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UNITED STATES BANKRUPTCY COURT
NORTHERN DISTRICT OF CALIFORNIA

In re
SAI SOLEDAD ENERGY, INC.,

Debtor.

Case No. 95-57598

Chapter 11

**ORDER SUSTAINING SAI'S OBJECTION
TO CLAIM FILED BY AXEL JOHNSON
ENERGY DEVELOPMENT, INC.**

I. INTRODUCTION

Before the court is debtor SAI Soledad Energy, Inc.'s ("SAI") objection to the \$6 million proof of claim filed by Axel Johnson Energy Development, Inc.¹ In 1990, SAI bought a power purchase agreement ("PPA") from AJED which would allow it to sell power that it developed to Pacific Gas & Electric Company ("PG&E"). Subsequently, PG&E paid SAI \$10 million to terminate the power agreement. AJED now claims a right to damages for SAI's breach of contract based on its option to repurchase the PPA if SAI

¹Axel Johnson Energy Development, Inc., its parent, Axel Johnson and Axel Johnson Engineering will be hereafter referred to jointly as "Axel Johnson" or "AJED" unless otherwise indicated.

1 determined not to develop a project using the PPA. Based on the
2 interpretation of several agreements entered into by the parties prior to
3 the termination of the PPA, the court finds that SAI did not breach its
4 agreement with Axel Johnson.

5 **II. FACTS**

6 **A. THE PG&E POWER PURCHASE AGREEMENT**

7 On June 27, 1985, Carl Oeberst entered into an Interim Standard
8 Operating Agreement No. 4 with PG&E. This power purchase agreement
9 obligated PG&E to purchase electrical power which might be produced from
10 Oeberst's future development of a proposed 16,000 kW biomass electricity
11 generation facility to be located at the Soledad Industrial Park in
12 Monterey County, California ("Soledad project"). The PPA required Oeberst
13 to commence distribution of power within five years from the date of
14 execution of the agreement ("Article 12 deadline"), that is, by June 27,
15 1990. No consideration was paid by Oeberst to PG&E for the PPA.

16 **B. OEERST SELLS THE PPA TO AXEL JOHNSON - THE 1988 PURCHASE**
17 **AGREEMENT**

18 Oeberst was unable to develop a project based on the PPA and
19 undertook to sell it.² Oeberst was put in contact with Axel Johnson,
20 whose agents represented it to be a large and financially capable energy
21 company.

22 On May 12, 1988, Oeberst sold the PPA to Axel Johnson pursuant to an
23 agreement referred to as the 1988 Purchase Agreement. The related
24 Assignment of the PPA to Axel Johnson is dated June 30, 1988, and was

25
26 ² Eventually part of Carl Oeberst's interest was conveyed to the Oeberst
27 Holding Trust and both entities are referred to jointly as "Oeberst."

1 accepted by PG&E on July 5, 1988. Under the 1988 Purchase Agreement, no
 2 monies exchanged hands at the time of the sale. Instead, AJED committed
 3 to pay Oeberst \$5.2 million for the PPA as follows:

- 4 1. \$1,450,000 upon Construction Financing Closing;
- 5 2. \$500,000 at the time of Term Financing Closing;
- 6 3. \$3,000,000 over thirty years after Construction
 7 Financing Closing;
- 8 4. \$250,000 over five years after Construction Financing
 9 Closing.

10 Under Paragraph 2.05 of the 1988 Purchase Agreement AJED was given
 11 an option to terminate the agreement on or after September 15, 1988 if the
 12 Soledad Project construction had not begun by that date. Hence, if AJED
 13 did not begin the project using the PPA, AJED was allowed to return the
 14 PPA to Oeberst with no further liability under the agreement. Axel
 15 Johnson did not exercise its option to terminate the agreement and
 16 thereafter became liable for payment of \$5.2 million for the PPA pursuant
 17 to the agreement.

18 **C. AXEL JOHNSON SEEKS EXTENSION AND A DEFERRAL FEE FROM PG&E**

19 Within four or five months after acquiring the PPA from Oeberst, in
 20 October 1988, Axel Johnson sought an extension of the Article 12 deadline
 21 from PG&E. In December 1988, Axel Johnson and PG&E entered into a
 22 deferral agreement referred to as the First Amendment to the PPA which
 23 provided for deferral of the Article 12 deadline to June 27, 1996. This
 24 agreement was subject to approval by the California Public Utility
 25 Commission ("CPUC").

26 Along with the extension of the Article 12 deadline, Axel Johnson

1 also sought a deferral fee for monies it had expended in the approximate
2 amount of \$3.7 million. This amount included more than \$2 million which
3 Axel Johnson represented to PG&E it was obligated to pay to Oeberst. PG&E
4 accepted the expenditure as a reimbursable expense and included that
5 amount in the deferral fee.

6 Almost one year later, in November 1989, the CPUC approved the
7 deferral agreement on the condition that the payout be reduced. Despite
8 the CPUC's reduction, Axel Johnson accepted the changed terms of the
9 deferral agreement with PG&E. The CPUC allowed PG&E to make the following
10 payments to Axel Johnson for the deferral:

- 11 1. \$2,205,000 immediately;
- 12 2. \$294,000 upon approval of AJED's critical path permit;
- 13 3. \$1,176,000 when the facility began energy delivery to
14 PG&E.

15 As a result, in December 1989, PG&E paid Axel Johnson \$2,205,000 based on
16 the CPUC's ruling.

17 Soon thereafter, Michael Leighton, president of AJED, made a
18 presentation to AJED's Board of Directors in an effort to get more funding
19 for the Soledad project. While Axel Johnson had represented to Oeberst
20 that it was a large and financially capable company, its experience with
21 alternative energy was limited to selling water turbines to small hydro
22 projects in the United States. The Board declined to provide additional
23 funding for the Soledad project. Also, possibly at the same meeting,
24 AJED's Board of Directors made a decision to get out of the power plant
25 business altogether.

26 **D. AXEL JOHNSON NEGOTIATES WITH OEERST**

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

1 While Axel Johnson was pursuing an extension and deferral fee from
 2 PG&E, AJED made an offer to Oeberst to settle its \$5.2 million obligation
 3 to Oeberst. In October 1988, prior to CPUC approval, Axel Johnson made
 4 a \$2 million offer to Oeberst which consisted of two payments:

- 5 1. \$1.5 million immediately upon receipt by Axel Johnson of
 6 the first deferral payment from PG&E (which was to be
 7 \$2,940,000);
- 8 2. \$500,000 when and if the project was placed in service
 9 and following receipt by Axel Johnson from PG&E of the
 10 second deferral payment (which was to be \$735,000.)

11 Oeberst did not accept this \$2 million offer.

12 In December 1989, Axel Johnson received the first payment of
 13 \$2,205,000 from PG&E based on the CPUC's ruling. This payment was
 14 \$735,000 less than the terms originally negotiated between PG&E and AJED.
 15 After AJED received the \$2,205,000 payment, and despite AJED's
 16 representations to PG&E and the CPUC of its intention to use the deferral
 17 fee to pay Oeberst, AJED did not make any payment to Oeberst. In
 18 January 1990, Oeberst's counsel, Archibald Mull, made a formal demand on
 19 AJED for payment of the monies due to Oeberst. In mid-January 1990, Axel
 20 Johnson met with Oeberst to discuss resolving Oeberst's complaints. In
 21 late January 1990, AJED offered to settle the claims for significantly
 22 less than offered prior to the CPUC hearing. According to a letter from
 23 Leighton to John Flegel, SAI's counsel, Axel Johnson had made Oeberst an
 24 offer of \$1,070,000 which consisted of:

- 25 1. \$425,000 cash paid immediately;
- 26 2. \$278,000 which represents 50% of distributable cash from

1 the second PG&E deferral payment;

2 3. \$367,000 which represents 50% of the final PG&E payment.

3 Oeberst declined the offer stating that the "offer was so far out of line
4 that we see no reason to make a counter-offer." By letter dated February
5 22, 1990 Oeberst stated that it had "determined that Axel Johnson is not
6 dealing in good faith" and had not dealt in good faith with the CPUC or
7 PG&E. Oeberst stated that it was fully prepared to file a lawsuit and
8 take all other actions to protect its interests if they did not hear from
9 AJED with an acceptable proposal by February 27, 1990.

10 **E. AXEL JOHNSON SELLS THE PPA TO SAI - THE 1990 PURCHASE AGREEMENT**

11 While communications and threats of litigation were being exchanged
12 between Axel Johnson and Oeberst, SAI Energy became interested in
13 acquiring the PPA from AJED. SAI Energy's principal interest in the PPA
14 was to utilize it for the sale of energy from an existing geothermal
15 plant. Axel Johnson was interested in ridding itself of its liability to
16 Oeberst.

17 In late February 1990, as negotiations with Oeberst were proving
18 unsuccessful, Axel Johnson requested that SAI Energy shorten the time
19 frame for concluding the sale of the PPA. At the end of March 1990,
20 Leighton left AJED and Bill Reynolds succeeded him in negotiating the deal
21 with SAI Energy. Nevertheless, Reynolds' role was only to document the
22 business deal already arranged by Leighton. Drafts of a purchase
23 agreement were circulated.

24 In preparation for the sale of the PPA, Axel Johnson incorporated
25 Axel Johnson Soledad, Inc. as a wholly-owned subsidiary and assigned the
26 PPA to this newly formed subsidiary. The PPA was its only asset. On June

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

28

1 22, 1990, the stock in the newly formed corporation, Axel Johnson Soledad,
2 Inc., was sold to SAI Energy, Inc. which was then renamed SAI Soledad
3 Energy, Inc. ("SAI Soledad"). The PPA was still its only asset. This
4 transaction was documented by an agreement referred to as the 1990
5 Purchase Agreement.

6 Under terms of the 1990 Purchase Agreement, Axel Johnson received
7 \$50,000 in cash from SAI Energy for the PPA. In addition, Axel Johnson
8 and the newly formed corporation, SAI Soledad, agreed to split liability
9 on any potential claim by Oeberst as follows:

- 10 1. AJED would pay the first \$250,000 due to Oeberst;
- 11 2. SAI Soledad would pay the next \$1 million;
- 12 3. AJED and SAI Soledad would split evenly the next
13 \$750,000;
- 14 4. SAI Soledad would be liable for any further sum due to
15 Oeberst.

16 (See Paragraph 5.2 of the 1990 Purchase Agreement.) Hence, this agreement
17 capped Axel Johnson's liability, which was \$5.2 million, at \$625,000 and
18 left the newly formed corporation, SAI Soledad, with unlimited liability
19 thereafter. Oeberst was not a party to this agreement and thus, despite
20 the liability cap, Axel Johnson could still be sued by Oeberst for the
21 entire \$5.2 million.

22 To protect Axel Johnson's new contractual position, the 1990 Purchase
23 Agreement included an option for AJED to get the PPA back if SAI Soledad
24 determined not to proceed with development of a project with respect to
25 the PPA. Paragraph 6.9 allows AJED to repurchase the PPA at an agreed
26 upon price, or in the event they cannot agree, as determined by a mutually

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1 agreed upon arbitrator. Paragraph 6.9 provides:

2 In the event that Corporation [Axel Johnson Soledad] or Buyer
 3 [SAI Energy] determines not to proceed with development of a
 4 project with respect to the PPA... Shareholder [AJED]... shall
 thereafter have an option to acquire from the Corporation [Axel
 Johnson Soledad] the PPA... upon payment to the Corporation....

5 To further protect Axel Johnson's new contractual position, the 1990
 6 Purchase Agreement also provided that the PPA shall at all times remain
 7 an asset of the new corporation, SAI Soledad. It could not be disposed
 8 of by SAI Soledad without the prior written consent of Axel Johnson.
 9 Paragraph 6.8 of the 1990 Purchase Agreement entitled "Development of PPA
 10 through Corporation" provides:

11 Buyer [SAI] and Corporation [Axel Johnson Soledad] agree that
 12 the PPA shall at all times remain an asset of the Corporation
 13 [Axel Johnson Soledad], and shall not be assigned,
 14 transferred, conveyed, sold, or otherwise disposed of by the
 Corporation [Axel Johnson Soledad], without prior written
 15 consent of Shareholder [Axel Johnson], which consent shall not
 be unreasonably withheld; provided that any party to which PPA
 16 is transferred shall expressly agree to perform the
 obligations of Buyer [SAI] pursuant to Article 5 and Buyer
 17 [SAI] shall not be released from such obligations. Any
 project developed with respect to the PPA shall be developed
 by the Corporation [Axel Johnson Soledad] and any assets
 18 acquired in connection with such project shall at all times
 be and remain assets of the Corporation [Axel Johnson
 Soledad].

19
 20 To add further protection to Axel Johnson's contractual position, any
 21 party to whom the PPA is transferred must expressly agree to perform the
 22 obligations of SAI Energy regarding the Oeberst claims and SAI Energy
 23 would not be released from such obligations.

24 Nothing in the 1990 Purchase Agreement gives Axel Johnson a
 25 continuing monetary interest in the development of a project using the
 26 PPA. Axel Johnson wrote to Flynn regarding shortening time to sell the

1 project and the PPA, and stated "[p]lease remember that the Project will
2 earn \$1,176,000 if it is placed in service under the terms of the deferral
3 amendment. However, SAI will be responsible for dealing with the Oeberst
4 group." Despite the fact that Axel Johnson knew that the project had the
5 potential for a significant profit, Axel Johnson did not request, and the
6 agreement did not contain, any type of royalty or profit sharing provision
7 in favor of Axel Johnson from a project that might be developed by SAI
8 Soledad using the PPA.

9 **F. OEERST SUES AXEL JOHNSON AND SAI AND THE PARTIES SETTLE - THE**
10 **SETTLEMENT AND AMENDMENT AGREEMENTS**

11 Only five months after Axel Johnson sold the PPA to SAI, in November
12 1990, Oeberst filed suit against AJED and SAI in the U.S. Bankruptcy Court
13 in Carl Oeberst's bankruptcy case.³ Oeberst sought \$5.2 million plus
14 punitive damages but did not seek the return of the PPA. AJED and SAI
15 were jointly represented by Charles Treat in regard to the Oeberst
16 lawsuit.

17 Ultimately Oeberst, AJED and SAI reached a resolution of the lawsuit
18 and entered into the "Settlement Agreement and Mutual Release" dated
19 January 2, 1992 ("Settlement Agreement"). Under the Settlement Agreement
20 AJED was only required to pay \$800,000 in cash to Oeberst in order to be
21 free from any further liability. SAI was required to give Oeberst several
22 promissory notes totaling \$2.1 million.⁴ These notes were to be paid by

23
24 ³SAI Energy, Inc. and SAI Soledad Energy, Inc. will hereafter be
referred to jointly as "SAI."

25 ⁴ The six promissory notes were payable to: the Oeberst Holding
26 Trust, the bankruptcy trustee (two notes), Jon R. Bryan, Archibald M. Mull
27 III, Bert Williamson.

1 the new corporation SAI Soledad, whose only asset was the PPA. The notes
2 were not guaranteed. In addition, mutual and complete releases were given
3 by each of the parties.

4 The Settlement Agreement included an option for Oeberst to reacquire
5 the PPA at no cost if SAI determines not to proceed with the project.
6 Paragraph 6 of the Settlement Agreement provides:

7 In the event that SAISE determines not to proceed with the
8 Project, SAISE agrees to immediately notify Archibald M. Mull
9 III in writing thereof. If such notice is given, or if the
10 Note Due Date shall not have occurred by June 30, 1995, the
11 Oeberst & Associates Holding Trust shall have an option to
acquire at no cost from SAISE the PG&E Power Agreement upon
demanding assignment thereof, subject to any consent from PG&E
or other third parties that may be required for the assignment
thereof.

12 In addition, Oeberst included in the Settlement Agreement a provision
13 that SAI may not assign all or substantially all of its interest in the
14 PPA without the consent of Oeberst. (See Paragraph 13(a) of the
15 Settlement Agreement.) Paragraph 13 of the Settlement Agreement also
16 provides for payment on the Oeberst notes from any net proceeds if, prior
17 to the note due date, SAI receives a deferral fee from PG&E or assigns or
18 otherwise alienates its interest in the PPA. Net proceeds is defined as
19 cash received by SAI as a result of an assignment or other alienation of
20 the PPA to the extent that such cash exceeds SAI's out-of-pocket
21 expenditures.

22 Concurrently with entering into the Settlement Agreement, Axel
23 Johnson and SAI also separately entered into a side agreement referred to
24 as the Amendment Agreement. The Amendment Agreement was entered into in
25 order to modify the 1990 Purchase Agreement in a manner consistent with
26 the new obligations created under the Settlement Agreement. Under the

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

1 1990 Purchase Agreement, Axel Johnson's liability to Oeberst had been
2 capped at \$625,000, at least in the sense that between AJED and SAI, SAI
3 was contractually responsible for all additional damages. However, under
4 the Settlement Agreement AJED had agreed to pay Oeberst \$800,000, that is,
5 \$175,000 more than originally agreed to in 1990. In addition, AJED had
6 incurred substantial legal fees in defending both AJED and SAI against the
7 Oeberst claims. As a result, pursuant to the Amendment Agreement SAI
8 agreed to give AJED a \$200,000 promissory note to cover these chan

9 **G. SAI TERMINATES THE PPA WITH PG&E**

10 Throughout 1993, SAI expended in excess of \$4 million for the
11 engineering, design, permitting, real property acquisition, construction
12 and financing commitments for the Soledad project. However, at some point
13 in time, SAI and PG&E began discussing a possible termination of the PPA.
14 In January 1994, PG&E outlined a potential buyout offer to SAI which would
15 pay SAI \$7.5 million for returning the PPA if SAI demonstrated the
16 viability of the Soledad project by completing permit applications and
17 obtaining certain permits "critical for developing this project" by June
18 25, 1994. In addition, SAI had to agree to maintain the viability of the
19 project until CPUC approval was received. A termination of the PPA would
20 have relieved PG&E from its obligation to purchase 30 years of high-priced
21 energy from SAI's viable project. PG&E estimated that it would be
22 required to pay more than \$90 million to SAI over the life of the PPA.
23 On April 14, 1994, after several months of negotiations, PG&E offered SAI
24 \$8.3 million for canceling the PPA.

25 On November 15, 1994, SAI and PG&E entered into an agreement to
26

1 terminate the PPA referred to as the Termination Agreement.⁵ The
2 Termination Agreement provided that PG&E pay SAI \$6 million for
3 termination of the PPA upon CPUC approval. In addition, PG&E was required
4 to make interim payments to SAI for the application process and for
5 project costs of approximately \$4 million.

6 In March 1995, Axel Johnson became aware of the Termination Agreement
7 and the scheduled July 6, 1995 hearing before the CPUC for approval of the
8 Termination Agreement. AJED thereafter asserted its alleged rights under
9 the 1990 Purchase Agreement. AJED was warned by SAI not to interfere with
10 the CPUC proceedings.

11 On July 6, 1995, the CPUC approved the agreement between SAI and PG&E
12 and authorized PG&E to pay SAI the sum of \$10 million based on the fact
13 that the Soledad project was viable. Prior to July 6, 1995, PG&E had
14 already paid out approximately \$4 million of that sum for designated
15 expenditures already incurred by SAI.⁶ PG&E then paid SAI \$6 million to
16 SAI upon CPUC approval.

17 In August 1995, AJED filed suit against SAI and PG&E in the Santa
18 Clara County Superior Court alleging breach of contract and various tort
19 claims. Axel Johnson alleged that SAI breached the 1990 Purchase
20

21 ⁵On December 22, 1994, SAI and PG&E entered into the First Amendment
22 to the Termination Agreement in order to modify the language of Paragraph
23 5 to clarify the parties' intent regarding the extension of the Article
12 on-line date. This First Amendment did not alter any other provisions
of the Termination Agreement.

24 ⁶From January 23, 1995 through October 11, 1995, SAI received a
25 series of payments from PG&E pursuant to the Termination Agreement for the
26 application process and for project costs totaling approximately \$4
million. The precise basis upon which PG&E made payments to AJED prior
to CPUC approval is not clear from the evidence.

1 Agreement because AJED had an option to repurchase the PPA once SAI
2 terminated the PPA. In September 1995, AJED obtained a writ of attachment
3 for \$6 million against SAI, which was conditioned upon AJED's waiver of
4 its alleged tort claims.

5 On November 16, 1995, SAI Soledad Energy, Inc. filed this voluntary
6 Chapter 11 petition in the Northern District of California. SAI scheduled
7 AJED's alleged claim as disputed, contingent and unliquidated. On March
8 25, 1996, AJED filed its present proof of claim for \$6 million. On April
9 4, 1996, SAI filed an objection to AJED's proof of claim which commenced
10 this contested matter. The court bifurcated the proceedings into a
11 liability phase and a damages phase. The parties presented evidence
12 during trial on the liability issues and the court took the matter under
13 submission.

14 **III. ISSUES**

15 In order to make a determination of whether Axel Johnson's \$6 million
16 claim should be allowed, the court must first determine the following
17 issues:

- 18 1. Whether SAI's termination of the PPA constituted a
19 "determination not to proceed with development of a
20 project with respect to the PPA" under paragraph 6.9 of
21 the 1990 Purchase Agreement.
- 22 2. Whether the Amendment Agreement extinguished AJED's
23 option to repurchase the PPA.
- 24 3. Whether SAI breached Paragraph 6.8 of the 1990 Purchase
25 Agreement.

26 **IV. LEGAL STANDARD**

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

1 This contested matter was initiated by the filing of an objection to
2 a proof of claim. Rule 3001(f) provides that a proof of claim complying
3 with the rules constitutes prima facie evidence of the claim's validity
4 and amount. The party objecting to the claim has the burden of going
5 forward and of introducing evidence sufficient to rebut the presumption
6 of validity. Once the presumption is rebutted, the burden then shifts to
7 the claimant. The claimant must establish the validity of the claim by
8 a preponderance of the evidence. See 9 Collier on Bankruptcy ¶ 3001.09
9 (15th ed. revd. 1997).

10 Axel Johnson filed a proof of claim for \$6 million in SAI's
11 bankruptcy case. SAI objected to the claim and has submitted sufficient
12 evidence to rebut the presumption of validity. The burden therefore
13 shifts to Axel Johnson to establish the validity of the claim by a
14 preponderance of the evidence.

15 V. DISCUSSION

16 A. TERMINATION OF THE PPA BY SAI DID NOT CONSTITUTE A 17 DETERMINATION NOT TO PROCEED WITH THE DEVELOPMENT OF A PROJECT 18 WITH RESPECT TO THE PPA

19 The first issue is whether SAI's termination of the PPA constituted
20 a "determination not to proceed with development of a project with respect
21 to the PPA" under paragraph 6.9 of the 1990 Purchase Agreement. The court
22 finds that it did not.

23 Axel Johnson contends that SAI's termination of the PPA was a
24 violation of Paragraph 6.9 of the 1990 Purchase Agreement because the
25 phrase "determines not to proceed with development of a project with
26 respect to the PPA" was intended to be broad and encompass any conceivable
27 circumstance in which a power plant was not built. Axel Johnson bases its

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1 interpretation on its underlying contention that Paragraph 6.9 was
 2 inserted for the intended purpose of realizing the value of the PPA for
 3 its own benefit. On the other hand, SAI contends that the phrase was
 4 intended to be narrow in scope and apply only in limited circumstances.
 5 SAI bases its interpretation on its contention that the intended purpose
 6 of Paragraph 6.9 was to protect Axel Johnson's \$625,000 liability cap with
 7 regard to the potential Oeberst claim.

8 **1. PLAIN LANGUAGE**

9 The language of a contract is to govern its interpretation if
 10 the language is clear and explicit. California Civil Code § 1638
 11 (entitled "Ascertainment of intention; language"); see also Toms v.
 12 Hellman, 115 Cal.App. 74 (1931). Paragraph 6.9 of the 1990 Purchase
 13 Agreement entitled "Option for Shareholder to Acquire Assets" states in
 14 part:

15 In the event that Corporation [Axel Johnson Soledad]
 16 or Buyer [SAI Energy] determines not to proceed with
 17 development of a project with respect to the
 18 PPA...Shareholder [AJED]...shall thereafter have an
 19 option to acquire from the Corporation [Axel Johnson
 20 Soledad] the PPA...upon payment to the
 21 Corporation....

22 This provision gave AJED the option to repurchase the PPA from SAI if SAI
 23 or its parent "determines not to proceed with development of a project
 24 with respect to the PPA."

25 Axel Johnson argues that the plain language of paragraph 6.9 of
 26 the 1990 Purchase Agreement is clear and unambiguous. Barry Flynn, on
 27 behalf of Axel Johnson, testified that the phrase "determines not to
 28 proceed with development of a project with respect to the PPA" is "a very

1 broad, general provision, and would include any decision by SAI not to
2 build a power plant pursuant to the PPA."

3 However, Paragraph 6.8 of the 1990 Purchase Agreement gave SAI
4 the right to sell the PPA. A sale of the PPA would necessarily include
5 a "decision by SAI not to build a power plant pursuant to the PPA." But
6 Axel Johnson does not contend that a sale of the PPA is a determination
7 not to proceed with development of a project which would trigger its
8 rights to get the PPA back.⁷ Axel Johnson's position regarding the
9 meaning of this phrase is inconsistent.

10 In addition, at the time of contracting the parties discussed
11 how SAI may utilize the PPA. The parties contemplated that SAI would use
12 the PPA to sell energy from a power plant it would build in Soledad,
13 California. The parties also knew that SAI was considering converting its
14 use of the PPA to sell energy from an existing power plant referred to as
15 the Geysers. Any decision SAI would make to use the PPA for the Geysers,
16 an existing power plant, would necessarily include a "decision by SAI not
17 to build a power plant pursuant to the PPA." However, Flynn testified
18 that such a conversion of the PPA for use at the Geysers would not be a
19 determination not to proceed with development of a project, despite the
20 fact that no power plant would be built.

21 Thus, it is apparent to the court that contrary to Axel
22 Johnson's position that the plain language is clear and unambiguous, the
23 meaning of the phrase "determines not to proceed with development of a
24

25 ⁷While SAI has the right to sell the PPA to a third party, no where
26 in the agreement is there a provision giving Axel Johnson a right of first
27 refusal in the event of such sale.

1 project with respect to the PPA" cannot be determined by the words alone.
2 The court must determine the intent of the language by reference to the
3 circumstances surrounding the formation of the contract.

4 2. CIRCUMSTANCES

5 A contract may be explained by reference to the circumstances under
6 which it was made. California Civil Code § 1647 (entitled
7 "Circumstances"). Intent may be ascertained from the words used and by
8 taking into account the entire contract and circumstances under which it
9 was made. See Moss Development Co. v. Geary, 41 Cal.App.3d 1 (1974). At
10 the time Axel Johnson was negotiating with SAI for the purchase of the
11 PPA, Oeberst was threatening to file a lawsuit against Axel Johnson for
12 breach of contract, intentional misrepresentation and other torts for
13 failing and refusing to pay Oeberst the deferral fee it received from
14 PG&E. Axel Johnson had received a \$2,205,000 deferral fee which sum
15 included an expense of over \$2 million which Axel Johnson represented to
16 PG&E and the CPUC that it owed to Oeberst. Also at this time, the option
17 to terminate the 1988 Purchase Agreement with Oeberst had expired and Axel
18 Johnson was obligated to pay Oeberst a total of \$5.2 million for purchase
19 of the PPA. It was in this atmosphere that Axel Johnson and SAI
20 negotiated an agreement to sell the PPA.

21 On a shortened time frame, in late February 1990, Axel Johnson and
22 SAI began formulating a deal. Axel Johnson's principle desire in entering
23 into the sale was to be free from the burden of its \$5.2 million
24 obligation to Oeberst under the 1988 Purchase Agreement. After all, Axel
25 Johnson had decided to get out of the power plant business altogether and
26 was not planning on utilizing the PPA to sell energy. SAI was interested

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28

1 in selling energy from an existing geothermal plant. By Axel Johnson
2 selling the PPA to SAI in return for SAI's promise to pay part of the
3 Oeberst obligations, the parties' business goals would all be met.

4 In order to accomplish the sale, Axel Johnson incorporated a wholly-
5 owned subsidiary and assigned the PPA to this newly formed corporation
6 named Axel Johnson Soledad. Hence, the asset that Axel Johnson actually
7 sold to SAI was the stock in the new corporation. The new corporation's
8 only asset was the PPA.

9 Under the terms of the 1990 Purchase Agreement, Axel Johnson received
10 only \$50,000 in cash from SAI Energy for the PPA. Axel Johnson and the
11 newly formed corporation then agreed to split the Oeberst contingent
12 liability, the principal consideration for the transfer. Axel Johnson's
13 liability was capped at \$625,000 ("\$625,000 liability cap"). The new
14 corporation, whose only asset was the PPA, then became responsible for
15 unlimited liability over and above \$625,000.⁸

16 Since the new corporation's only asset was the PPA, the only way it
17 could achieve Axel Johnson's goal under this agreement was for it to
18 generate income to satisfy any potential liability to Oeberst. If SAI
19 Soledad did not generate income, Axel Johnson would still be liable for
20 the \$5.2 million obligation to Oeberst and AJED's attempt to create a
21 \$625,000 liability cap would have failed.

22 The agreement contemplated three possible ways to utilize the PPA to
23 generate the income needed to pay the Oeberst contingent liability and

24
25 ⁸Although the parties agreed to cap Axel Johnson's liability at
26 \$625,000, because Oeberst was not a party to this contract, Axel Johnson
27 was still obligated to pay Oeberst \$5.2 million under the 1988 Purchase
28 Agreement.

1 thus protect Axel Johnson's \$625,000 liability cap. SAI Soledad could
2 develop a project using the PPA in the hopes that the project would
3 generate sufficient revenue to pay Oeberst. SAI could sell the PPA to a
4 third party to generate revenue to pay Oeberst or SAI could abandon the
5 PPA, allow Axel Johnson to repurchase it and hopefully utilize it in some
6 fashion to pay Oeberst.

7 First, SAI Soledad could develop a project. At the time the parties
8 were negotiating the sale of the PPA, it was clear that SAI intended to
9 develop a project in order to sell energy to PG&E using the PPA. If SAI
10 developed a project, the 1990 Purchase Agreement provided that all the
11 assets acquired in connection with the project would remain in the
12 corporation. Paragraph 6.8 of the 1990 Purchase Agreement entitled
13 "Development of PPA through Corporation" provides in part:

14 Buyer [SAI] and Corporation [Axel Johnson Soledad]
15 agree that the PPA shall at all times remain an
16 asset of the Corporation [Axel Johnson Soledad]...
17 Any project developed with respect to the PPA shall
18 be developed by the Corporation [Axel Johnson
19 Soledad] and any assets acquired in connection with
20 such project shall at all times be and remain assets
21 of the Corporation [Axel Johnson Soledad].

22 Hence, if a project is developed with respect to the PPA, this paragraph
23 provides that profits must remain in SAI Soledad. This provision
24 protected Axel Johnson by preventing dissipation of the assets and
25 ensuring that all assets would remain available to satisfy the Oeberst
26 claims.

27 However, if SAI developed a successful project, it would keep all of
28 its profits, subject only to the Oeberst liability. For example, if SAI
Soledad earned \$100 million from the sale of the energy, SAI Soledad would

1 keep the money subject only to any Oeberst liability. Axel Johnson would
2 not be entitled to any part of the profits. Although Axel Johnson
3 realized that the PPA had a great potential for generating a large income
4 stream, and that SAI Soledad would receive \$1,176,000 from PG&E when the
5 facility began energy development under the deferral agreement, Axel
6 Johnson did not request to participate in this potential success. No
7 where in the agreement is there a provision allowing Axel Johnson to
8 receive any part of the profits from the sale of energy. Nor did Axel
9 Johnson retain any shares of the newly formed corporation's stock before
10 selling the corporation to SAI. This behavior is not consistent with its
11 contention that its intention all along was to protect the inherent value
12 of the PPA for its own benefit. If Axel Johnson was in fact concerned
13 with realizing the value of the PPA rather than shielding itself from
14 liability, Axel Johnson would not have sold the PPA to SAI for a mere
15 \$50,000 with no other possibility for additional income.

16 Second, SAI Soledad could sell the PPA. The 1990 Purchase Agreement
17 allowed SAI Soledad to sell or otherwise dispose of the PPA in order to
18 generate money to pay the Oeberst contingent liability. Paragraph 6.8 of
19 the 1990 Purchase Agreement provides in pertinent part:

20 Buyer [SAI] and Corporation [Axel Johnson Soledad] agree
21 that the PPA shall at all times remain an asset of the
22 Corporation [Axel Johnson Soledad], and shall not be
23 assigned, transferred, conveyed, sold, or otherwise
24 disposed of by the Corporation [Axel Johnson Soledad],
25 without prior written consent of Shareholder [Axel
26 Johnson], which consent shall not be unreasonably
27 withheld; provided that any party to which PPA is
28 transferred shall expressly agree to perform the
obligations of Buyer [SAI] pursuant to Article 5 and
Buyer [SAI] shall not be released from such obligations.

1 Hence, if the PPA is assigned, transferred, conveyed, sold, or
2 otherwise disposed of by SAI Soledad, the consent of Axel Johnson is
3 required. This consent cannot be unreasonably withheld, that is, Axel
4 Johnson did not have unrestricted veto power over a transfer. Thus, if
5 SAI sold the PPA, the proceeds generated would be used to pay the Oeberst
6 contingent liability.

7 For example, if SAI Soledad sold the PPA for \$20 million, under
8 Paragraph 6.8 it would be again entitled to keep the money subject only
9 to the Oeberst contingent liability. Axel Johnson would not be entitled
10 to any part of the sale proceeds because the agreement does not contain
11 any profit-sharing provision and Axel Johnson did not retain any stock in
12 the corporation. This is consistent with SAI's contention that Axel
13 Johnson just wanted to cover any liability to Oeberst and was not
14 attempting to realize the inherent value of the PPA for itself.

15 Third, SAI Soledad could abandon the PPA. As previously stated, the
16 only way SAI Soledad could protect and limit AJED's liability to Oeberst
17 was for it to use it's only asset, the PPA, to generate income to satisfy
18 Oeberst's claim. If SAI Soledad abandoned the PPA, that is, did nothing
19 to generate income from it, Axel Johnson would still be liable for the
20 \$5.2 million and SAI would have done nothing to protect the \$625,000
21 liability cap Axel Johnson had created for itself in the purchase
22 agreement.

23 In order to protect itself, Axel Johnson negotiated an option for it
24 to get the PPA back if SAI Soledad determined not to proceed with a
25 project with respect to the PPA. Paragraph 6.9 provides in part:

26 In the event that Corporation [Axel Johnson Soledad]

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

1 or Buyer [SAI Energy] determines not to proceed with
2 development of a project with respect to the PPA...
3 Shareholder [AJED]... shall thereafter have an
4 option to acquire from the Corporation [Axel Johnson
5 Soledad] the PPA...upon payment to the
6 Corporation....

7 If SAI Soledad did nothing with the PPA, Axel Johnson could get it back
8 and try to use it in some fashion to generate sufficient proceeds to cover
9 any liability to Oeberst.

10 Axel Johnson claims that termination of the PPA constituted such an
11 abandonment.⁹ SAI contends that termination did not constitute an
12 abandonment because SAI did not "do nothing to generate income" with the
13 PPA giving rise to a need for AJED to get the PPA back to try to use it
14 in some fashion to generate income to cover any liability to Oeberst. SAI
15 argues that the parties intended that if SAI produced income to cover any
16 liability to Oeberst, Axel Johnson's option would not be triggered

17 The court agrees that the termination which generated proceeds to
18 cover any Oeberst liability was not an abandonment which triggered AJED's
19 option right. The termination of the PPA is more like a sale of energy
20 or the sale of the PPA rather than an abandonment of the PPA. Instead of
21 buying high-priced energy for a period of 30 years from a viable power
22 plant being developed by SAI, PG&E sought to pay SAI one lump sum to
23 release PG&E from its 30-year obligation. The termination agreement was
24 based on SAI demonstrating the viability of the project - which it did.

25 ⁹The parties did not expressly provide for what would happen if SAI
26 were to terminate the PPA and receive sufficient proceeds to cover any
27 Oeberst liability. The parties did not anticipate termination as a
28 possibility at the time of contracting. Not until long after the 1990
29 Purchase Agreement and 1992 agreements were entered into did PG&E make
30 termination a possibility.

1 SAI's project appeared to be so successful that it was paid \$6 million.
2 Under the 1990 Purchase Agreement, if SAI sold energy or sold the PPA,
3 Axel Johnson would not be entitled to any part of the profits or proceeds.
4 The court does not see how a sale of energy which generates \$6 million in
5 proceeds is any different from a termination which generates \$6 million
6 in proceeds. Because the intent of the parties was to protect their
7 positions regarding payment of the Oeberst contingent liability, this
8 result is consistent with the intentions of the parties.

9 Thus, based on the circumstances, SAI's termination of the PPA did
10 not constitute a "determin[ation] not to proceed with development of a
11 project with respect to the PPA" and Axel Johnson's option under Paragraph
12 6.9 was never triggered.

13 Because the court determined that Axel Johnson's option was never
14 triggered, the second issue of whether the Amendment Agreement
15 extinguished that option is moot.

16 **B. SAI DID NOT BREACH PARAGRAPH 6.8 OF THE 1990 PURCHASE AGREEMENT**

17 The final issue is whether SAI breached Paragraph 6.8 of the 1990
18 Purchase Agreement by terminating the PPA without Axel Johnson's prior
19 written consent. The court finds that it did not.

20 Axel Johnson contends that SAI breached Paragraph 6.8 of the 1990
21 Purchase Agreement which requires Axel Johnson's written consent before
22 the PPA is assigned, transferred, conveyed, sold or otherwise disposed of
23 by SAI. Paragraph 6.8 of the 1990 Purchase Agreement provides in
24 pertinent part:

25 Buyer [SAI] and Corporation [Axel Johnson Soledad] agree that
26 the PPA shall at all times remain an asset of the Corporation

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

1 [Axel Johnson Soledad], and shall not be assigned,
2 transferred, conveyed, sold, or otherwise disposed of by the
3 Corporation [Axel Johnson Soledad], without prior written
consent of Shareholder [Axel Johnson], which consent shall not
be unreasonably withheld....

4 SAI concedes that Axel Johnson had this right by virtue of the 1990
5 Purchase Agreement. SAI argues that Axel Johnson had a right to consent
6 to disposal of the PPA in 1990 because under the 1990 Purchase Agreement
7 AJED was still liable to Oeberst for \$5.2 million. Axel Johnson was
8 relying on SAI to split the liability using the PPA and thus Axel Johnson
9 had an interest in monitoring its disposal.

10 However, SAI contends that this right of consent was superseded by
11 a later agreement, the 1992 Settlement Agreement. "A later agreement will
12 supersede an earlier agreement if inconsistent therewith." See In re
13 Ferrero's Estate, 142 Cal.App.2d 473, 478 (1956). See also Crossen v.
14 Foremost McKesson, Inc., 537 F.Supp 1076, 1077 (N.D.Cal. 1982).

15 In the Settlement Agreement, AJED was completely released from any
16 further liability to Oeberst. After the settlement, Axel Johnson's only
17 concern was receiving payment on its \$200,000 note. On the other hand,
18 Oeberst was given \$2.1 million in promissory notes from SAI. SAI now had
19 a direct obligation to Oeberst and would have to use the PPA, its only
20 asset, to generate income to pay those notes. As a result, Oeberst now
21 had an interest in monitoring the PPA and its disposal. In the 1992
22 Settlement Agreement, Oeberst was given a right to consent to the disposal
23 of the PPA which superseded any past rights held by Axel Johnson who was
24 now completely out of the picture. On this basis, SAI contends that
25 Paragraph 6.8 of the 1990 Purchase Agreement was superseded by the 1992
26

1 Settlement Agreement and that it did not breach Paragraph 6.8.

2 A contract may be explained by reference to the circumstances under
3 which it was made. California Civil Code § 1647 (entitled
4 "Circumstances"). At the time that Axel Johnson, SAI and Oeberst were
5 negotiating a settlement, Axel Johnson and SAI were facing claims such as
6 intentional misrepresentation and damages of \$5.2 million plus punitive
7 damages. Axel Johnson and SAI were jointly represented by Charles Treat
8 in these negotiations.

9 As was the case with the 1990 Purchase Agreement, the 1992 Settlement
10 Agreement contemplated three possible ways to utilize the PPA to generate
11 income needed to satisfy the promissory notes due Oeberst and Axel
12 Johnson. SAI could develop a project using the PPA in the hopes that the
13 project would generate sufficient revenue to pay the Oeberst notes, or SAI
14 could sell the PPA to a third party hoping that proceeds would be
15 generated to pay the Oeberst notes. SAI could also abandon the PPA, allow
16 Oeberst to acquire it at no cost and Oeberst could then hopefully utilize
17 the PPA in some fashion to earn revenue for its beneficiaries.

18 First, SAI could develop a project. At the time of the settlement,
19 SAI intended to seek further amendment of the PPA and develop a geothermal
20 project located at the Geysers. See Recital S of the Settlement
21 Agreement. Hence, if SAI developed the project and sold energy to PG&E
22 under the PPA, the income generated would be used to pay the notes to
23 Oeberst and Axel Johnson. Although aware of the great potential for
24 income from the project, Axel Johnson again did not request any part of
25 the profits from the sale of energy. No where in the Settlement Agreement
26 is there such a profit-sharing provision. AJED would not be entitled to

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

1 any part of the profits above payment on its \$200,000 note. Such behavior
 2 by AJED is inconsistent with its position that it was trying all along to
 3 realize the inherent value of the PPA. However, this behavior is
 4 consistent with the position that AJED was no longer interested in the PPA
 5 and was only concerned about receiving payment on its \$200,000 note.

6 Second, SAI could sell the PPA. Paragraph 13 allows SAI to sell the
 7 PPA in order to generate revenue to pay the notes. Subsection (a) of
 8 Paragraph 13 of the Settlement Agreement provides that:

9 SAISE may not assign all or substantially all of its interest
 10 in the PG&E Power Agreement without the consent of Archibald
 M. Mull III, which consent shall not be unreasonably withheld.

11 SAI could sell the PPA subject to the consent of Oeberst but the consent
 12 could not be unreasonably withheld. Oeberst wanted control over
 13 disposition of the PPA because the PPA was its only source for the payment
 14 of the \$2.1 million notes.

15 Subsection (b) of paragraph 13 then provides for disbursement of any
 16 net proceeds from a sale of the PPA. Paragraph 13 states in part:

17 (b) In the event that, prior to the Note Due Date SAISE
 18 assigns or otherwise alienates its interest in the PG&E Power
 Agreement in such fashion as to substantially end SAISE's
 19 active involvement in the Project, then the Net Proceeds
 thereof shall be treated as follows:

20 (i) the Net Proceeds first shall be used to pay the
 21 principal amounts and accrued interest on the [Oeberst]
 Notes.... In the event that the Net Proceeds are
 22 insufficient to pay off the Notes in full, the payments
 shall be made pro rata between the two [Oeberst]
 23 Notes....

24 If SAI sells the PPA, then the net proceeds would first go to pay the
 25 Oeberst notes. Nothing in the Settlement Agreement referred to payment
 26 of Axel Johnson's \$200,000 note because the note was only part of a side

1 agreement between SAI and Axel Johnson.

2 In order to protect and secure its \$200,000 note, Axel Johnson
 3 requested that a provision be added to the Amendment Agreement to provide
 4 that if SAI assigns its interest in the PPA, the assignee must agree to
 5 assume the obligations of SAI under the Amendment Agreement, which
 6 obligations include payment of AJED's note. Paragraph 6 of the Amendment
 7 Agreement provides that:

8 In the event that SAISE assigns all or a part of its interest
 9 in the PG&E Power Agreement: (i) SAISE shall assure the
 10 assignee(s) agree to assume the obligations hereunder;
 11 provided, however, that any purported assignment of the
 12 obligations of SAISE hereunder to any person or party to which
 13 SAISE does not also assign the PG&E Power Agreement shall be
 14 null and void and of no effect; and (ii) SAISE shall apply all
 15 Net Proceeds remaining after payments, as defined in and as
 16 required by paragraph 13 of the Settlement Agreement, in
 17 payment of the Note payable to AJED.

18 Axel Johnson contemplated that SAI might sell the PPA. The Amendment
 19 Agreement does not require that SAI receive consent from Axel Johnson for
 20 such a sale. The Amendment Agreement only provides that a sale of the PPA
 21 be subject to the new buyer or assignee being obligated on Axel Johnson's
 22 \$200,000 note. Axel Johnson's request for this added layer of protection
 23 from dilution of SAI's only asset, the PPA, is unnecessary if, as AJED
 24 contends, it had a right to consent to any assignment of the PPA. Any net
 25 proceeds from a sale left over after paying the Oeberst notes would next
 26 be used to pay Axel Johnson's note. The provisions regarding a sale of
 27 the PPA support SAI's contention that AJED did not oppose sale of the PPA
 28 as long as it received payment on its note.

It appears that the parties also believed that once AJED was paid on
 its note, AJED had no other interest in the disposal of the PPA. During

1 the drafting of the 1992 agreements, Treat, who represented both Axel
2 Johnson and SAI, sent a letter dated January 2, 1992 to Bill Reynolds,
3 Barry Flynn, John Flegel and Marc Levinson. Treat outlined what AJED's
4 rights would be if SAI sold the PPA. The letter stated in part:

5 Still speaking as a neutral, I'd like to observe that the
6 chances that this issue will ever become significant are very
7 small. The disputed language would come into play only if SAI
8 gets completely out of the project, and sells out for so much
9 money that there is still some left after paying SAI's out-of-
pocket and paying Archie [Oeberst] off in full - an unlikely
occurrence. Further, if it does happen, the dispute is also
moot if the excess is enough to pay off both the services and
the \$200k note to Axel.

10 The letter clearly states that if SAI sells out for so much money that
11 there is still some left after paying SAI's out-of-pocket expenses and
12 paying Oeberst in full, the dispute is moot because SAI would pay off
13 AJED's \$200,000 note. This confirms that once Axel Johnson was paid, it
14 had no further rights regarding the PPA. Reynolds admitted during the
15 trial that he did not tell anyone that he had any different understanding
16 of AJED's rights than that set forth in Treat's letter. This supports that
17 AJED was only interested in receiving payment on its note, rather than
18 interested in realizing the inherent value of the PPA for itself.

19 Third, SAI could abandon the PPA. Paragraph 6 of the Settlement
20 Agreement provides:

21 In the event that SAISE determines not to proceed with the
22 Project, SAISE agrees to immediately notify Archibald M. Mull
23 III in writing thereof. If such notice is given, or if the
24 Note Due Date shall not have occurred by June 30, 1995, the
25 Oeberst & Associates Holding Trust shall have an option to
26 acquire at no cost from SAISE the PG&E Power Agreement upon
27 demanding assignment thereof, subject to any consent from PG&E
28 or other third parties that may be required for the assignment
thereof.

1 Under Paragraph 6 of the 1992 Settlement Agreement, Oeberst had an option
2 to acquire the PPA at no cost if SAI "determines not to proceed with the
3 Project." This phrase is the same phrase used in Paragraph 6.9 of the
4 1990 Purchase Agreement. The court previously determined that "determines
5 not to proceed with the project" means an abandonment of any effort to
6 generate revenue to pay the Oeberst contingent liability. Now that the
7 Oeberst liability is no longer contingent, the phrase refers to an
8 abandonment of any effort to generate revenue to pay the \$2.1 million
9 Oeberst notes. Thus, if SAI abandons the PPA, Oeberst would have an
10 option to acquire the PPA at no cost. Oeberst wanted to be able to get
11 the PPA back and try to use it in some fashion in order to pay its
12 beneficiaries if SAI did nothing with it. There was no equivalent right
13 given to Axel Johnson in the Settlement Agreement.

14 Furthermore, if, as Axel Johnson contends, the meaning of the phrase
15 includes any decision not to build a power plant, then Oeberst's option
16 would be triggered upon the termination with PG&E. However, Oeberst has
17 never taken such a position because it understood that the parties
18 intended that not proceeding with development of a project meant SAI not
19 doing anything to generate revenue to meet its obligations to Oebe

20 Upon abandonment, Oeberst's option to acquire the PPA at no cost was
21 subject to "any consent from PG&E or other third parties that may be
22 required for the assignment thereof." Axel Johnson contends that it is
23 a third party whose consent was required because it had a right to consent
24 to the assignment of the PPA under Paragraph 6.8 of the 1990 Purchase
25 Agreement. However, Axel Johnson was a signatory to the Settlement
26 Agreement and was never referred to as a "third party" in any of the

1 agreements. Axel Johnson did not inform anyone that it believed it was
2 a third party with consent rights superior to that of Oeberst despite
3 notice of the addition of the provision as a "notable change." Moreover,
4 SAI and Oeberst did not believe or understand the term "other third
5 parties" to include Axel Johnson. Treat, Flegel and Mull all believed the
6 term "other third parties" to refer to regulatory agencies or potential
7 lenders whose approval may be required. Furthermore, Paragraph 13 of the
8 Settlement Agreement already requires Oeberst's consent in order to assign
9 the PPA. Nothing in the 1992 agreements require Axel Johnson's consent
10 to assign the PPA. Moreover, Reynolds told Flegel and Mull that Axel
11 Johnson was "totally out of it" after paying Oeberst \$800,000 in
12 settlement.

13 Thus, if SAI abandoned the PPA, Oeberst's option to get the PPA back
14 at no cost would be triggered. If Oeberst chose to reacquire the PPA, SAI
15 would then assign the PPA to Oeberst subject only to consent from
16 regulatory agencies or potential lenders. Axel Johnson would not have the
17 right to consent to the assignment or have the right to repurchase the
18 PPA. It is clear that if Oeberst knew that Axel Johnson would be claiming
19 a right to consent to Oeberst getting the PPA back, Oeberst would not have
20 signed the Settlement Agreement. If Axel Johnson would be involved at all
21 after the settlement, Oeberst would not have entered into the settlement.
22 Williamson stated "if Axel Johnson was involved in the project from that
23 point [after the Settlement Agreement], I would never sign the contract.
24 We went into that contract to get rid of Axel Johnson."

25 Axel Johnson argues that SAI breached Paragraph 6.8 of 1990 the
26 Purchase Agreement because when it terminated the PPA, it assigned the PPA

1 to PG&E without Axel Johnson's prior written consent. However, based on
2 the evidence and circumstances surrounding the 1992 agreements, the court
3 finds that the parties intended that the Settlement Agreement, which
4 requires Oeberst's consent to assign the PPA, superseded Axel Johnson's
5 consent right under the 1990 Purchase Agreement.

6 If the PPA was terminated and SAI received enough money to pay
7 Oeberst's \$2.1 million in notes and Axel Johnson's \$200,000 note, then the
8 parties had no further rights. Once Oeberst is paid, it has no further
9 rights, and has not claimed any further rights, regarding its option to
10 get the PPA back. Likewise, once Axel Johnson is paid, it also has no
11 further rights regarding the PPA. The intent of the parties after the
12 settlement was to get paid on their promissory notes.

13 In addition, Axel Johnson argues that the Settlement Agreement was
14 not intended to affect the 1990 Purchase Agreement pursuant to Paragraph
15 11 of the Settlement Agreement. Paragraph 11 of the Settlement Agreement
16 provides that nothing in the Settlement Agreement is intended to affect
17 or alter in any way the "status of agreements that the parties may have
18 among themselves." Thus, Axel Johnson argues that its consent rights
19 under Paragraph 6.8 of the 1990 Purchase Agreement could not have been
20 superseded by Oeberst's consent rights under Paragraph 13(a) of the 1992
21 Settlement Agreement. However, such an application of Paragraph 11 to
22 Paragraph 13(a) of the Settlement Agreement goes against the intentions
23 of the parties.

24 A contract must be interpreted as to give effect to the mutual
25 intention of the parties as it existed at the time of contracting so far
26 as it is ascertainable and lawful. California Civil Procedure § 1636

1 (entitled "Mutual intention to be given effect") Also, "repugnancy in a
2 contract must be reconciled, if possible, by such an interpretation as
3 will give some effect to the repugnant clauses, subordinate to the general
4 intent and purpose of the whole contract." California Civil Code § 1652
5 (entitled "Reconcilement of repugnancies"). Particular clauses of a
6 contract are subordinate to its general intent. California Civil Code §
7 1650 (entitled "Particular clauses; general intent").

8 Under the settlement, Axel Johnson was released from any further
9 liability to Oeberst once it paid \$800,000 to Oeberst. Once the settlement
10 was finalized, the general intent of the parties was for Oeberst to get
11 paid on its \$2.1 million notes and for Axel Johnson to get paid on its
12 \$200,000 note. There was no reason to, and Axel Johnson did not, retain
13 any further rights regarding the PPA. Thus, the Settlement Agreement did
14 supersede Paragraph 6.8 despite the language of Paragraph 11.

15 **III. CONCLUSION**

16 Based on the intentions of the parties as evidenced by the
17 circumstances at the time the agreements were entered into, the court
18 finds that SAI did not make a determination not to proceed with the
19 project with respect to the PPA and thus did not breach Paragraph 6.9 of
20 the 1990 Purchase Agreement. In addition, the court finds that Axel
21 Johnson's consent rights were superseded by Oeberst's consent rights under
22 the 1992 Settlement Agreement and thus SAI did not breach Paragraph 6.8
23 of the 1990 Purchase Agreement. Therefore, Axel Johnson has not
24 established the validity of its claim by a preponderance of the evidence.
25 Based on the foregoing, SAI's objection to Axel Johnson's \$6 million claim
26 is sustained. The statements in this order shall constitute findings of

27 **ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.**

UNITED STATES BANKRUPTCY COURT
For The Northern District Of California

1 fact and conclusions of law pursuant to Federal Rule of Bankruptcy
2 Procedure 7052.

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ORDER SUSTAINING SAI'S OBJECTION TO CLAIM FILED BY AXEL JOHNSON ENERGY DEVELOPMENT, INC.

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