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DEC 28 2005

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U.S. BKCY. APP. PANEL
OF THE NINTH CIRCUIT

NOT FOR PUBLICATION

UNITED STATES BANKRUPTCY APPELLATE PANEL

OF THE NINTH CIRCUIT

In re: PACIFIC GAS AND ELECTRIC CO., Debtor. _____ MODESTO IRRIGATION DISTRICT, Appellant, v. PACIFIC GAS AND ELECTRIC CO., Appellee. _____	BAP No. NC-04-1574-MaMcB Bk. No. 01-30923-DM **M E M O R A N D U M**[1]

Argued and Submitted on September 28, 2005
at Pasadena, California

Filed - December 28, 2005

Appeal from the United States Bankruptcy Court
for the Northern District of California

Honorable Dennis Montali, Bankruptcy Judge, Presiding.

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Before: MARLAR, McMANUS[2] and BRANDT, Bankruptcy Judges.

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[1] This disposition is not appropriate for publication and may not be cited to or by the courts of this circuit except when relevant under the doctrines of law of the case, res judicata, or collateral estoppel. See 9th Cir. BAP Rule 8013.

[2] Hon. Michael S. McManus, Chief Bankruptcy Judge for the Eastern District of California, sitting by designation.

INTRODUCTION

In a contested claim allowance proceeding, the appellant contended that it was owed about $6 million in legislatively approved charges from the debtor utility under contracts it had entered into with the debtor's former customers. The bankruptcy court determined that the contracts did not provide for such a claim and rejected the appellant's offer of parol evidence to prove otherwise. The bankruptcy court disallowed that portion of the claim for lack of standing, and this appeal ensued. We conclude that the bankruptcy court did not err in interpreting the contracts and AFFIRM.

FACTS

Debtor, Pacific Gas and Electric Company ("PG&E"), filed for bankruptcy protection under chapter 11[3] on April 6, 2001. The effective date of the plan of reorganization was April 12, 2004. Modesto Irrigation District ("MID") filed a proof of claim in the amount of more than $89,000,000. This proof of claim had several components, one being MID's claim for negative Competition Transition Charges ("CTCs") in the amount of $10,104,226, which was subsequently reduced to $6,652,288. This is the only portion of the claim at issue in this appeal.

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[3] Unless otherwise indicated, all "chapter" and "section" references are to the Bankruptcy Code prior to its amendment by the Bankruptcy Abuse Prevention and Consumer Protection Act of 2005 ("BAPCPA"), 11 U.S.C. §§ 101-1330. "Rule" references are to the Federal Rules of Bankruptcy Procedure ("Fed. R. Bankr. P."), Rules 1001-9036.

CTCs were enacted by the California legislature when it deregulated the energy market. These charges allow electric utilities to recover costs of energy generation-related assets that had previously been included in the rates, but which might not otherwise be recoverable in a competitive market. These charges were computed by deducting the cost of power from the generation rate. There would be a positive CTC when the market rate cost was less than the cost of generating power with the utility's pre-regulation assets, thereby allowing the utility to recover from its customers some of the money it was losing. While it was not generally contemplated as a possibility, there would be a negative number when the utility could produce the power with its own pre-regulation assets cheaper than the market rate. This issue has not yet been addressed in a court of law, and it has not been determined whether the electric utilities are liable, back to their customers, when there is a negative CTC. We need not, and do not, decide that question here.

MID entered into contracts with certain former customers of PG&E, offering to provide them power at a cheaper cost. In those contracts, as an inducement to switch utilities, MID assumed the customer's CTC liability <u>to</u> PG&E:

> MID agrees to bear the responsibility for any CTC which Applicant may owe to Pacific Gas and Electric Company, accruing during the period beginning at the commencement of service hereunder, through December 31, 1998, arising out of and directly attributable to Applicant's receipt of electric service pursuant to this Agreement.

Agreement for Electrical Service (August 28, 1998), p. 2, ¶ 4.

> . . . MID agrees to assume the financial responsibility for any increase in costs, obligations or charges to Applicant attributable to the inability to fully apply

> such CTC exemptions, as described in the preceding paragraph, to Applicant.

Agreement for Electrical Service (July 27, 1999), p. 2, ¶ 6.

The contracts between MID and PG&E's former customers did not mention what would happen if the CTCs ever became negative. In fact, MID has conceded that at the time of contracting the parties "anticipated that the CTCs would always be positive." See Appellant's Opening Brief (Feb. 23, 2005), p. 6. However, MID's $6,652,288 claim is for negative CTCs.

PG&E objected to MID's claim to negative CTCs on the grounds of lack of legal basis and lack of standing, because the customer contracts did not explicitly assign the negative CTCs to MID.

MID contended that the right to such beneficial negative CTCs was implicitly assigned to it from the customers and that it was entitled to collect such amounts from PG&E. Although the contracts did not expressly address negative CTCs, MID offered to present evidence that the parties' intent was to assign any right to negative CTCs to MID. It proposed to do this through testimony or declarations of customers and MID employees.

The bankruptcy court sustained PG&E's objection to the introduction of such extrinsic evidence, in its memorandum decision dated October 19, 2004, and disallowed MID's claim, concluding that MID lacked standing to file a claim for negative CTCs because the contracts did not make any such assignments. The final judgment was entered on November 12, 2004.

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ISSUES

1. Whether the bankruptcy court erred in excluding extrinsic evidence concerning the treatment of negative CTCs between MID and its customers.

2. Whether the bankruptcy court erred in holding that MID lacked standing to file a claim against PG&E for negative CTCs.

STANDARDS OF REVIEW

On appeal, questions of law are reviewed de novo, United States v. Wyle (In re Pac. Far East Lines, Inc.), 889 F.2d 242, 245 (9th Cir. 1989), and findings of fact are reviewed under the clearly erroneous standard. Ankeny v. Meyer (In re Ankeny), 184 B.R. 64, 68 (9th Cir. BAP 1995); Fed. R. Bankr. P. 8013. To the extent questions of fact cannot be separated from questions of law, they will be reviewed as mixed questions of law and fact under a de novo review. Ratanasen v. Cal., Dep't of Health Servs., 11 F.3d 1467, 1469 (9th Cir. 1993). Contract enforcement and interpretation are questions of law, which we review de novo. Ankeny, 184 B.R. at 68.

We may affirm on any basis supported by the record. O'Rourke v. Seaboard Surety Co. (In re E.R. Fegert, Inc.), 887 F.2d 955, 957 (9th Cir. 1989).

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DISCUSSION

A. Parol Evidence Rule

Under California law, a written contract supersedes all prior and contemporaneous agreements concerning the same subject matter, and if "the writing is intended by the parties as the final expression of their agreement," it cannot be contradicted by parol evidence. See Cal. Civ. Proc. Code § 1856(a); Cal. Civ. Code § 1625. See also Ankeny, 184 B.R. at 70; Casa Herrera, Inc. v. Beydoun, 32 Cal. 4th 336, 343, 83 P.3d 497, 502, 9 Cal. Rptr. 3d 97, 102 (2004). The intent of the parties should be ascertained from the writing alone whenever possible. See Cal. Civ. Code § 1639; United States Cellular Inv. Co. of Los Angeles v. GTE Mobilnet, Inc., 281 F.3d 929, 934 (9th Cir. 2002). However, extrinsic or parol evidence may be admitted for a few exceptions, such as for "consistent additional terms," "mistake or imperfection," and "extrinsic ambiguity." Cal. Civ. Proc. Code § 1856(b), (e) and (g).

1. MID Offered Inconsistent, Additional Terms to an Integrated Contract

MID argues that its proffered evidence should have been considered under Cal. Civ. Proc. Code § 1856(b), which allows extrinsic evidence to prove "consistent additional terms unless the writing is intended also as a complete and exclusive statement of the terms of the agreement." In other words, extrinsic or parol evidence will only be admitted where the written agreement was not intended to be the complete and final agreement and where

the additional terms are consistent with the written agreement.

Whether or not a contract is considered to be a final expression of the agreement, or a fully integrated contract, is a question of law which is reviewed de novo. Ankeny, 184 B.R. at 70; Sullivan v. Mass. Mut. Life Ins. Co., 611 F.2d 261, 264 (9th Cir. 1979). A written contract is considered to be the complete and final agreement where the parties intended a writing to be the sole and exclusive embodiment of the agreement. See Ankeny, 184 B.R. at 70. In determining whether a contract is fully integrated, a court should consider: "(1) whether the written agreement appears to state a complete agreement; (2) whether the alleged oral agreement directly contradicts the writing; (3) whether the oral agreement might naturally be made as a separate agreement; and (4) whether a jury might be misled by the introduction of the offered parol evidence." Id. at 70-71 (citing Sullivan, 611 F.2d at 264).

Addressing each in order, we note first that the subject written contracts appear to contain complete agreements. These contracts were written by sophisticated parties and define all the basics of the entire relationship. As the bankruptcy court pointed out, the contracts address the electric service to be provided by MID, the date of commencement, the rate schedule, rights of way and easements, and even the assumption of CTC obligations and application for CTC exemptions. MID argues that these contracts are not the complete agreements because they did not cover all the subjects other contracts cover. While there may be some details or hypothetical possibilities which are not addressed in the MID contracts, they sufficiently covered who the

parties are and the extent of their obligations, duties and relationships. No contract can cover every possible scenario. That fact, however, does not make them ambiguous or incomplete.

Second, the oral testimony which MID proffered would have directly contradicted the written agreements. Concerning CTCs, the written agreements state that "MID agrees to assume the financial responsibility for any increase in costs, obligations or charges" and "MID agrees to bear the responsibility for any CTC which Applicant may owe to Pacific Gas and Electric" (emphasis supplied). The bankruptcy court found that the purpose of these provisions was to attract customers, and that an assignment of the right to collect negative CTCs would be a disincentive. This factual finding by the bankruptcy court was not clearly erroneous. It established that any assignment of negative CTCs was inconsistent with, and missing from, the written agreements when it could have been easily inserted into the terms.

Third, the terms contained in the testimony which MID proffered would not logically be contained in a separate agreement and, thus, would add terms significantly changing the written agreement based upon a subsequent condition that was not contemplated when the agreement was entered into. Therefore, any assignment of so-called negative CTCs should have been reasonably addressed in the written contracts, not in separate ones.

Fourth, since there are no juries in straight claims objections in bankruptcy court, the fourth requirement is inapplicable.

MID also argues that these contracts are deserving of parol evidence because they do not contain "integration clauses." While

an integration clause may be a factor in determining whether a contract is fully integrated, it is not the only factor, Sicor Ltd. v. Cetus Corp., 51 F.3d 848, 859 (9th Cir. 1995), nor is it a necessary factor, Software Design and Application, Ltd. v. Price Waterhouse, LLP, 49 Cal. App. 4th 464, 470, 57 Cal. Rptr. 2d 36, 39 (1996).

Further, even if the contracts were not fully integrated, the evidence which MID sought to admit was inconsistent with the terms in the MID contracts. Extrinsic evidence cannot vary, add to or alter the written terms of an agreement. Ankeny, 184 B.R. at 70; Pac. Gas & Elec. Co. v. G.W. Thomas Drayage & Rigging Co., 69 Cal. 2d 33, 39, 442 P.2d 641, 645, 69 Cal. Rptr. 561, 565, (1968). Here, the evidence MID sought to present would have clearly altered and added terms to the written agreement. Importantly, MID admitted that negative CTCs were not contemplated at the time of the written agreements. Thus, including an assignment of negative CTCs now would be inconsistent with the contracts' original meaning.

In summary, the bankruptcy court was correct in holding that the MID contracts were fully integrated contracts and the parties intended such agreements to be the exclusive agreements between them. Therefore, the bankruptcy court correctly denied the extrinsic evidence because the contracts were fully integrated and the proferred terms would not add consistent additional terms.

2. The Contract Terms Were Not Ambiguous

MID also argues that extrinsic evidence should have been

admitted to clarify ambiguities. Cal. Civ. Proc. Code § 1856(g) states in relevant part: "(g) [t]his section does not exclude other evidence of the circumstances under which the agreement was made or to which it relates ... or to explain an extrinsic ambiguity or otherwise interpret the terms of the agreement . . . ." The determination of whether there are ambiguities in a written contract is a question of law which is reviewed de novo. Ankeny, 184 B.R. at 70.

MID argues that courts should follow a two-step process to determine ambiguities in written contracts. Winet v. Price, 4 Cal. App. 4th 1159, 1165; 6 Cal. Rptr. 2d 554, 557 (1992). MID maintains that the court should first provisionally receive the evidence to determine if there are any ambiguities or "whether the language is 'reasonably susceptible' to the interpretation urged," and then actually admit the extrinsic evidence if it finds that there were ambiguities. Id.; see also Pac. State Bank v. Greene, 110 Cal. App. 4th 375, 386, 1 Cal. Rptr. 3d 739, 747 (2003).

Concerning the first step, "[t]he test of admissibility of extrinsic evidence to explain the meaning of a written instrument is not whether it appears to the court to be plain and unambiguous on its face, but whether the offered evidence is relevant to prove a meaning to which the language of the instrument is reasonably susceptible." So. Pac. Transp. Co. v. Santa Fe Pac. Pipelines, Inc., 74 Cal. App. 4th 1232, 1241, 88 Cal. Rptr. 2d 777, 783 (1999) (quoting Pac. Gas & Elec., 69 Cal. 2d at 37, 442 P.2d at 644, 69 Cal. Rptr. at 564). Thus, while a court is not to determine the admissibility of parol evidence on its own view of whether the written contract seems plain and unambiguous, the

determination is correctly made by considering the relevance of the evidence and whether the written language is even "reasonably susceptible" to the proposed meaning.

So. Pac. Transp. involved a dispute concerning the determination of a rent increase. The written agreement provided that it would be determined "in accordance with the fair market value of the easement." So. Pac. Transp., 74 Cal. App. 4th at 1236, 88 Cal. Rptr. 2d at 780. Such language is distinguishable from the language in the MID contracts. The parties in So. Pac. Transp. legitimately disputed the specific methodology used to determine the fair market value. The court was required to apply custom, usage and course of dealing to determine the fair market value. Extrinsic evidence had to be used in order to give effect to the parties' intentions regarding valuation. Id., 74 Cal. App. 4th at 1240, 88 Cal. Rptr. 2d at 782.

In contrast here the MID contracts state nothing concerning negative CTCs or any assignments of them. There is no ambiguous language, nor is there any language that is "reasonably susceptible" to an inference that the customers assigned unanticipated negative CTC rights to MID. Thus, the bankruptcy court, even after provisionally considering the proferred evidence, was correct in rejecting it because the contract language was not ambiguous.

Pac. Gas & Elec. concerned a dispute over the interpretation and coverage of an indemnity clause. Pac. Gas & Elec., 69 Cal. 2d at 35, 442 P.2d at 642, 69 Cal. Rptr. at 563. The offered parol evidence concerned circumstances that would give possible different meanings to words in the written agreement. The court

in Pac. Gas & Elec. relied on the principle that the "parties' understanding of the words used may have differed from the judge's understanding." Id., 69 Cal. 2d at 39, 442 P.2d at 645, 69 Cal. Rptr. at 565. The court held that there should be a "preliminary consideration of all credible evidence" to help place the court in the same situation of the parties for the purpose of determining whether the written agreement was reasonably susceptible to the posited interpretation. Id.

Pac. Gas & Elec. is also distinguishable from our case because MID was not urging the court to adopt a new interpretation of any words or phrases, but instead to add new and different clauses and thus vary the terms of the existing contracts, upon which point the existing contracts are "deafeningly silent"!

The rule is, then, that there must be some language in the contract that is reasonably susceptible to a meaning urged by a party. See Casa Herrera, 32 Cal. 4th at 343, 83 P.3d at 503, 9 Cal. Rptr. 3d at 103 (extrinsic evidence as to new terms was irrelevant as a matter of law). Otherwise, anyone could claim "ambiguity" in a contract and all extrinsic evidence would have to be considered - at least provisionally. This would, in effect, bury the parol evidence rule. Extrinsic evidence to explain the meaning of a written instrument should be excluded only when it is "feasible to determine the meaning the parties gave to the words from the instrument alone." Pac. Gas & Elec., 69 Cal. 2d at 38, 442 P.2d at 644, 69 Cal. Rptr. at 564. Here, the meaning of the words in the MID contracts are not disputed and the parties' full intent can be determined from the writing alone. As the contracts state: "MID agrees to assume the financial responsibility for any

increase in costs, obligations or charges" and "MID agrees to bear the responsibility for any CTC which Applicant may owe to Pacific Gas and Electric" (emphasis supplied). Nothing in these provisions is reasonably susceptible to a meaning that the customers assigned any benefit due to them, or even gave a thought to any "right" concerning what they now call "negative CTCs."

MID additionally argues that the contracts are ambiguous because they do not have standard indemnification clauses, do not address negative CTCs, and are not similar to the examples in Cal. Legal Forms published by Matthew Bender. However, these are not ambiguities. There was simply no assignment of negative CTCs. Since they were not mentioned, any such right would remain with the customers. Further, MID can only fault itself for not having contracts as thorough as those found in Cal. Legal Forms, but that oversight does not create an ambiguity.

Cal. Civ. Proc. Code § 1856(g) allows parol evidence to assist in interpreting ambiguities, not to add or alter the written agreement. Ankeny, 184 B.R. at 72; Casa Herrera, 32 Cal. 4th at 343, 83 P.3d at 503, 9 Cal. Rptr. 3d at 103; Pac. Gas & Elec., 69 Cal. 2d at 39, 442 P.2d at 645, 69 Cal. Rptr. at 565. "[S]uch evidence cannot serve to create or alter the obligations" of the parties. Casa Hererra, 32 Cal. 4th at 344, 83 P.3d at 503, 9 Cal. Rptr. 3d at 103 (citation omitted).

Also, in its determination of whether or not an ambiguity was present, the bankruptcy court assumed that the proffered evidence would show that the parties intended to assign MID the right to negative CTCs and that such testimony was credible. The bankruptcy court concluded, nonetheless, that it was inadmissible

because it constituted incompetent evidence of "undisclosed subjective intent." See Price, 4 Cal. App. 4th at 1166 n.3, 6 Cal. Rptr. 2d at 558 n.3.

MID contends that even undisclosed intentions must be considered, citing Pac. Gas & Elec. Co. v. Zuckerman, 189 Cal. App. 3d 1113, 234 Cal. Rptr. 630 (1987). MID misreads Zuckerman, a case in which the proferred extrinsic evidence was "not a mere undisclosed subjective intent" but was about correspondence and discussion between both parties "as to what the contract was supposed to be about." Id., 189 Cal. App. 3d at 1140, 1141-42, 234 Cal. Rptr. at 647, 648 (emphasis added).

Here, MID admitted several times that the parties did not discuss or even contemplate negative CTCs at the time they entered into the contracts. Thus, the bankruptcy court's assumption was negated by MID's own admission. MID offered evidence that was prohibited by the rule against undisclosed intention, which prevents a party from "saying one thing but meaning another." Id. at 1141.

In summary, MID was not requesting clarification, but rather was attempting to add to and alter the written agreement. Therefore, the bankruptcy court did not err in refusing to admit the parol evidence which was offered to clarify only manufactured ambiguities.

3. MID Did Not Prove Mutual Mistake

MID also argues that the extrinsic evidence should have been admitted under Cal. Civ. Proc. Code § 1856(e), which states,

"[w]here a mistake or imperfection of the writing is put in issue by the pleadings, this section does not exclude evidence relevant to that issue."

The bankruptcy court considered this to be a reformation request, and then held that it would not reform a contract where there was no motion for reformation and where an affected individual or entity was not a party to the contested claim objection proceeding, i.e., the customers.

California law provides a remedy of reformation "to effectuate the common intention of both parties which was incorrectly reduced to writing." Bailard v. Marden, 36 Cal. 2d 703, 708, 227 P.2d 10, 13 (1951). The relevant statute provides:

> WHEN CONTRACT MAY BE REVISED. When, through fraud or a mutual mistake of the parties, or a mistake of one party, which the other at the time knew or suspected, a written contract does not truly express the intention of the parties, it may be revised on the application of a party aggrieved, so as to express that intention, so far as it can be done without prejudice to rights acquired by third persons, in good faith and for value.

Cal. Civ. Code § 3399.

MID argues that § 1856(e) does not require a motion for reformation or for affected individuals to be parties in the contested matter, citing Hess v. Ford Motor Co., 27 Cal. 4th 516, 41 P.3d 46, 117 Cal. Rptr. 2d 220 (2002).

In Hess, the injured party in an automobile accident and the tortfeasor's insurer signed a boilerplate release which included the release of third parties. Later, the injured party filed a lawsuit against the car manufacturer, Ford. Ford then asserted a third-party beneficiary claim to enforce the contract. In a separate lawsuit, the injured party then sued the driver and

insurer for reformation of the release contending that the parties did not intend to release Ford. The court granted reformation and entered a judgment striking the offensive language. The injured party then alleged mutual mistake as a defense to Ford's claim in the first lawsuit, and he prevailed by presenting both extrinsic evidence and the reformation judgment.

In our case, MID did not file an action for reformation, but alleged mutual mistake as a defense to PG&E's assertion that it lacked standing under the contract. See Hess, 27 Cal. 4th at 525, 41 P.3d at 52, 117 Cal. Rptr. 2d at 227 (a party raising mutual mistake as a defense to enforcement of onerous terms does not have to ask for a reformation). Under state law, however, MID was required to prove by clear and convincing evidence that the contracting parties actually agreed to assign to MID the customers' alleged negative CTC rights. See Bank of Am. Nat'l Trust & Sav. Ass'n v. Craig, 193 Cal. App. 2d 281, 286, 14 Cal. Rptr. 476, 480 (1961); Moore v. Vandermast, Inc., 19 Cal. 2d 94, 96-97, 119 P.2d 129 (1941).

In Hess, the court allowed extrinsic evidence of the parties' settlement negotiations to show that the injured party had expressed his intention to sue Ford and would not have signed the release without retaining that right of action. Such evidence of the parties' "disclosed" intentions was relevant to a determination of mutual mistake, the court found. Hess, 27 Cal. 4th at 528. This decision comports with the contract law principle that "[t]he true intent of a contracting party is irrelevant if it remains unexpressed." Shaw v. Regents of Univ. of Cal., 58 Cal. App. 4th 44, 55, 67 Cal. Rptr. 2d 850 (1997).

In contrast, MID could not meet its burden of proof because it conceded that no mutual intent to assign negative CTCs was expressed or disclosed by the parties at the time of contracting. MID's offer of parol evidence to show that the contract terms nonetheless encompassed a continuum of charges, both positive and negative, was therefore irrelevant, and the bankruptcy court properly refused to admit it.

Finally, it was undisputed, and the bankruptcy court's finding has not been challenged, that the contracts were incentives to attract customers by relieving them of charges due to positive CTCs. An interpretation of the contracts as assigning to MID the customers' rights to claim negative CTCs would be a prohibited rewriting of the contracts. Hess held that the court "has no power to make new contracts for the parties . . . . Rather, the court may only reform the writing to conform with the mutual understanding of the parties at the time they entered into it, if such an understanding exists." Hess, 27 Cal. 4th at 524, 41 P.3d at 52, 117 Cal. Rptr. 2d at 226-227.

In summary, the bankruptcy court did not err in rejecting MID's offer of parol evidence to prove mutual mistake and reform the contracts.

B. Plain Meaning

Contract terms are to be given their plain meaning whenever possible. Pac. Gas & Elec., 69 Cal. 2d at 39, 442 P.2d at 645, 69 Cal. Rptr. at 565. Here, the contracts' language was clear and unambiguous. They contained no assignment of negative CTCs.

Concerning CTCs, the MID contracts only stated that MID would "bear the responsibility for any CTC which Applicant may owe" and "assume the financial responsibility for any increase in costs, obligations or charges to Applicant." According to the plain language of the contracts, there was never any assignment of negative CTCs, and MID therefore held no such interest and thus lacked standing to bring this claim against the estate. That right belonged, and still does belong, solely to the customers themselves, those that owned the right in the first place.

CONCLUSION

MID's extrinsic evidence to support a claim for negative CTCs was inadmissible because: (1) it was an attempt to add new and inconsistent terms to an integrated contract; (2) the proffered language was not reasonably susceptible to an ambiguity; and (3) there was insufficient admissible evidence of a mutual mistake and supplying new terms of assignment of negative CTCs would have been the making of new contracts for the parties, which the bankruptcy court could not do.

MID's claim was properly disallowed because there was no such assignment made in the agreements and MID therefore lacked standing to bring such a claim.

AFFIRMED.