UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF TEXAS
CORPUS CHRISTI DIVISION

IN RE:	)	**CASE NO: 07-20027**
	)	
	)	**Corpus Christi, Texas**
SCOTIA DEVELOPMENT, LLC,	)	
	)	**Monday, July 7, 2008**
	)	**(5:03 p.m. to 5:42 p.m.)**
Debtor.	)	

RULING

BEFORE THE HONORABLE RICHARD S. SCHMIDT,
UNITED STATES BANKRUPTCY JUDGE

Appearances:	**See next page**
Courtroom Deputy:	**Frances Carbia**
Court Recorder:	**Janet Silika**
Transcribed by:	**Exceptional Reporting Services, Inc.** **14493 S. Padre Island Drive** **Suite A-400** **Corpus Christi, TX 78418-5940** **361 949-2988**

Proceedings recorded by electronic sound recording; transcript produced by transcription service.

COURTROOM APPEARANCES FOR:

Debtor:	**NATHANIEL PETER HOLZER, ESQ.** **Jordan Hyden Womble and Culbreth** **500 N Shoreline** **Suite 900 N** **Corpus Christi, Texas 78471**
Also present:	**JOHN PENN, ESQ.**

TELEPHONIC APPEARANCES FOR:

CSG Investments:	**DAVID F. STABER, ESQ.** **Akin Gump**
Department of Justice:	**ALAN TENENBAUM, ESQ.**
Environmental Protection Information Center:	**SHARON DUGGAN, ESQ.** **Law Office of Sharon Duggan**
DK Partners:	**EPHRAIM DIAMOND, ESQ. (Listen only)** **DK Partners**
Scotia Pacific Company:	**KATHRYN COLEMAN, ESQ.** **Gibson Dunn, et al** **200 Park Avenue** **New York, NY 10166**
Mendocino Redwood Co.:	**ALLAN BRILLIANT, ESQ.** **CRAIG P. DRUEHL, ESQ.** **Goodwin Procter**
Official Committee of Unsecured Creditors:	**JOHN FIERO, ESQ.** **Pachulski Stang, et al.**
Also present:	**ERIC FROMME, ESQ.**
Maxxam, Incorporated:	**JEFFREY E. SPIERS, ESQ.** **Andrews Kurth, LLP** **600 Travis** **Suite 4200** **Houston, Texas 77002**
Marathon Structured Finance Fund:	**JENNIFER N. WHITE, ESQ.** **Winston and Strawn, LLP** **200 Park Avenue** **New York, NY 10166**

TELEPHONIC APPEARANCES FOR: (Continued)

Bank of New York Trust Company:	**MARK A WORDEN, ESQ.** **Fulbright and Jaworski, LLP** **Fulbright Tower** **1301 McKinney** **Suite 5100** **Houston, Texas 77010**
Houlihan Lokey:	**TODD HANSON (Listen only)**
Aurelius Capital Management:	**JEFFREY H. DAVIDSON, ESQ.** **ISAAC PACHULSKI, ESQ.** **Stutman Treister & Glatt** **WEI WANG, ESQ.** **Aurelius Capital**
CSG Investments:	**JACOB CHERNER, ESQ. (Listen only)** **CSG Investments**
Scotia Pacific Company, LLC:	**WENDY LAUBACH, ESQ.** **Diamond McCarthy Taylor and Finley** **909 Fannin** **Suite 1500** **Houston, Texas 77010**
Plainfield Asset Management:	**ROBERT DAMSTRA, ESQ.(Listen only)** **Plainfield Asset Management, LLC**

Corpus Christi, Texas; Monday, July 7, 2008; 5:03 p.m.

(Counsel appear in person and telephonically)

(Call to Order)

THE CLERK: All rise.

THE COURT: Be seated. Send in the call.

All right, let's see, Brian Hall?

(No audible response)

THE COURT: Eric Winston?

(No audible response)

THE COURT: David Staber?

MR. STABER: Here, your Honor.

THE COURT: Kathryn Coleman?

MS. COLEMAN: Present, your Honor.

THE COURT: Mark Worden?

MR. WORDEN: Present, your Honor.

THE COURT: Allan Brilliant?

MR. BRILLIANT: Here, your Honor.

THE COURT: Jeffrey Davidson?

MR. DAVIDSON: Good afternoon, your Honor.

THE COURT: Steven Schwartz?

(No audible response)

THE COURT: Jeffrey Spiers?

MR. SPIERS: Good afternoon, your Honor.

THE COURT: Isaac Pachulski?

MR. PACHULSKI: Good afternoon, your Honor.

THE COURT: Alan Tenenbaum?

MR. TENENBAUM: Present, your Honor.

THE COURT: Jeffrey White?

(No audible response)

THE COURT: John Fiero?

MR. FIERO: Good afternoon, your Honor; John Fiero for the Committee.

THE COURT: Eric Fromme?

MR. FROMME: Good afternoon, your Honor.

THE COURT: Jacob Cherner?

MR. CHERNER: Present, your Honor.

THE COURT: Robert Damstra?

MR. DAMSTRA: Present, your Honor.

THE COURT: Craig Druehl?

MR. DRUEHL: Yes, your Honor.

THE COURT: Sharon Duggan?

MS. DUGGAN: Yes, your Honor.

THE COURT: Wendy Laubach?

MS. LAUBACH: Present, your Honor.

THE COURT: Dan Kamensky?

(No audible response)

THE COURT: Stephen Wolpert?

(No audible response)

THE COURT: Todd Hanson?

MR. HANSON: Present, your Honor.

THE COURT: Wei Wang?

MR. WANG: Present, your Honor.

THE COURT: Ephraim Diamond?

MR. DIAMOND: Good afternoon, your Honor.

THE COURT: Kenneth Crane?

MR. CRANE: Ken Crane, and I have Jim Pelke (phonetic) and Richard Higginbotham (phonetic) on the phone.

THE COURT: Thank you. Joli Pecht?

MS. PECHT: Present, your Honor.

THE COURT: Demetra Liggins?

MS. LIGGINS: Present, your Honor, with (***) Herndon (phonetic).

THE COURT: Okay. Heather Muller?

MS. MULLER: Good afternoon, your Honor.

THE COURT: Gary Clark?

MR. CLARK: Present, your Honor.

THE COURT: Frank Bacik?

MR. BACIK: Good afternoon, your Honor.

THE COURT: All right, anyone else on the phone?

MR. LEE: Yes, your Honor.

THE COURT: Go ahead.

MR. LEE: Kyung Lee.

THE COURT: Okay.

MS. WHITE: And this is Jennifer White with Carey Schreiber.

THE COURT: All right. And then in the courtroom we have someone from Marathon.

MR. JORDAN: Your Honor, this is Shelby Jordan and Lucky McDowell on the phone.

MR. PENN: John Penn, and we have Tony Gerber on the phone, your Honor.

THE COURT: Who is that on the phone?

MR. PENN: Toby Gerber.

THE COURT: Thank you. And Pete Holzer is in the courtroom?

MR. HOLZER: Thank you, your Honor.

THE COURT: I'm not sure whether anyone -- I tried to announce earlier in a hearing -- What hearing was that?

MR. SPEAKER: Asarco's hearing.

THE COURT: Oh, was it Asarco's hearing? But not everyone was there, and I see Mr. Tenenbaum is on the line now. I had announced that I had permission to announce that the lawsuit in Brownsville would not be decided during the month of July, so if the parties wanted to get together to work out something, they have that opportunity.

All right, we're here now for my ruling on the administrative claim, alleged administrative claim of the Indenture Trustee.

I'd like to start with background of how we got to this point because I think it's important. The case of course

was filed on June 18th, 2007. The parties have mediated this case with Judge Houser and Judge Isgur. There was a confirmation hearing on April 8th through the 8th, and then a continued confirmation hearing on April 29th through May 2nd.

On May 1st, the IT filed a motion to grant the IT a super priority administrative claim.

On May 2nd, the IT's attorney asked the Court to set the administrative claim for hearing with closing argument. The Court then asked the attorney how much the claim was, and for some reason that wasn't answered. Another question I guess was answered but we never got back around to that, and we discussed the confirmation -- the closing argument.

On May 15th when I set closing argument, we had the closing argument but the IT first filed a motion to reopen the evidence to introduce the Sierra Pacific offer. The motion was granted. No motion was made to reopen the evidence to submit any evidence of an administrative claim.

The IT's proposed findings that they filed, number 297 and 299, were consistent with the motion for the super priority administrative claim that they filed claiming a failure of an equity cushion and a $20 million dollar cash collateral shortage.

On June 6th, 2008, findings of fact and conclusions of law were entered by the Court and a status conference was set. Finding number 286: The Court made a finding that the IT

got 530 million less an adjustment of approximately 13 million, and set a status hearing. The IT then, at the status hearing, announced to the Court that it had an administrative claim that might be as much as $200 million dollars. This was the first the Court had ever heard of that and was concerned that that wasn't brought up in the confirmation hearing, but the Court set the administrative claim hearing for the 9th of June.

IT then asked for a continuance, which the Court granted, and set the hearing on the administrative claim for June 30th through July 2nd.

Now, we should keep in mind that up until the hearing, the IT's administrative claim was based on a finding that it was oversecured at the cash collateral hearing. However, over-security was not the basis of the use of cash collateral.

At the cash collateral hearing, ScoPac attempted to introduce evidence of the value of the timberlands, arguing that a valuation prior to confirmation hearing would be critical to plan negotiations as well as expected upcoming hearings on granting of a priming lien to a DIP lender, et cetera. The Indenture Trustee however, objected, arguing that the valuing evidence was irrelevant.

The Court decided not to hear the valuation testimony regarding the equity cushion over any valuation of their claim. ScoPac relied on its prior record to the effect that the trees

would grow faster if they are cut, and that once cut, they remain subject to Bank of New York's lien and are log inventory and then they become receivables once they're sold. The IT acknowledged that the Court had previously found that the tree growth constituted accurate perception. Ultimately, the Court noted that the value of the timberlands was unclear at that time but nevertheless overruled the IT's objection and approved the use of cash collateral.

Now, it's elementary Chapter 11 law. Section 1129(a)(9) requires the payment in full on the effective date of the plan of all of these administrative claims, any administrative claims. The Court's finding number 286, that the IT got 530 less the adjustment, which the Court believed to include any potential administrative claim, for a total of 517 million. There was no evidence at the confirmation hearing that the property had declined in value.

In Chapter 11, administrative claims are usually dealt with after a confirmation unless an objector is alleging that the plan violates 1129(a)(9), which is perhaps what's being alleged here. Here, the determination of this administrative claim is only a determination vis-à-vis the Marathon/Mendocino plan. Obviously, if the plan is not confirmed or if the case is converted to seven or if the property is foreclosed at a later date or something else traumatic happens at a later date, there could be a different

administrative claim which might be filed, so, any ruling today is only an administrative claim as it concerns this plan.

The super priority status of this claim has absolutely no bearing at this point because all administrative claims must be paid. It obviously might have a significant bearing in a later Chapter 7 case if one ever resulted.

The Court could have ruled that the IT had its shot at confirmation and chose not to litigate it during the confirmation hearing and is barred by the Court's findings. However, because of the unusual way that this whole thing arose and the context of the way it arose, the Court believed that, as a court of equity, that the IT should be given the right to prove its claim.

Now, at the trial of the claim, the IT did produce witnesses as to value but also introduced evidence and took basically an approach that perhaps could be consistent with reconsidering the order of confirmation and perhaps trying the issue as though it were part of the confirmation case.

First of all, the IT asserted that the conduct of Marathon and Mendocino in this case and their presentation in this particular case was an affront to the integrity of the bankruptcy system. They introduced two e-mails; one was a September 7th e-mail. Keeping in mind that this was during the period of this case when there was exclusivity, it was prior to the three mediations, obviously the first one being in November

of 2007. It was in September of 2007, at a time when Marathon was apparently courting Mendocino to be a participant perhaps in a potential plan. However, there was no right to file a plan at that time because there was exclusivity.

In that e-mail, Mr. Dean describes a number of things which, taken out of context, certainly can sound as affronts to the integrity of some jurisdiction systems. However, they have to be kept in mind in the context of this case.

First of all, there was a comment that the log deck, ScoPac getting a log deck and moving the log from PALCO to ScoPac, was a sleight of hand. Well, I mean, perhaps that's a description someone might give of it. If that's the only description of it, I mean, they were describing Mr. Horowitz's conduct in the case, and I can assure you there have been far more colorful descriptions, and I'm not suggesting any of them correct. However, if it were a sleight of hand, it was a sleight of hand that was approved by the Court.

There was no question that the Court was not aware of exactly what happened. All the parties are well represented in this case and had the opportunity to object to the log deck situation. Those objections were made and the Court ruled. So, I mean, it's hard to consider that as something that is an affront to the judicial system.

Then there was the comment about a bogus appraisal. You know, we talked about MAI appraisers in this particular

case, and the Court is mindful of the standard joke that MAI stands for 'made as instructed.' Well, you know, there is no question that businessmen have different impressions about the impacts of appraisals in cases. The statement was made that 'the debtor or Marathon might use a bogus appraisal to cram down the note holders.' Well, that's exactly the concern the Supreme Court had in the *LaSalle* case, and to avoid that possibility, the Court lifted exclusivity.

So, the Court is certainly mindful of the fact that while there's exclusivity, a debtor might try to use appraisals to cram down note holders, and it would be inappropriate under LaSalle, but putting it out into the market by lifting exclusivity does, in fact, provide a mechanism for everyone to be able to avoid the possibility that somebody might use a so-called bogus appraisal to cram down someone in a bankruptcy case.

And then of course, throughout the e-mail there was the notion that Marathon wanted to steal equity. I'm not sure what is meant by 'equity' when Mr. Dean said 'stealing equity', because nobody in this case has any equity. Perhaps maybe Bank of America in the sense, in the traditional sense of having it, and even then - If you mean value over the debt, the debtor certainly had no equity in this case and ultimately gave up because they knew they had no equity.

IT had no equity; that's the certainly the finding

that I've made, and I think that's the position they took early on in the case and throughout the case.

Marathon certainly had no equity in this case. If what he meant when he said 'equity' -- he's not lawyer, he's a businessman; if what he meant was ownership, that they meant to steal ownership, well, by lifting exclusivity, again, everybody then is given equal opportunity to steal the other person's ownership. That's what the effect of lifting exclusivity is. Maybe we don't say it quite that coldly, but that's exactly what happens once you lift exclusivity. It's then everybody's chance to put forth a plan that might give them the best possible situation.

In fact, the IT in this case had a $750 million dollar claim and 510 worth of security as leverage against Marathon, which I think had something in the neighborhood of $125 million dollar claim. And perhaps the important assets, the mill and the electric plant, were worth perhaps 25 million as security. Thus, the IT had perhaps a 20-to-1 leverage advantage over Marathon to propose a buyout of all the assets.

I have no idea why the IT didn't decide to just take some money and buy out the claim of Marathon. I don't know. Obviously they wouldn't have been able to buy it from Marathon but they could cram down Marathon to the value of their claim.

They either relied on the false assumption that the amount of their -- the value of their claim, even as

undersecured, was so high that nobody would possibly try to buy it out, or, more likely, their strategy was to hold out to delay and foreclose their lien. Nothing wrong with that. That's their strategy. If they want to live with it, that's fine. However, if somebody proposed a plan, the Court has a duty to look at the plan to see if it's confirmable.

Second, there was an e-mail later in the case about Mr. Barrett or Dr. Barrett's proffer, from Sandy Dean. In that, he said there was no significant increase in the forest; that they harvested everything; that the roads added no value, they were much like -- I think he said they were like a roof on a house, that it added no value but it's good for the buyer to get -- and that perhaps the watershed analysis might add some value.

Dean's proffer in the case said that the timber prices were higher in 2007 but expected them to climb; that the discount rate had declined, and that the original value of the forest, using his sustained-yield philosophy, was $425 million dollars. I didn't find anything remarkable about the e-mail describing the proffer or, I don't find it to be in conflict to what he testified either in his proffer or in the original court hearing.

Underlying all of this I guess is the notion that laymen, and even lawyers, who don't practice bankruptcy believe that bankruptcy is hocus pocus; that it's smoke and mirrors,

especially to business people and non-bankruptcy lawyers, as I said. Many of the provisions in a bankruptcy are counter-intuitive. But, to the extent it is, it's Congress-mandated hocus pocus. I mean, in the sense that once -- I mean, it's difficult for people to understand that they can have a deal with somebody and go into bankruptcy and it gets turned around. But it happens.

The goal of bankruptcy is to maximize assets for creditors, not to favor any one creditor over another. Secured creditors get significant protections in bankruptcy, but those protections are not the same as outside of bankruptcy. And, to the extent that they change, all of that is counter-intuitive to a businessman. So, it is not surprising to me that businessmen speak in such kinds of terminology during the course of a bankruptcy case.

Another issue that the IT brought up about the affront to the integrity of the case was the conduct of the appraisers. In a complex case like this, appraisers may differ in their valuation, and it is no surprise nor is it any bad faith, that an appraiser's selection of value favors the appraiser's client. Again, that, again, is the problem that *LaSalle* and the Supreme Court have pointed out.

Plenty of reasonable minds have differed as to the value in this case. Let's start with Houlihan. They had two different values from the same firm. In September, the value

was between 250 and 500, Mr. DiMauro. Then at confirmation, Glen Daniels, it was at 589 to 716. Mr. Glen Daniels even invented -- you know, we hear appraisals on property and the three different approaches to value over and over again in a bankruptcy court, and Mr. Daniels created a fourth one, which was a bid procedure.

Now, you know, I think he did a reasonable job. I don't think anything he did was incorrect. I mean, I don't think it was improper what he did, but it certainly did cast question on the weight to be given to his testimony.

Mr. Fleming. Mr. Fleming dated his appraisal in October of 2007, some nine months prior to the confirmation; found a value and held out to the Court that that was the same value nine months later. Yet when he testified in open court on the administrative claim hearing to a time period just ten months before his appraisal -- not nine but ten -- it was $46 million dollars higher. He stayed with the same value at confirmation, but then wanted to change it at the time of the administrative claim hearing, even though the significant market factors had occurred and, significantly, many of them occurred after his appraisal.

Look at Mr. Lamont. He testified that the property was worth between 425 and 430. Mr. Lamont also had difficulty remembering, when he took his deposition, that a chart that he selected -- Let me start over. Mr. Lamont selected for his

valuation a chart of timber prices that he'd never used before and which are about ten percent lower than another chart which he normally uses. That perhaps was favoring his client. And then in a deposition, he forgot that that not all of the prices that he had gotten that he had listed in his report were from that chart even, because the chart was not published after a certain date.

Now, if you look at his notes, it's clear that there was a gap after the date that they were published and then there were new figures after that. I think that ultimately, I don't think he lied on the stand in court; I think he forgot what he had done. All of that goes to the weight to be given to his testimony of course, but, remember, he valued this at 425 to 430. I didn't accept that. I found the value at 510.

Interestingly enough, the values that the Houlihan people came up with, if you average all of them, that's only around 523.

It's significant that Mendocino throughout this case has had a whole different approach to value than some of the other appraisers. Mendocino's philosophy differs; they were a purchaser in this case, and for them to purchase this, the value would be determined by the way they would use it. That may not be the fair value of it -- fair market value of it, but as far as the value for them, it's going to be based upon a discounted cash flow analysis of the amount of timber that they

would harvest with their philosophy, a philosophy that includes a sustained yield, a philosophy that does not include clear-cutting. So, as a result, it seems to me that the Mendocino approach erred in that it erred on the conservative side for value.

The debtor, with perhaps what we would call terminal optimism, believed the value near one billion dollars, based it on artificially high prices with a 4.5 per annum rise in prices, and based on a computer model that harvests a maximum timber, even beyond practicality and beyond sustainability, where they were harvesting sometimes one log. But the model created a timber yield that was artificially high, and I so found.

The Court's duty in determining value, I must consider all the evidence presented and reach my own conclusions. I did not adopt any appraisal. In fact, the Court's figure was almost directly halfway between Mr. Fleming and Mr. Lamont. However, that is not how the Court arrived at its value. The Court used all the appraisals, as pointed out in the opinion, giving appropriate weight to those appraisals and came up with what I believe to be the value. The Court gave various weights and listed various things about all of these appraisers, and I'm not changing any of those findings with respect to the analysis that I did in the opinion on confirmation.

Now, turning to administrative super priority. The law of administrative super priority claims, the burden of proof of course is upon the claimant to establish an administrative super priority claim. For instance, there's the *Rebel Brentz* (phonetic) case out of the Central District of California: The burden of proof is on the claimant.

Section 507(b) affords a super priority claim arising from the failure of adequate protection, and its provisions provide that if the Trustee, or here the debtor, under Section 362(3) or (4), provides adequate protection of the interest of a holder of a claim secured by a lien on property of the debtor, and if, not withstanding such protection, such creditor has a claim allowable under Section (a)(2) of this section arising from the sale, use, or lease of such property under 363, et cetera, then such creditor's claim under said subsection shall have a priority over every other claim allowable under said subsection.

In order to establish a right under 507(b), there of course have been cases that set out three criteria: The debtor or the Trustee must have provided them with adequate protection that proves to be inadequate; that the creditor must have an allowable claim under 507(a)(1), which in turn requires the claim to be allowable as an administrative expense under 503(b); and third, the creditor's claim must have arisen from the use, sale, or lease of the creditor's collateral. And

citing, there's a Fourth Circuit case. There's also Collier's cites to all of that.

Now in this case, the administrative claim is not based upon the normal section in the Code that provides for administrative claims, but rather the cash collateral orders. The cash collateral orders that have been issued in this case each contain a provision which says that each of Bank of America and the Trustee, on its own behalf and on behalf of the Bank of America and the note holders, is also granted a super priority cost of administration priority claim under 11 U.S.C. 507(b) to the extent of the pre-petition diminution of their respective interests in the pre-petition collateral and cash collateral.

In addition to that, the cash collateral order suggests that the administrative cost of administration claim granted by the order shall be subject and subordinate to a carve out for the payment of allowed consultant and professional fees and disbursements incurred by consultants and professionals retained, et cetera. It provides that the expenses of the committee in investigating or reviewing the pre-petition claims of Bank of America and the Trustee and the note holders can be paid out of the cash collateral. It provides that 'the same may be payable, and the amounts so paid shall be free and clear of any liens in the super priority administrative claims of Bank of America and the Trustee.'

So in this case, we have an order which establishes an administrative claim if the note holder can provide -- can prove that a post-petition diminution of their interests in pre-petition collateral and cash collateral. I think it's significant first of all, that it uses the word 'interests', which is the same as the Code.

Now, so it seems to me that in order to determine whether or not the note holders have an administrative claim under this section of the cash collateral order, I must determine whether or not their interests have been diminished. And I think that I have two things that I can look at: the evidence in this case, which the IT has presented, goes to whether there is a potential decrease in the timberland value; and second, whether there is a potential decrease in the other security value. So, I'll analyze those separately, first turning to the timber value.

I believe that the Trustee, the Indenture Trustee, failed to meet its burden of proof or provided insufficient evidence that there was any change in value to the timberlands.

First of all, Mr. Fleming's value at the date of filing was 646 and 605 at confirmation. That was only a difference of 41 million. I mean, that's significant money. If you use my analysis, which I found that the value at confirmation was approximately 84 percent of his 605 figure, that would really -- 84 percent of 41 million is 34.5 million.

The difference was based upon his belief that there are more trees to harvest at filing and therefore it could sustain a higher harvest rate and thus a higher value.

The statement is contrary to all the testimony in this case. All of the other evidence in this case demonstrates that the trees continue to grow, and that even after harvesting, there is either more or, if you believe Sandy Dean's e-mail, there is at least as much, equal to the total volume of timber each year.

There was a mortgage banker who testified that as to macro-economic forces in the market, in the industry of wood there's been a turndown since the filing of this case. However, he was not able to tie that with any specificity to this case, to this county, to the redwood forests, or this industry specifically.

The case law suggests that the Code provision for protection for loss of secured creditors -- the Code protects the loss of secured creditors' interest in the property. With non-cash property, the interest that secured creditor has a right to is the right to foreclose. Therefore, the case law suggests that the appropriate value to protect is the foreclosure value of the property and not the fair market value of the property.

Now, both sides have cited the *In Re: Stembridge* (phonetic) case out of the Northern District of Texas which

states, even though it was reversed on other grounds, it states: 'With regard to the provision of adequate protection, a secured creditor is entitled to have his interest protected against diminution by reason of the estate's ongoing possession and use of creditor's collateral. The interest of the secured creditor is properly valued from the secured creditor's perspective. In other words, the secured creditor must be protected such that the total realizable from its collateral through foreclosure does not decrease as a result of the delay imposed by the bankruptcy case or the enforcement of its rights.'

All of the cases dealing with adequate protection of undersecured creditors, like those that came out before timbers, for instance, based the value of adequate protection on the liquidation or foreclosure value. Here, the plan pays for the payment of fair market value of the IT's lien. No evidence was presented to suggest that the liquidation or foreclosure value at filing was higher than the fair market value at confirmation. In fact, the evidence shows that the liquidation value at filing was in the range of 300 million. Moreover, foreclosing without permits or an adjacent sawmill may lead to an even lower value.

But all of this is speculative, so that it seems to me that the evidence suggests that there has not been a decline from the -- In fact, there's been no evidence as to a decline

in the foreclosure value of the case, but even looking at the fair market value, the evidence showed that from filing to confirmation, the forests grew so that there are more trees. Capital improvements were made -- roads, tree planting, watershed analysis -- which freed more areas for harvesting. Perhaps the roads don't add any value, as Mr. Dean suggested, but the tree planting and the watershed analysis did free up more areas for harvesting, which ultimately will lead to more value. All of this may lead to a value being higher at confirmation, but the Court is not prepared to make that finding that there has been any change in value since the filing.

Significant evidence suggests that the discount rate has gone down since filing. The discount rate, the Court believes, under the appropriate analysis for the value of a forest, the discount rates are a far bigger indicator of a change in value than change in the price of the logs. Because Marathon's expert did a comprehensive analysis of discount rates using sales, publications, and other techniques, because discount rate is a significant driver of value, lowering the discount rate results in a value of the forest being higher at confirmation. Fleming on the other hand, simply used a bond chart to pick a discount rate.

However, despite the increase in the forests and the decrease in the discount rate, the Court believes that the

value of the forests has remained relatively constant since the filing. This is consistent with the long-term approach to valuing commodities like this forest whose worth is based on constantly growing timber, the unique nature of these acres in this place, and with this type of wood.

The question before the Court is whether the value has decreased, and the Court finds it has not. The IT has argued that finding number 158 of my findings was tantamount to a finding that the price of the forests had declined. This is not true. To the extent the finding is unclear, the Court will clarify that this was merely pointing out the fallacy of Mr. Fleming's methodology. Because he chose to use a ten-year rather than a 50-year methodology, the initial price of the timber significantly drives the final outcome of value. The Court was merely pointing out the flaw; not adopting the approach, nor was I opining that his result was reasonable; only pointing out that this small change in price changes the value significantly, from 605 to 452. I did not adopt 452 as a value in this particular case.

Finally, then, if the value of the forests is the same, then the Court has to look at the value of other assets that provide security for the IT to determine whether or not he's being paid an amount in the plan equal to the value of his assets at confirmation and equal to the value of his assets -- equal to or greater than the value of his assets at the

beginning of the case and equal to the value of his assets, or greater than the value of his assets at confirmation.

The undisputed testimony about value of all other security items other than -- I'm not talking about the lawsuit. That's a separate asset that's been dealt with in the confirmation findings. But if you look at the attachments to Mr. Young's testimony and the testimony of the accountant or chief financial officer for ScoPac, you'll find that on the day of filing, in addition to the forests and the lawsuit, that the other assets that were the security for the Indenture Trustee equaled 48.7 million.

However, there was a claim of Bank of America of 36.2 million as of that time, and therefore, the remaining assets were 12.5 million, so that on the date of filing of the bankruptcy, the Indenture Trustee had security of 522.5 million.

At confirmation, it's not clear exactly how much the assets of the Indenture Trustee are worth, for a number of reasons. First of all, there was forests in the same amount, 510; there were other assets of 44.1, although among all of those there's some question as to whether all of those are dollar-for-dollar worth the value, and presumably they're not; and the Bank of America debt was 37.6 at confirmation, so that the net, assuming that all of those properties are equal dollar-for-dollar, the value of their security was 6.5. So, it

in fact was -- the value of their security was less than the amount that they had at filing.

So, for the plan to be confirmable, it has to pay them at least the value of their security at the filing of the case, which was, remember, 522.5.

The Indenture Trustee has already been paid for professional fees 8.9 million, so that that is a total of 518.9 million if they get 510 in cash for the forests and add in the 8.9 million that they've already been paid. That would leave them 3.6 million deficient. So, therefore, I am not -- I don't have to go to the issue of whether or not the auction rate securities are valued or whatever because they don't get those under the plan. All they get is their 510 for the forests under the original order that I contemplated and the 8.9 million that they've already been paid.

So therefore, I will change my order to say that they must pay them a minimum of 513.6 million in order to avoid any administrative claim. That'll be my order.

If there are those contingencies that are still in that confirmation, if Marathon and Mendocino want to go forward with that, then they should submit a confirmation order consistent with that and I'll confirm the plan.

Thank you. You-all are excused.

(This proceeding was adjourned at 5:42 p.m.)

CERTIFICATION

I certify that the foregoing is a correct transcript from the electronic sound recording of the proceedings in the above-entitled matter.

Signed

July 9, 2008

Dated

TONI HUDSON, TRANSCRIBER