



Background: Our history with Southern Montana Electric Cooperative

Southern Montana Electric Generation and Transmission Cooperative began operations in 2004 after its five rural electric cooperative members negotiated an exit from Central Montana Electric Generation and Transmission Cooperative. From the separation the Southern cooperatives took their agreed share of power purchase contracts with Bonneville Power Administration and Western Area Power Administration and network transmission rights with NorthWestern Energy Corporation. The Southern cooperatives paid no premium to leave and received a cash payment of approximately \$1.8 million in capital credits. Electric City Power, a utility arm of the city of Great Falls that wished to supply power to several industrial customers, soon joined Beartooth Electric (BEC), Fergus Electric, Mid Yellowstone Electric, Tongue River Electric, and Yellowstone Valley Electric (YVEC) as a Southern member.

Southern quickly began efforts to finance and build a 250 MW coal-fired power plant, the Highwood Generating Station, near Great Falls. BEC members openly questioned their board's support for HGS after repeated rate increases were attributed to financing requirements for the power plant and the Rural Utility Service denied funding. YVEC withdrew support for the plant in 2008 and Southern began looking for private financing for a 40 MW gas-fired plant at the HGS site. Loans were obtained in 2010 from Prudential Insurance Company of America and others.

In 2010 BEC members elected two new trustees opposed to the construction of HGS and other decisions made at Southern. In September of 2011 BEC elected three more trustees who did not agree with the former board's support for Southern's actions. The new board elected a BEC representative for Southern who was denied a seat by the Southern board on the same day that Southern declared bankruptcy.

In 2011 the BEC board created a due diligence committee to examine power supply alternatives in the event the BEC contract with Southern could be terminated. The committee and board concluded that a legal exit from Southern would benefit BEC members. In 2012 BEC filed an adversary proceeding in U.S. Bankruptcy Court, seeking to void the 2008 contract with Southern and its pledge of BEC's all-requirements contract as collateral to the secured noteholders. BEC also joined the other Southern members seeking declaratory judgment that the all-requirements contracts with Southern are unenforceable, unassignable, and unassumable. In June 2013 BEC joined a motion to convert the Chapter 11 bankruptcy action to Chapter 7 liquidation. In October Southern's members filed a plan of liquidation. In December 2013 BEC and Fergus filed a second motion to convert to Chapter 7 liquidation.

After mediation in January 2014 Southern and its members reached a settlement agreement with Prudential Insurance and its associated noteholders. The settlement provides for payment of \$21 million for amended notes. Payment of the reduced debt is projected for a period of 4 years. The settlement Term Sheet allows BEC to have its all-requirements contract with Southern removed as collateral for the debt on payment of its share of the noteholder debt. BEC is negotiating with Southern and its member co-ops to take advantage of the settlement provision and exit Southern.

Southern filed a reorganization plan and disclosure statement in U.S. Bankruptcy Court on April 21, 2014. Southern's counsel also filed a motion to expedite the hearing on the plan, which was granted. A hearing on the disclosure statement is set for May 9 in Great Falls. If the disclosure statement is approved, the confirmation hearing on the plan could be held on May 20 in Billings.

April 23, 2014

Updates are provided at www.beartoothelectric.com