approving notification and hearing procedures for trading in equity interests); In re US Airways Group, Inc., Case No. 02-83984 (SSM) (Bankr. E.D. Va. Oct. 2, 2002) (approving notification procedures and restrictions on certain transfers of claims against and equity interests in the debtors); In re Metrocali, Case No. 02-11579 (RE) (Bankr. D. Del. June 6, 2002) (debtor provided five business days' notice to object to proposed transfers of stock that would result in the transferee holding 5% or more of debtor's stock or reduction in ownership interest of existing 5% or greater shareholder); In re Casual Male Corp., Case No. 01-41404 (REG) (Bankr. S.D.N.Y. May 18, 2001) (enjoining transfers of common stock and convertible notes that would result in transferee's holdings increasing to or beyond 4.99%); In re Worldtex, Inc., Case No. 01-785 (MFW) (Bankr. D. Del. Apr. 2, 2001) (debtor provided 30 days' notice to object to proposed transfers that would result in transferee's holding 5% or more of debtor's common stock or decrease ownership interest of existing 5% or greater shareholder).

47. Courts granting such relief generally have done so by imposing notice and hearing requirements on any proposed transfer of stock to or by a person whose holdings of such stock exceeds, or would exceed as a result of the proposed transfer, a certain threshold amount. To accomplish this, the court and the debtor are given notice of any proposed transfers of stock by persons whose aggregate stock holdings exceed a certain dollar or share threshold, giving the debtor an opportunity to object to such transfer at a hearing. The order in First Merchants Acceptance was typical in this regard. See 1998 Bankr. LEXIS 1816 (Bankr. D. Del. 1998). In that case, the court entered an order imposing on any party intending to (i) acquire, accumulate or sell more than a prescribed number of shares of the debtor, or to add additional shares to such a block, or (ii) acquire or sell any subordinated reset notes or unsecured claims against the debtors, a duty to provide notice to the court and to debtor's counsel, after which the debtor was afforded 30 days to object to such transaction and a hearing would be held so that the court could decide whether to allow any such transfer to be consummated. See also In re US Airways, Inc., Case No. 04-13819 (SSM) (Bankr. E.D. Va. Apr. 1, 2005) (claims trading restrictions applied to claimholders expected to fall outside the de minimis rule); In re US Airways Group, Inc., Case No. 02-83984 (SSM) (Bankr. E.D. Va. Oct. 2, 2002) (same); In re Williams Comm. Group, Inc., Case No. 02-11957 (BRL) (Bankr. S.D.N.Y. July 24, 2002) (same); In re Worldtex Inc., Case No. 01-785 (MFW) (Bankr. D. Del. Apr. 2, 2001) (stock trading restrictions applied to persons who were, or would become as result of proposed transfer, a 5% stockholder). Although the relief that the Debtors request in this Motion is similar to that granted in First Merchants Acceptance, it excludes transfers by claimholders from the scope of the notice and hearing procedures, thus making the requested relief even less burdensome than the relief granted in First Merchants Acceptance.

48. The Debtors' Tax Attributes are valuable assets of their estates that will inure to the benefit of their stakeholders and facilitate the Debtors' reorganization. Unrestricted trading in the Debtors' equity securities, with no advance warning of such trades, jeopardizes these assets and impairs their value for the Debtors' stakeholders at large. The requested relief imposes a minimal burden to achieve a substantial benefit for the Debtors and their creditors and other interested parties. Accordingly, this Court should grant the requested relief and establish a notice and hearing procedure governing the trading of Calpine equity securities.

#### **Memorandum of Law**

49. This Motion includes citations to the applicable authorities and a discussion of their application to this Motion. Accordingly, the Debtors respectfully submit that such citations and discussion satisfy the requirement that the Debtors submit a separate memorandum of law in support of this Motion pursuant to Rule 9013-1 of the Local Bankruptcy Rules for the Southern District of New York.

#### **Notice**

50. No trustee, examiner or creditors' committee has been appointed in these chapter 11 cases. Notice of this Motion has been provided to: (a) the United States Trustee for the Southern District of New York; (b) the Debtors' 80 largest unsecured creditors on a consolidated basis, as identified in their chapter 11 petitions; (c) counsel to the administrative agents for the Debtors' prepetition secured lenders; (d) counsel to the Ad Hoc Committees; (e) the indenture trustees pursuant to the Debtors' secured indentures; (f) counsel to the Debtors' proposed postpetition lenders; (g) the Securities and Exchange Commission; (h) the Internal Revenue Service; and (i) the United States Department of Justice. In light of the nature of the relief requested, the Debtors submit that no other or further notice is required. A copy of the Motion is also available on the website of the Debtors' notice and claims agent, Kurtzman Carson Consultants LLC, at <http://www.kccllc.net/calpine>.

**No Prior Request**

51. No prior motion for the relief requested herein has been made to this or any other court.

WHEREFORE, the Debtors respectfully request an entry of an order, substantially in the form attached hereto as **Exhibit A**, (a) authorizing the implementation of a notice and hearing procedure governing the transfer of Calpine equity securities and (b) granting such other further relief as is just and proper.

Dated: December 20, 2005  
New York, New York

Respectfully submitted,

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