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**Attorneys for Tongue River Electric Cooperative, Inc.**

**IN THE UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF MONTANA**

**In Re:** ) **Case No. 11-62031-RBK**  
)  
**SOUTHERN MONTANA ELECTRIC** ) **Notice of Hearing**  
**GENERATION and TRANSMISSION** ) **Date: September 24, 2013**  
**COOPERATIVE, INC.** ) **Time: 1:30 p.m.**  
) **Location: Federal Courthouse**  
**Debtor.** ) **2601 Second Ave North**  
) **Billings, Montana**  
)

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**TONGUE RIVER ELECTRIC’S OBJECTIONS TO  
TRUSTEE’S DISCLOSURE STATEMENT**  
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Tongue River Electric Cooperative, Inc. (“Tongue River”) through counsel, objects to the Disclosure Statement filed by the Chapter 11 Trustee herein on September 12, 2013 (“Disclosure Statement”) on the following grounds.

**Lack of Adequate Information to Make Informed Judgment About Plan**

The Disclosure Statement does not provide Tongue River or any other creditor with sufficiently definite factual information in order to evaluate the Trustee’s Second Amended Chapter 11 Plan of Reorganization dated September 12, 2013 (the “Plan”) for Debtor Southern Montana Electric Generation and Transmission Cooperative, Inc. (“Southern” or “Debtor”) or make a decision on whether to accept or reject the Plan. Accordingly, the Disclosure Statement does not satisfy the requirements of 11 U.S.C. § 1125.

As discussed below, the Disclosure Statement fails to satisfy the basic requirements applied by bankruptcy courts for information on numerous mandatory categories. The Disclosure Statement fails to explain the pre- and post-petition deteriorated relationship between Southern and its members, fails to provide necessary information about valuation of estate property, fails to provide adequate information about the Plan's proposed assumption of executory contracts that are the essence of the Plan, fails to explain future governance and management of Southern, fails to provide adequate information about future litigation, avoidance actions or disputed claims, fails to adequately discuss the absolute priority rule and the unfair discrimination rules and how the Plan fails to comply with those rules, fails to explain the treatment given to executory contract holders and how the plan violates bankruptcy law with respect to executory contracts.

**Failure to Satisfy *In Re Metrocraft* Standards**

In the case of *In Re Reilly*, 4 Mont. B. R., 150, 153-154 (1987), this Court recognized the criteria established in *In Re Metrocraft Pub. Service Inc.*, 39 B.R. 567, 568 (Bankr. N.D. Ga. 1984), for the requirements of an adequate disclosure statement. See also, *In Re Cardinal Congregate I*, 121 B.R. 760 (Bankr. S.D. Ohio 1990)

Of the nineteen types of information identified in *In Re Metrocraft* to be included in a disclosure statement, the Disclosure Statement fails to provide adequate information as required by 11 U.S.C. §1125(a)(1) on at least eleven of these items:

**Events Leading to the Filing of the Bankruptcy Petition.**

The Disclosure Statement provides little information about the extent that the litigation filed by Yellowstone Valley Electric Cooperative ("YVEC"), the City of Great Falls/Electric City Power, and the Billings Gazette against Southern contributed to the filing of Southern's bankruptcy. There is no discussion of the deadlock that existed on Southern's Board of Trustees prior to Southern's bankruptcy filing. There is no discussion of the dissension and deadlock

created in Southern when Beartooth elected a new trustee to Southern's Board of Trustees and Southern's Board refused to seat her due to contentions that she would not honor Southern's confidentiality obligations. These were precipitating matters, occurring immediately prior Southern's bankruptcy filing, and are necessary to creditors' understanding of the untenable relationships present at Southern today.

**Description of Available Assets and Their Value.**

The Disclosure Statement provides little or no information about the value of Southern's assets at confirmation. The Trustee filed a Motion for Valuation of Security on April 19, 2013 [Dkt. 816] seeking a determination of the value of the collateral of U.S. Bank as Indenture Trustee and the Noteholders (collectively "Prudential"). Prudential's collateral security consists of a mortgage on the Highwood Generating Station ("HGS") and security interests in Southern's interest in wholesale power contracts between Southern and its members ("WPC's") (HGS and WPC's are collectively referred to as "Prudential Collateral").

The Chapter 11 Trustee initially asserted that the value of HGS was \$5,600,000; and, that Southern's rights under the WPC's had no fair market value. In support of these values, the Trustee filed a corresponding appraisal of HGS by MR Valuation and a valuation of the WPC contract rights by Harper Hofer & Associates. On June 24, 2013, the Trustee provided an updated expert report from MR Valuation appraising HGS at \$14,398,000 in an orderly liquidation. On June 27, 2013, the Trustee provided an additional report from MR Valuation appraising the fair market value of HGS at \$1,818,000.

On June 27, 2013, Prudential provided an expert report prepared by Alvarez & Marsal Valuation Services, LLC stating an appraised value of HGS between \$7,400,000 and \$16,500,000; and, the intrinsic value of the WPC's at \$125,700,000. Prudential also apparently asserts a security interest in Southern's WAPA Contracts which Alvarez & Marsal valued at \$7,200,000.

Hearing on the Motion for Valuation was scheduled for July 29, 2013. On June 28, 2013, the Trustee filed a Motion to Adjourn the valuation hearing and vacate the related scheduling order on the grounds that he had reached a settlement with Prudential. [Dkt 918] The Trustee's Motion to Adjourn states that the issues of valuation of the Prudential Collateral and the limited objection to the Prudential Proof of Claim (both of which objections were joined in by other parties in interest including Tongue River, Fergus and Mid-Yellowstone) would be reserved until hearing on confirmation of an amended plan of reorganization to be prepared by the Trustee and the Noteholders. On July 1, 2013, the Court granted the Trustee's Motion to Adjourn. [Dkt 922]

The only explanation of the value of the Prudential Collateral contained in the Disclosure Statement is in the Liquidation Analysis which shows the value of HGS at \$14,398,000 and shows no value for the WPC's. The Disclosure Statement should state the value of the Prudential Collateral so that creditors can determine whether the Trustee's proposed treatment of the Prudential Allowed Secured Claim is appropriate.

**Anticipated Future of the Reorganized Company.**

There are four remaining members in Southern - Tongue River, Mid-Yellowstone Electric Cooperative, Inc. ("Mid-Yellowstone"), Fergus Electric Cooperative, Inc. ("Fergus") and Beartooth Electric Cooperative, Inc. ("Beartooth") (collectively the "Members").

The Disclosure Statement lacks information about the management, finances and operations of a reorganized Southern. One criteria for confirmation of a plan of reorganization under 11 UCS §1129(a)(11) is that confirmation is not likely to be followed by liquidation or need for further financial reorganization of the debtor. The Disclosure Statement contains no discussion of: 1) the willingness or unwillingness of the Members to continue in their membership and WPCs with Southern; 2) dissension among the Members and their rural electric members/customers regarding retail electric rates; 3) disagreement among the Members regarding retention or disposal

of HGS; or, 4) the effect of any Member's bankruptcy filing on Southern's Plan and proposed reorganization.

Section IV. X. of the Disclosure Statement recognizes that "several" of the Members joined in the Unsecured Creditors Committee's Motion to Convert the Southern bankruptcy case to Chapter 7. However, there is no discussion of the effect of the Members' contentious relationship with Southern or their willingness to have Southern continue as a Montana rural electric cooperative. Similarly, although Section III.B.8, describes the 43.7% increase in Southern's rates charged to its Members between January 1, 2009 and June 2011, there is no discussion of the effect of these rate increases on the viability of a reorganization by Southern or their effect on the Members' customers' electricity prices.

In order for creditors to make a knowledgeable decision about voting on the Chapter 11 Plan, they must have information about the expected future of Southern as a result of the reorganization.

#### **Source of Information Provided in Disclosure Statement**

The Disclosure Statement does not discuss the source(s) of information provided therein. The Trustee's Motion to Adjourn Hearing [Dkt 918] states that the Trustee and the Noteholders will prepare a plan and disclosure statement. The Disclosure Statement should describe what role and what information therein is provided by Prudential and the firm of Alvarez & Marsal.

#### **Present Condition of the Debtor While in Chapter 11.**

As discussed above, the Disclosure Statement provides no information about the current relationship of the Members with Southern or their willingness to support reorganization.

The Disclosure Statement provides little or no information about the status or viability of Southern's primary asset - HGS. There is no information about the current condition of HGS; what expenditures are necessary to make it full operational under various start times; HGS's

history of operation since the Southern bankruptcy was filed; the cost of retaining and running HGS; HGS property taxes; what spare parts and service agreements are needed and their cost; what upgrades and repairs are needed and their cost; the presence of any deferred maintenance; or, the likelihood or cost of making HGS usable for wind power firming, backup generation or tolling.

There is no discussion of Southern's ability post-confirmation to afford or finance major repairs or expenses related to HGS. The valuations of HGS submitted by the Trustee and Prudential for the Motion for Valuation hearing reflect serious depreciation - from a loan of \$85,000,000, to a cost of construction of about \$68,000,000, to the Trustee's fair market value of \$1,118,000. However, there is no discussion or explanation of the reasons for this depreciation or the likely continuation of such depreciation.

The Disclosure Statement does not inform creditors whether any post petition claims have been threatened or asserted against Southern or persons associated with Southern.

There is no discussion of the effect of the loss of the loads of YVEC and the City of Great Falls/ECP on Southern's current or future financial condition.

There is no discussion of the failure of negotiations between the Members and Prudential. Similarly there is no discussion that the Members did not participate in the negotiations and the settlement reached between the Trustee and Prudential.

Adequate information regarding Southern's present condition should include discussion of the continued dysfunction and dissension among Southern's Members and their trustees post-petition; including their deadlock at the only post-petition annual meeting held of Southern's Board of Trustees.

#### **Future Management of the Reorganized Company.**

The Disclosure Statement provides little information about future management. Section V.C.5 of the Disclosure Statement, at page 52, identifies the current Trustees of Southern, but

provides no explanation of their role in management of Southern. The Disclosure Statement does not disclose that at least five trustees are required for a board of trustees under § 35-18-311 of the Montana Rural Electric and Telephone Cooperative Act.

Section V.F. of the Disclosure Statement, at page 57, states “[T]he Trustee shall continue to serve as the representative of the Estate and the Estate shall continue in existence from and after the Confirmation Date and until all payments and distributions to holders of Allowed Claims under the Plan have been mad under the Plan ...”. There is no disclosure or discussion of the relative roles of the Southern Board of Trustees and the Chapter 11 Trustee of the Estate who apparently will continue to act for at least 12 years.

Section V.C.4 of the Disclosure Statement states that Southern’s Articles of Incorporation and Bylaws will be amended and restated in the form of “Corporate Governance Agreements” to be included in the “Plan Supplement”. The terms and provisions of these amendments and the process for approval must be explained. Does the Plan intend to impose amendments to Southern’s corporate governance documents without approval of its Members? The “Corporate Governance Agreements” are not provided or explained. Understanding the future governance of Southern is critical to adequate disclosure regarding its management. Creditors should not be expected to vote on the Plan without information about future management.

The Members were advised by email on September 13, 2013, that the Trustee had selected a new general manager for Southern. There is no explanation of the need for a general manager or his role, compensation, and terms of employment. There is no disclosure that Southern’s Members and Board of Trustees did not participate in the selection of the general manager.

**Estimated Administrative Expenses.**

There is presently litigation pending between Southern and its Members and between Southern and the HGS construction lien claimants. The Trustee’s Plan would assume the

Southern Members' WPC's without their consent; and impose a Plan on Southern's Members against their will, depriving them even of a right to vote. This will result in significant additional litigation expenses that are all ultimately borne by the Members. What is the estimated expense of this litigation for the Trustees' professionals and those of the Unsecured Creditors Committee and Prudential? This information is necessary for creditors deciding whether to accept the Plan.

**Financial Information, Valuations and Projections Relevant to Creditors' Decision about Plan.** Creditors are given no meaningful information about the value of the Prudential Collateral supporting the secured claims.

**Information Relevant to Risks being Taken by Creditors and Interest Holders.**

The Disclosure Statement does not provide any information or discussion regarding the risks to Southern of a Member's bankruptcy or a Member's legal or public action to leave Southern. There is no discussion of the risks to Members' customers from the increased rates called for in the Plan and Disclosure Statement.

**Actual or Projected Values from Avoidable Transfers.**

The Disclosure Statement does not identify any avoidable transfers or explain the projected recoveries to the Estate from such litigation.

**Relationship of the Debtor with Affiliates.**

The Members are affiliates or related parties of Southern. In addition to being the only members of Southern under the Montana Rural Electric and Telephone Cooperative Act and Southern's Bylaws, the Members are the only customers and source of revenue for Southern. The Members' WPC's are the sole source and basis to fund the Plan.

The Plan is based upon and requires a continued contractual relationship between Southern and its Members. The relationship between Southern and its members has deteriorated since 2008 to the point that two members, YVEC and the City of Great Falls/ECP, have departed from

Southern and terminated their WPCs. This litigation lasted over four years. The deteriorated relationship between Southern and the Members extends beyond legal disagreements to extensive public dissension in the press and political pressures with State and Federal elected officials, including efforts to change the Montana Rural Electric and Telephone Cooperative Act. The Members' relationships with Southern range from tenuous to openly antagonistic. Beartooth has filed an adversary proceeding against Southern seeking to void its WPC. The other Members have intervened in that action.

The lack of stability in the essential interlocking relationship among Southern and its Members is not discussed in any meaningful way. The effect of this deteriorated relationship on the viability of the Plan is not discussed. The Disclosure Statement should describe these relationships and their likely effect on the Plan.

In addition to omitting information under the *In Re Metrocraft* standards, the Disclosure Statement has additional deficiencies as follows:

**Temple Report**

Section IV.U of the Disclosure Statement briefly mentions the "Trustee's Report" but provides no substance.

On January 3, 2012, the Chapter 11 Trustee filed an Application [Dkt. 184] requesting authority to retain Nancy Temple and the law firm of Katten & Temple, LLP to assist the Trustee in investigating the acts, conduct, assets, liabilities, and financial condition of the debtor and related matters pursuant to 11 U.S.C. §1106(a)(3) so that the Trustee can fulfill his fiduciary duties pursuant to 11 U.S.C. §1106(a)(4). Section 1106(a)(4) requires the Trustee "as soon as practicable – (A) to file a statement of any investigation conducted under paragraph (3) of this subsection, including any fact ascertained pertaining to ... a cause of action available to the estate." The Order granting the Application was issued January 4, 2012. [Dkt.185]

It has now been 20 months since Ms. Temple was employed. The Disclosure Statement states that Ms. Temple has not “finalized” her report and the Trustee has not yet completed and filed his statement. The creditors and the Members should be entitled to both reports and should be informed of any claims or future litigation that Ms. Temple or the Trustee have found from their investigation. The time and expense of such litigation is an important consideration for creditors and the Members in determining whether to accept or reject the Plan.

#### **MSCGI Agreement**

The Plan provides for a new 10 year power purchase agreement between Reorganized Southern and Morgan Stanley Capital Group (“MSCGI Agreement”). There is no discussion of the effect of inaccurate load forecasts, or any Member’s bankruptcy or default in power purchases, on the Members or Southern under the MSCGI Agreement.

The Trustee’s Second Amended Plan filed on September 12, 2013, now discloses that “[U]nder the MSCGI Agreement, prior to the start date of any transaction thereunder, the Debtor shall provide or cause to be provided a Guarantee Agreement from each of the Members in favor of MSCGI.” The Disclosure Statement fails to explain the terms of such Guarantee Agreements or how the Debtor will obtain such a Guarantee Agreement from each of the Members. Will the Members be required to guarantee Southern’s power purchase agreement when they have not done so in the past?

#### **Information About Absolute Priority Rule and Unfair Discrimination**

The Disclosure Statement contains a discussion about how the Plan can be confirmed if it is fair and equitable, but it does not contain an explanation about the absolute priority rule in 11 U.S.C. § 1129(b)(2)(B), or the unfair discrimination rule in 11 U.S.C. § 1129(b)(1), and except for conclusory statements, how the Plan satisfies or does not satisfy those rules. The Trustee’s conclusion that the Plan can be confirmed as fair and equitable under cram down principles ignores Section 1129 problems with

the Plan. The 11 Plan is unclear as to whether the Members should be considered equity owners or creditors and whether they are receiving anything from the Plan.

**Failure to Disclose Information About Plan's Treatment of Executory Contracts**

The Disclosure Statement does not provide basic information about executory contracts that are to be assumed or rejected. The Disclosure Statement references Exhibit B to the Plan which lists WPC's for Tongue River, Fergus, Mid-Yellowstone and Beartooth which are to be assumed and assigned to Reorganized Southern under the Plan.

The Disclosure Statement fails to provide information or discuss whether the WPC's can be assumed and/or assigned as provided in the Plan without the consent of the Members under 11 U.S.C. § 365(c)(1). Clearly, existing WPC's cannot be modified under 11 U.S.C. § 365 without consent of the Members. There is no discussion whether the WPC's can be modified as proposed in the Plan. The Disclosure Statement should include information to advise creditors that the treatment of the WPC's as proposed in the Plan may render the WPC's void or unenforceable and may be in violation of the Bankruptcy Code.

Creditors and Members must be informed in the Disclosure Statement of their rights under § 365.

**Inadequate Information About Proposed Settlement with Prudential**

As discussed above, the Disclosure Statement does not discuss the value of the Prudential Collateral. The Disclosure Statement should inform parties that the settlement reached between the Trustee and Prudential did not involve participation in negotiations or consent of other objecting parties, including the Members and the Unsecured Creditors Committee. It should also disclose that the Trustee and the Members alleged that the Prudential "Make Whole Payment" was improper and usurious and that Tongue River submitted an expert report reflecting that the effective rate of the Prudential Make

Whole Payment was in excess of 15%. Prudential did not submit any report to contradict this effective interest rate.

**Inadequate Information About Disputed Claims and Voting**

Neither the Disclosure Statement nor the Plan identify what claims will be disputed.

**Conclusion**

For the reasons set forth above, the Disclosure Statement fails to comply with the requirements of 11 U.S.C. § 1125 and its approval should be denied.

DATED this 18<sup>th</sup> day of September, 2013.

Guthals, Hunnes & Reuss, P.C.

By: /s/ Jeffrey A. Hunnes  
Attorneys for Tongue River Electric  
Cooperative, Inc.

**CERTIFICATE OF SERVICE**

I, the undersigned, certify under penalty of perjury that on September 18, 2013, or as soon as possible thereafter, a copy of the foregoing Tongue River Electric's Objections to Trustee's Disclosure Statement was served electronically by the Court's ECF notice to all persons/entities requesting special notice or otherwise entitled to the same and that in addition service by mailing a true and correct copy, first class mail, postage prepaid, was made to the following persons/entities who are not ECF registered users: none.

**Guthals, Hunnes & Reuss, P.C.**

By: /s/ *Jeffery A. Hunnes*  
Attorneys for Tongue River Electric  
Cooperative, Inc.