

UNITED STATES BANKRUPTCY COURT
SOUTHERN DISTRICT OF TEXAS
CORPUS CHRISTI DIVISION

IN RE: SCOTIA PACIFIC, *
 * CASE NO. 07-20027
DEBTOR *

* * * * *

DAILY COPY

JUNE 30, 2008

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On the 30th day of June, 2008, the above entitled and numbered cause came on to be heard before said Honorable Court, RICHARD S. SCHMIDT, United States Bankruptcy Judge, held in Corpus Christi, Nueces County, Texas.

Proceedings were reported by machine shorthand.

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1 THE CSO: All rise.

2 THE COURT: Be seated. I will just take
3 a second before we send in the call. Okay. You can
4 send in the call. All right. Basil Umari.

5 (No response.)

6 THE COURT: Rebecca Riley. Is anybody on
7 the call? Okay. Well, I guess we lost the call, so
8 I'll hang up.

9 SPEAKER: We're here.

10 SPEAKER: We're here, Your Honor.

11 THE COURT: Okay. Let's start again.
12 Basil Umari.

13 MR. UMARI: Present, Your Honor, with
14 Jeff Spiers.

15 THE COURT: Okay. Rebecca Riley.

16 MS. RILEY: Present, Your Honor.

17 THE COURT: Isaac Pachulski.

18 MR. PACHULSKI: Good afternoon, Your
19 Honor.

20 THE COURT: Dan Kamensky.

21 MR. KAMENSKY: Present, Your Honor.

22 THE COURT: Alan Gover.

23 SPEAKER: I don't believe he will be
24 joining, Your Honor.

25 THE COURT: Okay. Jeffrey Spiers.

1 MR. SPIERS: Present, Your Honor.
2 THE COURT: Kyung Lee.
3 MR. LEE: Present, Your Honor.
4 THE COURT: Jennifer White.
5 MS. WHITE: Present, Your Honor.
6 THE COURT: Eric Winston.
7 MR. WINSTON: Present, Your Honor.
8 THE COURT: Mark Worden.
9 (No response.)
10 THE COURT: Andy Black.
11 MR. BLACK: Present, Your Honor.
12 THE COURT: Mike Neville. Michael
13 Neville. California.
14 (No response.)
15 THE COURT: Demetra Liggins.
16 MS. LIGGINS: Present, Your Honor.
17 THE COURT: Ira Herman.
18 MR. HERMAN: Present, Your Honor.
19 THE COURT: Brett Young.
20 MR. YOUNG: Present, Your Honor.
21 THE COURT: Robert Damstra.
22 MR. DAMSTRA: Present, Your Honor.
23 THE COURT: James Delaune.
24 MR. DELAUNE: Present, Your Honor.
25 THE COURT: Tom Walper.

1 (No response.)
2 THE COURT: David McLaughlin.
3 (No response.)
4 THE COURT: Melissa Kahn.
5 MS. KAHN: Present, Your Honor.
6 THE COURT: Peter Laurinaitis.
7 MR. LAURINAITIS: Present, Your Honor.
8 THE COURT: Wendy Laubach.
9 MS. LAUBACH: Present, Your Honor.
10 THE COURT: Christopher Johnson.
11 (No response.)
12 THE COURT: Wei Wang.
13 MR. WANG: Present, Your Honor.
14 THE COURT: Sharon Duggan.
15 MS. DUGGAN: Present, Your Honor.
16 THE COURT: John Driscoll.
17 MR. DRISCOLL: Here, Your Honor.
18 THE COURT: Erin Ross.
19 MR. ROSS: Present, Your Honor.
20 THE COURT: Francine Montagna.
21 MS. MONTAGNA: Present, Your Honor.
22 THE COURT: Clara Strand.
23 (No response.)
24 THE COURT: Daniel Zazove.
25 MR. CRANE: He is not on the call but

1 this is Ken Crane in his place.

2 THE COURT: All right. Todd Hanson.

3 MR. HANSON: Present, Your Honor.

4 THE COURT: Joli Pecht.

5 MS. PECHT: Present, Your Honor.

6 THE COURT: Shaye Dively.

7 MS. DIVELY: Present, Your Honor.

8 THE COURT: Was I close?

9 MS. DIVELY: Close enough.

10 THE COURT: Okay. Van Durrer, II.

11 (No response.)

12 THE COURT: Nathan Rushton.

13 MR. RUSHTON: Present, Your Honor.

14 THE COURT: Jacob Cherner.

15 MR. CHERNER: Present, Your Honor.

16 THE COURT: Dominic Santos.

17 MR. SANTOS: Present, Your Honor.

18 THE COURT: Gary Clark.

19 MR. CLARK: Present, Your Honor.

20 THE COURT: David Kitchen.

21 (No response.)

22 THE COURT: Heather Muller.

23 MS. MULLER: Present, Your Honor.

24 THE COURT: Anyone else on the call?

25 MR. NEVILLE: Yes, Your Honor, this is

1 Michael Neville.

2 THE COURT: All right. Thank you.

3 MR. DIAMOND: Your Honor, you have
4 Ephraim Diamond.

5 THE COURT: Who is that?

6 MR. DIAMOND: Ephraim Diamond.

7 THE COURT: Okay. Thank you. Anyone
8 else? All right. The courtroom, Mr. Greendyke.

9 MR. GREENDYKE: Good afternoon, Judge,
10 Bill Greendyke, Fulbright & Jaworski. I'm here together
11 with my partners, Zack Clement, Louis Strubeck, Richard
12 Krumholz, Todd Shields and Mr. Toby Gerber are here. We
13 represent the Bank of New York as Indenture Trustee.
14 Welcome home.

15 THE COURT: Thank you. Anyone at this
16 table?

17 MR. FIERO: John Fiero, Pachulski Stang,
18 for the Committee, along with Max Litvak, Your Honor.

19 MR. PENN: Your Honor, John Penn along
20 with David Neier, Steve Schwartz and Carey Schreiber on
21 behalf of Marathon.

22 MR. BRILLIANT: Good afternoon, Your
23 Honor. Alan Brilliant and Brian Hail on behalf of
24 Mendocino Redwoods Company.

25 THE COURT: All right. Whoever is the

1 closest to the mic just go right ahead.

2 MS. COLEMAN: Good afternoon, Your Honor,
3 Kathryn Coleman and Eric Fromme from Gibson Dunn &
4 Crutcher for Scotia Pacific.

5 THE COURT: All right.

6 MR. GIBBS: Good afternoon, Your Honor,
7 Chuck Gibbs with Akin Gump Strauss Hauer & Feld here on
8 behalf of CSG Investments and its various affiliates.

9 THE COURT: All right. Who is CSG
10 Investments?

11 MR. GIBBS: CSG Investments and its
12 affiliates are the largest holders of the notes.

13 THE COURT: Okay. Well, welcome.

14 MR. DAVIDSON: Good afternoon, Your
15 Honor, Jeffrey Davidson, Stutman Treister & Glatt here
16 on behalf of three individual noteholders.

17 THE COURT: Thank you.

18 MR. PASCUZZI: Good afternoon, Your
19 Honor, Paul Pascuzzi for the California State Agencies.

20 THE COURT: All right.

21 MR. JONES: Good afternoon, Your Honor,
22 Evan Jones of O'Melveny & Myers representing Bank of
23 America.

24 MR. STERBACH: Good afternoon, Your
25 Honor, Charles Sterbach for the United States Trustee.

1 SPEAKER: Glad to be back. Your Honor,
2 I'm here today representing Sierra Pacific Industries.
3 Sierra is the second largest lumber manufacturer in the
4 country. I'm here with co-counsel who I would like to
5 introduce, Mr. David Dunn. He's with the law firm of
6 Dunn & Martinbeck from California. Also with me, Your
7 Honor, are two of the senior executives of Sierra
8 Pacific, Mr. A.A. Red Emerson, the president and CEO of
9 Sierra Pacific and the owner. He's over there. They've
10 been in business for over 50 years. And Mr. George
11 Emerson, the chief operating officer.

12 THE COURT: All right. Thank you.

13 MR. McDOWELL: Good afternoon, Your
14 Honor, Lucky McDowell with Baker Botts on behalf of the
15 Palco debtors.

16 THE COURT: All right.

17 MR. McDOWELL: Your Honor, I also have
18 the order of battle today, if there aren't any more
19 introductions.

20 THE COURT: Okay.

21 MR. McDOWELL: We have ten items. The
22 Court should have received two notebooks today.

23 THE COURT: I do have them.

24 MR. McDOWELL: And I believe we have ten
25 items now on the agenda for the next three days. Take a

1 couple of them out of order than what's listed on your
2 agenda and they're both hopefully uncontested and are
3 finance related. One of them I would like to take at
4 the beginning of the hearing, one of them we would like
5 to push at the end of today if the Court would set aside
6 ten minutes.

7 The one that we would suggest that the
8 Court take up first is the cash collateral budget that
9 Scopac has requested. It is tab number 44 in the
10 Court's notebook. After that, Your Honor, we would pick
11 up with essentially what is in the order of the agenda
12 in the Court's notebook, the first motion being the
13 507(b) claim; the second being the entry of a
14 confirmation order, if we get there, Your Honor, on
15 whether the revised plan and order meet the Court's
16 requirements set out in its findings of fact and
17 conclusions of law.

18 And then if we get there, we have a --
19 presumably we will be facing a state pending appeal.
20 Although we don't have a motion yet, we do have
21 objections and some proffers offered in connection with
22 that. After that things get a little dicey depending on
23 where these first motions end up. We have different
24 scenarios, including 363 sales, DIP financing, etcetera.
25 I'm not going to go through all of them right now. I

1 think that we can probably take them up as we march
2 through the progression of things.

3 The last item, again, today that I would
4 like the Court to set aside ten minutes on has to do
5 with an arrangement between Palco and Scopac. Palco is
6 facing a current cash crisis and its most recent budget
7 does not project that it will have sufficient cash to
8 pay Scopac for the logs that are delivered for the month
9 of July. The problem, however, is that Palco also only
10 has a couple more days worth of logs in inventory and
11 Scopac needs to sell some logs. The agreement was
12 reached that Scopac would continue to sell logs to Palco
13 for the month of July on the same terms that it did in
14 June. And the big agreement here, the principal
15 agreement is that Marathon has agreed to carve out of
16 its collateral for the benefit of Scopac on those logs
17 that are delivered. The cross mechanism that's set
18 forth in the motion.

19 Unfortunately the motion was just filed a
20 couple of hours ago, so I would request that we push
21 that off to the end of the day so we can have an
22 opportunity to discuss it with all the parties. It is
23 the same exact motion that was filed and approved last
24 month and I'll ask that we just push that off to the end
25 of the day.

1 THE COURT: So we're now on the
2 additional budget for continuing cash collateral, docket
3 No. 44 in this book, but it's some other docket number.

4 MR. McDOWELL: It is docket number --

5 THE COURT: 3158?

6 MR. McDOWELL: Yes, Your Honor. And I'll
7 turn it over to Ms. Coleman now.

8 THE COURT: All right.

9 MS. COLEMAN: Thank you, Your Honor. I
10 don't believe we have very much of an issue here. This
11 request is for the use of cash collateral for another
12 four weeks. Pursuant to the budget that was attached to
13 our motion, we have agreement from everybody who has an
14 interest in the cash collateral; i.e., the Noteholders
15 and Bank of America.

16 The committee filed an objection, I
17 believe, based on their view that the budget included
18 amounts to be paid to professionals that are due and
19 owing and they don't think the professionals should be
20 paid. However, the committee, as you know, has no
21 interest in the cash collateral and we believe that the
22 budget is appropriate and should be approved given the
23 approval from everybody who does have an interest in the
24 cash collateral. So we would ask that the Court enter
25 the order allowing Scopac to use the cash collateral

1 pursuant to that budget for the next four weeks.

2 THE COURT: All right. Does anybody have
3 anything to say now?

4 MR. FIERO: Your Honor, to properly
5 characterize our objection, our objection is that
6 Bankruptcy Code Section 506 doesn't allow unsecured
7 creditors to receive their attorneys fees or expenses
8 under their loan documents, and that is all we're
9 objecting to. We're not objecting to the continued
10 payment of Gibson Dunn and the other professionals of
11 Scopac. But with regard to any monies that would go to
12 the Fulbright firm, to any of the Indenture Trustee's
13 valuation professionals, those amounts are only
14 available to over secured creditors.

15 This Court has found that the Indenture
16 Trustee is an undersecured creditor. This Indenture
17 Trustee has admitted that it is an undersecured
18 creditor. And so it's just fine if everybody wants to
19 agree that those fees can continue to be paid except for
20 the fact that it's not allowed by the code and this
21 company could use the money.

22 Your Honor, we expect that this case will
23 end with a conclusion that will provide certainty to
24 everyone in a reasonable period of time. The request is
25 to use cash for the next 30 days and the committee

1 doesn't see any reason why Scopac should jeopardize its
2 cash position any further by the continued payment of
3 attorneys fees and other professional fees to the
4 Indenture Trustee's professionals. We don't want to
5 come back in here and talk about the Lehman DIP, we
6 don't want to hear that Scopac is out of money, and the
7 easiest way to do that is, one, not approve the budget
8 that's been put forward which provides for the payment
9 of these fees which should not be paid; and two, order
10 the disgorgement of the fees which has been paid to date
11 which is the subject of the separate motion, Your Honor,
12 which is on calendar for today.

13 MR. JONES: Your Honor, Evan Jones on
14 behalf of Bank of America. We certainly don't object to
15 the debtor using cash collateral to operate. I think
16 there is perhaps an issue over the payment of the
17 Indenture Trustee's fees that the Court might want to
18 resolve today, at least going forward. And I haven't
19 actually read the pleading, but I'm told that the
20 Indenture Trustee filed about an hour ago a pleading in
21 response to the whole disgorgement motion.

22 As Your Honor knows, there's been a
23 motion filed saying the Indenture Trustee has to give
24 back all the fees he has received. We filed a semi
25 joinder saying well, it certainly -- those fees ought to

1 be applied to any administrative claim that the
2 Indenture Trustee has. I gather, I haven't read it, but
3 I gather the Indenture Trustee takes the position no,
4 those fees get applied just to our general secured
5 claim. It would strike me that at least in a going
6 forward basis if the Court is inclined to permit further
7 fees to be paid to the Indenture Trustee, it ought to at
8 least be clear in the order going forward that those
9 fees have to be applied to any administrative claim that
10 the Indenture Trustee has.

11 We will suggest at the appropriate time
12 that that ought to be the case with all of the fees that
13 have been paid, but it seems to me it is incumbent to at
14 least resolve today, since we now know there apparently
15 is an issue over what you do with those fees, we ought
16 to resolve at least on a going forward basis what
17 happens to them. Thank you, Your Honor.

18 THE COURT: Okay. What was the deal -- I
19 was going to ask Mr. Greendyke anyway. What was the
20 deal we had with respect to the fees? We didn't have --
21 we had a deal to where I thought that there was some
22 accounting -- there was going to be an accounting of the
23 fee.

24 MR. GREENDYKE: I mean, I think that's
25 always your prerogative and your power, Judge.

1 THE COURT: Right. But I thought that
2 that was part of the deal to use cash collateral in the
3 first place was that there was the big fight over the
4 fees and there was a settlement of that with some sort
5 of deal.

6 MR. GREENDYKE: The deal -- I wasn't
7 there when the deal was being made, or at least not
8 standing here with Ms. Coleman when the deal was being
9 made, but my understanding of the deal was that there
10 was a limit, there was a collar on how much of the fees
11 could be paid so that the debtor would be able to work
12 through its cash flow needs on an ongoing basis. I
13 don't disagree with anything Mr. Jones just said about
14 the pendency of the disgorgement motion and the Court's
15 ability either with the disgorgement motion or
16 ultimately to decide if we're an unsecured creditor,
17 that you can allocate those fees to principle or admin
18 claim. It's the same dollars, it's just a question of
19 which column you put those in at some point or fashion.
20 We don't object to their use of the cash collateral.

21 And the only other thing I want to say
22 before I relinquish the podium is that I don't
23 necessarily agree with the order of proceedings that was
24 set forth by Mr. McDowell. This is another motion I
25 think that should precede in being dealt with by the

1 Court, any consideration of the confirmation order and
2 that's the settlement motion that the debtor filed in
3 connection with the Headwaters litigation. I think
4 that's a dispositive motion. That is an important
5 motion on our client and that after the Court gets done
6 with the 507 claim --

7 THE COURT: There is a settlement of the
8 Headwaters agreement?

9 MR. GREENDYKE: There is a settlement of
10 the lawsuit that the debtor filed against the Indenture
11 Trustee disputing the nature and extent of the --

12 THE COURT: The lien on the Headwaters
13 agreement.

14 MR. GREENDYKE: Right.

15 THE COURT: Okay.

16 MR. GREENDYKE: That's been settled. I
17 think that needs to be dealt with before we start
18 talking about --

19 THE COURT: And which debtor filed that?

20 MR. GREENDYKE: Scopac.

21 THE COURT: And has that been settled?
22 Is there agreement among all the parties as to the
23 settlement or has there been objections to the
24 settlement?

25 MR. NEIER: No, Your Honor, there have

1 been objections.

2 THE COURT: Okay. And who are the
3 objecting parties?

4 MR. NEIER: The pleadings have come so
5 fast and furious I may forget some people but Marathon
6 has objected, I believe the committee has joined in that
7 objection, Mr. Jones may have joined in that objection,
8 I'm not sure. I think actually Palco joined in that
9 objection.

10 THE COURT: Okay.

11 MR. GREENDYKE: I think the standing to
12 make that objection is the committee. Marathon -- I
13 don't understand how Marathon would have an objection to
14 its settlement with Scopac since it's not a creditor.

15 MR. PACHULSKI: Your Honor.

16 THE COURT: Yes.

17 MR. PACHULSKI: Excuse me. This is Isaac
18 Pachulski, I apologize. I don't think I'm interrupting
19 but I'm not there. I certainly apologize for not being
20 there, but because of surgery last week I really can't
21 be hobbling around airports and courts, otherwise I
22 would have been there in person. And I appreciate the
23 opportunity to participate by phone.

24 On this issue of the payment of the
25 Indenture Trustee's fees, there's one fact that I think

1 has been lost site of. Those fees have been paid out of
2 the Indenture Trustee's cash collateral. So let's
3 pretend that I don't know the number. Let's pretend
4 it's \$6 million, all right? If the \$6 million hadn't
5 been paid, we would have had \$6 million more cash
6 collateral. And as the Court recognized -- so there
7 would be \$6 million more in the bank account subject to
8 our lien, so it's a wash. It can't be applied to our
9 administrative claim because it would simply have meant
10 that there would have been more collateral for our
11 claim.

12 So instead of \$2 and a half million in
13 the account that was addressed in the footnote in Your
14 Honor's findings that required that the Noteholders be
15 compensated, there would be \$8 and a half million in the
16 account. So this is really much ado about nothing
17 because it's a wash. Our collateral was used to pay the
18 Indenture Trustee so instead of having \$8 and a half
19 million in the account or \$9 and a half million in the
20 account, there's \$2 and a half million in the account.
21 It's that simple. Thank you, Your Honor.

22 THE COURT: Okay. But Mr. Pachulski, if
23 there was \$8 and a half million in the account and now
24 there's \$2 and a half million in the account and you
25 think you're entitled to a \$6 million administrative

1 claim because of that, if that \$6 million was given to
2 you, why wouldn't that be that a wash against that \$6
3 million?

4 MR. PACHULSKI: Your Honor, that was
5 actually dealt with in the brief and when the -- and
6 actually, in the brief when the Indenture Trustee went
7 through the computation, the Indenture Trustee -- and
8 Mr. Greendyke and Mr. Strubeck can correct me because
9 they're more familiar with it. They did not ask for an
10 administrative claim, I believe, for the amount of the
11 diminution in cash collateral. That's attributable to
12 the payments to the Indenture Trustee.

13 THE COURT: Well, if that's the case then
14 it would probably be a wash.

15 MR. PACHULSKI: Okay. And that's my
16 understanding of what the brief says.

17 THE COURT: Okay. Good.

18 MR. PACHULSKI: Thank you.

19 MR. NEIER: Your Honor, we don't believe
20 that's a correct statement of what's in the brief.

21 THE COURT: Okay. But somebody is going
22 to have an accountant on the stand that's going to tell
23 me how all this stuff -- when we started the case, how
24 much money there was, how much everything there was,
25 what's been paid out, what's left and what's left over

1 at the end and we can properly account for
2 Mr. Pachulski's statement if it's correct as to how it
3 applied and that they are not counting for diminution of
4 cash amounts that were paid to them, then it ought to
5 all wash out.

6 MR. NEIER: Absolutely correct, Your
7 Honor.

8 THE COURT: If that's what the
9 accountants are doing and it's being done, all right,
10 then we don't really have an issue.

11 MR. NEIER: Yes, Your Honor.

12 THE COURT: Go ahead.

13 MS. COLEMAN: Your Honor, I simply wanted
14 to put some numbers on this and to answer Your Honor's
15 question about the amounts. You are correct, there was
16 a deal struck a little over a year ago, actually it was
17 exactly a year ago today pursuant to which the Indenture
18 Trustee would be paid some but very clearly at that
19 time, and certainly it's been borne out by the passage
20 of time, not all of its fees. And the deal was that the
21 Indenture Trustee's professionals collectively would be
22 paid \$100,000 out of Scopac's operating cash every month
23 and then up to \$150,000 for a total of \$250 out of the
24 SAR account, and so that's how these payments have been
25 made and they have all been made pursuant to that

1 stipulation. I would also just point out that -- and so
2 as a result of that, the Indenture Trustee's
3 professionals have been paid nothing like what their
4 actual fees are and Your Honor is going to have to
5 figure that out in connection with the 507(b) claim.

6 The Scopac budget that we're asking for
7 approval of now includes \$759,000 in payments to the
8 Indenture Trustee's professionals collectively. And the
9 reason that it is that amount is that they have not been
10 getting paid because of these liquidity issues in the
11 SAR account and because of some of the terms of the
12 second amended cash collateral order, so it's to some
13 extent catch-up. But I just wanted to make the point
14 that we're not talking about these large numbers.

15 I would say finally, Your Honor, the
16 termination of whether the Indenture Trustee is fully
17 secured or not has been made by this Court. It is
18 not -- it is not yet a final determination and Scopac's
19 view is that given it is the Indenture Trustee's cash
20 collateral, we are willing to continue making the
21 relatively small fraction of the actual cost and fees
22 incurred going forward as we -- as we go forward and
23 ultimately determine where these monies are going to be
24 allocated and how they're going to be counted against
25 the claim if in fact they are and if in fact it is

1 finally determined that they are undersecured. But we
2 would simply say that there is no reason to finance the
3 operations of the company off of -- off of the law firms
4 that are providing service here. That goes for
5 everybody, even though the specific objection is only to
6 the Indenture Trustee in this connection. Thank you.

7 MR. JONES: Your Honor, Evan Jones. I
8 was here when the deal was struck. Your Honor may
9 recall I think it was the first time we saw Mr. Clement
10 in this case. And I agree with the Court's description
11 that the deal was that if it turned out the Indenture
12 Trustee was undersecured, that the Court could make
13 appropriate rulings on what happened with the -- how you
14 reallocated the payments that have been made.
15 Mr. Bolton was kind enough to leave a copy of their
16 brief on the disgorgement at dusk for me this morning so
17 I read it quickly.

18 If Mr. Pachulski's description, though,
19 is the position of the Indenture Trustee, I think that
20 does resolve my concern. We just want to make sure that
21 we don't double count in the sense that they say we have
22 an administrative claim because the cash collateral
23 disappeared even though it was going to the Indenture
24 Trustee's counsel. So if that's the Indenture Trustee's
25 position as described by Mr. Pachulski or Your Honor's

1 order this morning, we have no problem with the -- or
2 this afternoon, we have no problem with the cash
3 collateral.

4 THE COURT: Okay. Well, I'm going to
5 hold off on ruling on this cash collateral just simply
6 because I don't know that it's important to rule on it
7 right this second and I have this feeling it's all going
8 to work itself out in the course of the -- I mean,
9 because this administrative claim issue is really tied
10 to the issue of whether -- how much money should the --
11 how we deal with the monies that were paid to the
12 Indenture Trustee.

13 So all of that issue -- the whole issue
14 of disgorgement, the issue of whether you ought to pay
15 them now, I don't think it's enough to worry about quite
16 honestly. I agree with the committee that normally we
17 do not have payments of fees for lawyers of undersecured
18 creditors, I agree with that, nor do we lend them the
19 money pending disposition of paying that amount of money
20 that they might have of their secured claim which they
21 could then carve out. But on the other hand, it's what
22 we've been doing. You know, sort of the past practice
23 of this case. But so rather than have to rule contrary
24 to the law, I would prefer to see how this goes and see
25 where we are.

1 MS. COLEMAN: Your Honor, of course,
2 that's privileged.

3 THE COURT: I don't think -- think we
4 have to resolve all of that in resolving this whole
5 administrative claim issue.

6 MS. COLEMAN: Your Honor, I think that's
7 absolutely right. I would just point out and maybe we
8 can come to some way of accommodating this, but Scopac
9 doesn't have the authority to spend any money after
10 midnight tonight, so that basis --

11 THE COURT: Okay. So can we reserve the
12 issue of the trustee's fees? They're in the budget but
13 we're not going to pay those and go forward with this
14 and rule on that perhaps later in the week after we have
15 had the whole administrative claim deal?

16 MR. GREENDYKE: Yes. I think -- I
17 haven't had an opportunity obviously to check with my
18 client but I think we have to -- we have to tell you --

19 THE COURT: Okay. So between now and
20 later today, midnight tonight.

21 MR. GREENDYKE: I think probably the best
22 way to resolve it is to reserve our right to request
23 that we go back to the way it was and if something
24 happens that we can't resolve it tonight, then you sign
25 an order that says subject to that right of further

1 consideration of that prior convention that we have all
2 been following that they get to use that cash
3 collateral, they get to write checks tomorrow.

4 THE COURT: There is one way, in just
5 thinking it through, that it could impact the overall
6 bottom line of the confirmation order, if there ever is
7 one; and that is if it's being taken off the amount
8 that's owed, there's no real way to do that based on the
9 confirmation -- based on the findings that I made. I
10 just found that -- I just found that the maximum based
11 on the evidence that I have that it was worth the 510
12 and if you paid at least 510 that's there.

13 So if you carve down your claim somehow
14 and you still get 510 or some amount over it based on
15 the whole -- it does make an impact, in other words. So
16 if it can all be dealt with in the administrative claim
17 deal, then it doesn't make an impact. If it -- in other
18 words, if it's -- but we'll see how it works.

19 All right. Let's move on. So we're
20 going straight on with the 507 or whatever. I'm so good
21 with numbers. So your claim.

22 MR. GREENDYKE: Yes, sir.

23 THE COURT: Who's doing it?

24 MR. GREENDYKE: Mr. Strubeck.

25 THE COURT: Okay. Good. I have a number

1 of proffers, so do you have -- who are your witnesses?

2 MR. STRUBECK: Your Honor, again, Louis
3 Strubeck. I hope you were as excited as you suggested
4 that I am going to be making this presentation on the
5 507(b) motion. But we have got three direct -- two
6 direct witnesses that we have submitted proffers.

7 THE COURT: Okay.

8 MR. STRUBECK: And the first of those is
9 Mr. Joseph Radecki and we are calling him as an expert
10 on the effective financial markets and conditions and
11 the value of stressed and distressed -- distressed and
12 stressed assets and companies. He's the first one. And
13 then James Fleming. You heard Mr. Fleming testify in
14 connection with the confirmation hearing.

15 THE COURT: All right.

16 MR. STRUBECK: We have other witnesses,
17 but those are the only two that we have submitted
18 proffers.

19 THE COURT: I notice there are also a lot
20 of designated deposition testimony, etcetera.

21 MR. STRUBECK: Correct, Your Honor.

22 THE COURT: Now, are we going to just
23 consider the testimony concerning at confirmation as to
24 values as to be considered as the testimony that's being
25 presented on the value as of the date of confirmation?

1 MR. STRUBECK: Yes. I had understood,
2 Your Honor, I was here earlier and I'm going to talk
3 about that in a little bit as well, but I understood you
4 to say you did not want to get into any issues of
5 reconsideration of value decisions that you made
6 pursuant to the confirmation hearings. So with that in
7 mind, we have assumed for purposes of this motion and we
8 have reserved all of our rights with respect to whether
9 this moves into another direction, that the findings you
10 made are the findings that apply as to the values as of
11 the confirmation hearing, if that helps.

12 THE COURT: All right. Thank you. So we
13 have two witnesses for you. Now Marathon, how many
14 witnesses are you calling?

15 MR. NEIER: Your Honor, we have directly
16 with respect to Marathon, we have Mr. LaMont and
17 Mr. Johnston, but in addition there are several officers
18 and debtors, they are also on the Indenture Trustee's
19 list so we're trying to figure out if they're going to
20 call them or we're going to call them, but they would be
21 Mr. Young and Mr. -- and Dr. Barrett as two of the
22 witnesses. And there are several others that
23 Mr. Strubeck may want to call as well and we'll see
24 where we get to.

25 MR. STRUBECK: Yes, Your Honor, you had

1 asked me initially about the witnesses that we had
2 proffers for and I told you who those two were.

3 THE COURT: So you have some cross.

4 MR. STRUBECK: We have some cross. We
5 have a witness that we are going to call adversely as
6 well, which is Mr. Dean.

7 THE COURT: Who is that?

8 MR. STRUBECK: Mr. Dean, Sandy Dean. And
9 we also intend to call Mr. John Young, who is the acting
10 chief financial officer for Scopac. He was one of the
11 individuals that Mr. Neier just referred to.

12 MR. NEIER: So in response, Your Honor,
13 the only additional officer we would call on 507(b)
14 would be Dr. Barrett potentially.

15 THE COURT: Okay.

16 MR. NEIER: In addition to Mr. LaMont and
17 Mr. Johnson and Mr. Dean, depending on whether they call
18 him adversely or whether then we call him for our direct
19 and what have you.

20 THE COURT: All right. Now, what about
21 Scopac, are they calling witnesses?

22 MR. FROMME: Your Honor, we submitted
23 proffers. Eric Fromme, Gibson Dunn & Crutcher on behalf
24 of Scopac. We submitted proffers of John Young, Scopac
25 CFO, and Dr. Barrett, Scopac's CEO. And those are the

1 witnesses that we will present. If they call them
2 adversely, then they will call them adversely.

3 THE COURT: Okay. So is there any reason
4 why we shouldn't just take them -- I mean, is there some
5 reason why we shouldn't just get their proffer on first
6 and then you do whatever you want. You're not bound by
7 the proffer but it might be -- I don't know if that
8 would be a quicker way to do it or would you prefer to
9 call them first on cross?

10 MR. STRUBECK: I think we prefer to call
11 them first on cross.

12 THE COURT: Okay.

13 MR. STRUBECK: In the case of our adverse
14 witness, Judge.

15 THE COURT: Okay. Any other parties that
16 were going to call a witness? Okay. So it looks as
17 though in terms of live witnesses, Joseph Radecki,
18 Fleming, Dean, Young, LaMont, Johnston and Barrett. Is
19 that correct?

20 MR. STRUBECK: That's correct, Your
21 Honor. Now, it may be that in the course of this,
22 depending upon how the testimony evolves, but there will
23 be other witnesses who will be called. But as things
24 stand right now, that's the best estimate that I can
25 give you.

1 THE COURT: Good. Make an opening
2 statement?

3 MR. STRUBECK: Yes, sir, if I may.
4 Again, Your Honor, Louis Strubeck on behalf of the
5 Indenture Trustee. I had a question, Judge, because we
6 were debating on our side today just how much time we
7 had for opening statement purposes.

8 THE COURT: How much do you want?

9 MR. STRUBECK: Well, I don't think it's
10 going to take as long as I had thought initially. I'm
11 assuming that I'm going to make a closing argument.

12 THE COURT: You are going to get to make
13 a closing argument.

14 MR. STRUBECK: But here's the question,
15 Judge. On our side we thought it was somewhere between
16 30 minutes and an hour and a half. Mr. Schwartz told me
17 he thinks it's an hour and I will be happy to tailor my
18 opening statement in terms of however the Court wants to
19 hear it with the proviso that I have a couple other
20 lawyers on my side which would include Mr. Davidson who
21 represents some of the Noteholders individually and
22 Mr. Gibbs. So whatever time you decide is appropriate,
23 I will reserve some time so they can make some comments
24 if they want to.

25 THE COURT: Okay. Well, how about 45

1 minutes?

2 MR. PACHULSKI: Excuse me, Your Honor,
3 this is Isaac Pachulski. I believe that on this part
4 Mr. Davidson has ceded our involvement to me on the
5 opening statement. Same time, just different person
6 with a beard.

7 THE COURT: Okay. So can we do it in 45
8 minutes a side?

9 MR. STRUBECK: I know I can, Your Honor.

10 THE COURT: Is that good for the other
11 side?

12 MR. NEIER: Your Honor, that's okay for
13 the people that are the plan proponents, that is the
14 committee, Mendocino and Marathon. We haven't consulted
15 at all or know who else is giving an opening statement
16 from either Scopac, Palco, I see Mr. Jones rising so
17 those are not what I would traditionally think of as our
18 side. But there are other people who have interest in
19 this motion.

20 THE COURT: Okay.

21 MR. JONES: Your Honor, Evan Jones on
22 behalf of Bank of America. We'll just reserve
23 everything for closing. I did have a procedural
24 question though that I just wanted to make sure I know
25 the rules. There are obviously a number of motions that

1 we have before the Court. And there have been some --
2 the discovery was done on a combined basis, I believe.
3 Are we going to try to take --

4 THE COURT: We are not doing anything
5 other than the administrative claim at this point.

6 MR. JONES: Thank you, Your Honor.

7 THE COURT: However, I find it very
8 difficult to separate the administrative claim issue
9 from this disgorgement issue. So it seems to me that
10 while it may be a separate motion, it may get surpassed
11 by the ruling on the administrative claim. That issue
12 may get all taken care of in this hearing and so
13 everybody needs to understand that the legal issue of
14 all of that may have to be determined in terms of some
15 sort of accounting for the administrative claims, which
16 may be as simple as Mr. Pachulski says as just saying we
17 got it, it would have been part of this, and we got it,
18 so we're not counting that as a part of our
19 administrative claim. And if that's the case, then
20 that's good. That's easy. Okay.

21 MR. JONES: Thank you, Your Honor. I was
22 really concerned more about the potential stay.

23 THE COURT: There hasn't been anything
24 appealed right now.

25 MR. JONES: Thank you, Your Honor.

1 THE COURT: We're not requiring anyone to
2 argue any of that. I just wanted people to be aware of
3 the fact that this case now had a two-week delay and it
4 was probably all my fault, but regardless of that fact,
5 we're going to move quickly. I don't know how this
6 turns out. I haven't seen the evidence, I haven't seen
7 the arguments. And actually, it's the first time this
8 specifically kind of an issue has ever come up in a case
9 so -- in my 20 years. So we're going to try to decide
10 that and if we have a plan confirmed, I know that the
11 one side, whoever is -- whoever loses is going to want
12 to stay pending appeal and so I would like people to be
13 prepared to do that quickly and that's what I asked you
14 to be ready for in the event we get to that point.

15 MR. JONES: Yes, sir. Thank you, Your
16 Honor.

17 THE COURT: But it will be a separate
18 hearing, different issue. Go ahead.

19 MR. STRUBECK: Thank you. Your Honor, I
20 want to echo what Mr. Greendyke said when he came up
21 initially and that is welcome back. I have a sense that
22 in the courtroom today there's probably a difference of
23 opinion between the Court and everybody else here as to
24 how happy we are that you're back. You're probably not
25 quite as happy to be back as all of us are to see you

1 but in the two weeks that you've been gone, we've had a
2 lot of things to do in this case and I think we are
3 prepared, as you had asked us to do, at least the last
4 time I was before you, to present all the things that
5 you're expecting to be presented this week in rapid
6 order. And depending upon how you rule on different
7 things, that's going to dictate what you hear in what
8 order.

9 But Judge, I was thinking that one of the
10 lasting impressions that you probably had as a result of
11 the two weeks that you spent out of town was one that
12 was similar to the one that I had when I was at the same
13 place that you were at. And that has to do with kind of
14 the history of where you were and also value. In
15 particular, how your American dollar was able to be
16 stretched or not stretched when you were spending it
17 overseas. And coincidentally, Judge, those are pretty
18 much the same things we're going to talk to you about or
19 at least you're going to hear about in terms of the
20 super priority administrative expense claim that I'm
21 presenting this afternoon.

22 And Judge, you know, it sounds
23 complicated but the more that I got into this, and you
24 know that I'm kind of a Johnny-come-lately to this case.
25 It really is pretty simple. And again, we think it's

1 all about history and as a subsection of that integrity,
2 specifically your Court's orders and findings in
3 connection with the cash collateral and in connection
4 with the confirmation hearing that concluded not all
5 that long ago, and we think that the testimony that
6 you're going to hear, and I'm going to outline that for
7 you quickly in a second, is going to show you that from
8 a historical standpoint, all we're really asking is that
9 the integrity of the history in the case, the positions
10 taken by the parties in the case, and your findings and
11 your conclusions and your orders be respected.

12 And they fall into two categories.
13 Again, they fall into the findings you made consistently
14 with respect to cash collateral issues; and they fall
15 into the findings that you made with respect to the
16 confirmation issues. And you asked me a second ago the
17 starting place for all this was going to be the value
18 that you determined for purposes of the confirmation
19 hearing. And it is, in addition to some of the findings
20 that you made that helped you get to that value at the
21 end of the day.

22 So what you're going to hear from our
23 side, Judge, is history is history, integrity is
24 important as a subsection of that, and like you said at
25 the confirmation hearing, it's still all about value, to

1 a certain extent. And we maintain, and we base frankly
2 this position a lot on the findings that you made, that
3 the value significantly declined, at least from
4 September 2007 to the confirmation hearing date. And
5 I'm going to show you in a little while some of the
6 particular findings that I'm referring to in that
7 regard.

8 And so really all I've tried to do,
9 Judge, or I should say we tried to did is to kind of
10 take back the September 2007 date, or October 2007 date
11 to the petition date and try to show you what happened
12 to the value of our collateral from the petition date
13 through and including I guess it would be June the 6th
14 when you issued your findings and conclusions.

15 THE COURT: Now, is it true that we've
16 got two separate things to look at, one is an accounting
17 for cash collateral.

18 MR. STRUBECK: Correct.

19 THE COURT: I mean, cash and cash
20 equivalents and things of that sort; and another is the
21 value of the real estate.

22 MR. STRUBECK: Exactly. And as a matter
23 of fact, you're helping me advance my opening statement,
24 Judge. And what I was about to tell you is there kind
25 of -- there's a hard piece and there's an easy piece.

1 Again, we think this is pretty easy overall, at least as
2 far as how our argument is going to be structured and I
3 think they think it's easy too for different reasons.
4 Because we're just going to say here it is, Judge, here
5 are your orders, here are your findings, and based upon
6 these orders and findings we think it's been established
7 there's been a decline in value and we think you've
8 already established, Judge, that we're entitled to an
9 administrative, actually it's super priority
10 administrative expense claim and that all that remains
11 to be done in that is for you to quantify what that is.

12 You're going to hear them say something
13 different about that, but again, back to the point where
14 I think we're not trying to do revision of history like
15 I think Marathon and MRC are. You're going to hear some
16 astounding things in the course of this and you're going
17 to hear them say that the value of the timberlands
18 actually went up during the course of the case. And I
19 don't see how you can possibly reconcile that with the
20 evidence they put on and the proposed findings they
21 asked you to make, many of which you adopted but you're
22 going to hear that.

23 And I think you're going to hear from us
24 that our position has really been unchanged. We said
25 from day one, we thought we were protected by an equity

1 cushion but we told you the value was going down every
2 time we had a cash collateral hearing and you have
3 confirmed in your mind, at least, that the value has
4 gone down. So again, we're going to start with your
5 confirmation findings and then we're going to try to
6 build on that and take you back to the petition date.

7 Real briefly, Judge, in terms of
8 background, we filed this motion on May 2nd. There's no
9 deadline set yet for filing any kind of motions for
10 administrative expenses. In fact, that deadline really
11 can't come into effect until the confirmation order is
12 entered, and as I understand it under the plan that you
13 have indicated you're going to confirm, there's 60 days
14 before administrative expense motions need to be filed.
15 So we filed ours early.

16 In fact, there's no deadline that's even
17 approaching at this point in time and we did it because
18 we didn't want to play hide behind the law. We wanted
19 to bring it up just in the event that Your Honor
20 concluded the value was less than we thought it was
21 going to be.

22 THE COURT: So let me just say that if
23 you really didn't want to hide behind the law, somebody
24 at the stand should have said during the confirmation
25 hearing this little tiny adjustment to the 530, that

1 adjustment might be \$200 million. Nobody said that.
2 Now, maybe I should have figured that out myself, but I
3 mean, that's a big enough hickey that usually
4 somebody -- I'm not -- I'm not holding that against you.
5 I'm just saying we all failed to see the significance of
6 this May 2nd motion in the confirmation because if you
7 have a \$200 million claim, there's no way that they can
8 confirm the plan, this plan for certain.

9 MR. STRUBECK: Correct. And we talked
10 about that, Judge, and at the risk of reintroducing a
11 word that I think you probably would not like to hear
12 again, snookering. When I came in here on June 9th, I
13 hadn't been involved in the case all that much up until
14 then, as you know. And I came in and argued a motion
15 for continuance because at that point in time this
16 motion had been scheduled for trial, I think that
17 Friday, Friday the 13th.

18 And so we had all the lawyers who
19 appeared on the phone or in person have a dialogue about
20 the whole motion, the filing of it, the timing of it,
21 whether people had overlooked it. And my only point is,
22 Judge, when we filed the motion -- there are good and
23 bad things about standing up here today. One of the
24 good things, I suppose, is I wasn't here during a good
25 chunk of the confirmation hearings so I can maybe have

1 others from my side answer that question you posed a
2 second ago later.

3 THE COURT: That's okay.

4 MR. STRUBECK: So the good news is that I
5 came in looking at this kind of fresh and trying to
6 figure out exactly what your thought process was when
7 you entered your confirmation findings and your
8 confirmation orders. And again, when I came in here on
9 the 9th of June to make the argument, I was telling you
10 if we had a fair and reasonable opportunity to present
11 our administrative expense claim, that I thought that we
12 would make a really compelling case and I believe that
13 and I think that we really will.

14 And just as one other aside to take you
15 through the procedural history of this. When we filed
16 the motion that Mr. Greendyke, of course, told the Court
17 we had filed it, and we requested a hearing as is the
18 Court's custom on normal notice and it was set on July
19 the 18th.

20 So we filed it, we didn't wait to have it
21 set and we were prepared for it to be tried on the 18th.
22 The reason we're here today isn't because we asked it to
23 be expedited, the reason we're here today is because
24 they have got a problem based upon the plan that's been
25 confirmed and they're in a box. And what they're

1 basically saying to you is, you know, we're going to
2 postpone the effective date of our plan unless we know
3 for sure that there's no administrative expense claim,
4 in this case the super priority administrative expense
5 claim that the Indenture Trustee has. So just to bring
6 us up to where we are, that's the reason we're here
7 today. We're here because of all the issues that this
8 claim and the potential magnitude of the claim presents
9 and that's what you get to resolve, I guess, over the
10 course of the next couple of days with hopefully help
11 from all the parties.

12 I want to start, Judge, with a little
13 presentation I've got. And first of all, the value of
14 the Noteholders primary collateral, timberland and the
15 cash equivalents have declined by at least \$170 million
16 during the pendency of the case. We said that in the
17 brief we filed yesterday. I know you have a whole lot
18 to catch up on and you probably didn't have a chance
19 to --

20 THE COURT: I did get your brief
21 actually. Since it was lately filed, it was one of them
22 I did get to look at. I sort of went backwards but go
23 ahead.

24 MR. STRUBECK: Okay. Well, I'm glad
25 you've seen it then and that will probably shorten some

1 more of my opening statement. But anyway, for starters,
2 Judge, this is the position that we take as far as the
3 decline of value, diminution in value of our position
4 since the petition date. And actually, Judge, that
5 finding, as you're going to see in a second, is geared
6 or proposition is geared to a specific series of
7 findings by you under the confirmation hearing.

8 That number can actually go up. If you
9 start with the proposition that from the beginning of
10 the case, Scopac really believed, and from what I've
11 seen, Judge, I think you probably did, too, that there
12 was a whole lot more value here than you concluded on
13 the confirmation hearing date was here.

14 And so if you assume that the value was
15 significantly higher back when the first cash collateral
16 order was entered and throughout the pendency of the
17 case, then that \$170 million number actually goes up
18 significantly. That number is based primarily on -- if
19 you flip to the next one, please. That number is based
20 primarily, Judge, on what you're going to hear our
21 appraiser say the value was as on the petition date.
22 And that's going to be a later slide.

23 I want to go back for a second to talk
24 about why I think this is simple. And we said this, I
25 think, in our brief. We start with the proposition,

1 Judge, as you can see on the screen that the Court
2 granted the Noteholders a super priority cost of
3 administration under 11 U.S.C. 507(b) to the extent of
4 post petition diminution of its interest in the
5 timberlands and its cash collateral in its final order
6 authorizing use of cash collateral pursuant to Section
7 363 of the bankruptcy code and in all of its final cash
8 collateral orders. Would you do the next screen,
9 please.

10 And Judge, now what I just want to show
11 you is the first of these final orders that Your Honor
12 had entered. And again, we highlighted the language
13 that we think is appropriate. This is -- the screen
14 that's up now is the first order, the first final order
15 that was entered on March 9, 2007. Would you flip to
16 the next screen, please. The next screen, Judge, is the
17 second final order that was entered and you can see it's
18 got exactly the same highlighted language as far as Your
19 Honor's granting to us a super priority cost of
20 administration priority claim. Third one, please.

21 And finally, Judge, the third final
22 order -- I always like it when there are different
23 variations of final orders, but the third final order,
24 this one agreed authorizing the use of cash collateral,
25 and this one, I believe, was entered on March 18, 2008.

1 It says 2007 but I think that's 2008. And once again, I
2 just refer the Court to the highlighted language that
3 clearly reflects that the trustee is granted a super
4 priority cost of administration priority claim under
5 section 507(b).

6 So, Judge, our position for starters is
7 we have a grant of a super priority cost of
8 administration. You've ordered it. It's the law of the
9 case. No one has appealed any of these orders. And so
10 the only thing that remains for you to do is to decide
11 whether there's really been a diminution in value. We
12 think there is, as the first screen indicated, and that
13 that diminution value is at least \$170 million. And
14 there is two components to that as Your Honor has
15 pointed out.

16 Next screen, please. The first one,
17 Judge -- I'm going to take these in reverse order as far
18 as magnitude. Obviously the most significant of the two
19 is going to involve the decline in value of the
20 timberlands. And we believe, Judge, and I'm going to
21 show you a screen on this in just a second, that that
22 value decline for the timberlands is at least in the
23 range of \$100 million to \$153 million and that's based
24 upon some findings I'll show you in a second. But I
25 want to take the other part of this first because I

1 don't think it requires quite as much analysis and
2 consideration of testimony and evidence as you're going
3 to have to go through, unfortunately, on the timberlands
4 value. And this screen is meant to just show the
5 decline in value of cash and cash equivalents in excess
6 of \$40 million. And you can see, Judge, that on January
7 18, 2007, the beginning cash and cash equivalents
8 position -- and this is all reflected in the monthly
9 operating report that was recently filed was
10 \$46,888,930. There's a comma missing and a number
11 missing. On the right-hand side, the cash equivalent
12 balance, according to what Mr. Young just testified or
13 just referred to in his declaration is that it's
14 \$5,047,057. So there's a decline in the value of cash
15 and cash equivalents in excess of \$40 million.

16 Next slide, please. And all that is,
17 Judge, is the monthly operating report that was just
18 recently filed and highlights the numbers that you saw
19 in the prior screen, the beginning cash number and the
20 ending cash number.

21 Next screen, please. Now, going to the
22 decline in the timberlands collateral between the
23 petition date and the confirmation hearing date. On
24 January 18, 2007, you can see that we've listed two
25 values, the first of which is \$758 million, the second

1 of which is \$646 million. We then fast forward to the
2 October valuation, the course of which is Mr. Fleming,
3 who was the Indenture Trustee's valuation expert during
4 the confirmation hearing. And then finally you get to
5 June 2007, the confirmation date. And the footnotes
6 reflect this progression. The \$758 million number that
7 we used is based upon what we believe a fair assessment
8 of what Scopac was telling you from the beginning was
9 approximately what the value was for these timberlands.

10 And there's actually, Judge, a portion
11 from a transcript back in December of 2007 and you
12 didn't make a particular finding about this, but in
13 deciding what you were going to do with the cash
14 collateral issues then, you indicated that there was a
15 suggestion to you that the forest is worth way more than
16 \$758 million. That's where that quote comes from. So
17 this is just to depict, I told you at the very beginning
18 we think the claim is somewhere north of \$170 million.
19 It can actually be much higher depending on what you
20 thought the value of this was back when you first
21 entered your initial cash collateral order.

22 Next slide, please. Now, Judge, in your
23 June 6, 2008 findings, and this is the piece I talked
24 about earlier in terms of how we're relying on your
25 findings and conclusions. And by the way, we think that

1 Marathon and MRC are bound by them because you adopted
2 most of what they proposed in terms of findings. The
3 Court repeatedly found that log prices had significantly
4 dropped in the last six months by as much as 10 to 15
5 percent and particularly in young growth redwoods, and
6 concluded that this drop resulted in a decline in the
7 timberlands value.

8 Next screen, please. So here is the
9 first of the findings, Judge, and I'll spend much more
10 time on these in closing, but your finding No. 111
11 reflects that in the last six months log prices have
12 dropped significantly by as much as 10 to 15 percent,
13 basically reiterates the first part, the last slide was.
14 Likewise, Douglas Fir prices are at an all time low.
15 Next, this decrease in log prices is attributable to the
16 economic slowdown, particularly in the housing market,
17 which has resulted in a decline in building and
18 remodeling activity. You're going to hear Mr. Radecki
19 tell you the same thing, Judge. Mr. Lamont's analysis
20 accounts for this decline in pricing.

21 Next slide, please. You found, Judge,
22 that Mr. LaMont is a credible witness whose testimony
23 deserves significant weight and whose conclusions are
24 given great weight by the Court.

25 Next slide. Log prices have dropped

1 significantly from October 1, 2007 to the present by as
2 much as 10 to 15 percent. Again, particularly in young
3 growth redwoods. Recent market sales of young growth
4 redwood logs indicate that the price is more
5 appropriately valued around \$800 to \$850 per thousand
6 board feet.

7 Next slide. Mr. Fleming's appraisal is
8 currently only through October 1, 2007. And Judge,
9 that's the reason the other chart I showed you had the
10 middle valuation that Mr. Fleming had provided. And
11 just to refresh the Court's recollection, he had said
12 during the confirmation hearing that the value was \$605
13 million then. The finding goes on to say "despite the
14 considerable drop in log prices during the six month
15 period from October 1, 2007, through the present time,
16 Mr. Fleming made no efforts to update his findings to
17 reflect the value of the timberlands during this time.
18 He did not know that redwood prices have declined since
19 October 1, 2007, the date of his appraisal."

20 Next slide. All this is finding 158.
21 Changing only this one price of this one type of log to
22 \$800 to \$850 MBF and keeping all other aspects of
23 Fleming's report the same reduces Fleming's valuation by
24 \$100 to \$153 million, dropping his fair market value of
25 the timberlands from \$605 million to \$452 million.

1 That's a specific finding, Judge, that I referred to in
2 the beginning of my opening.

3 Next slide, please. That's the last one?
4 Mr. Fleming's -- I'm sorry. Yeah. Next finding is 206.

5 "However, redwood prices have been stagnant for over a
6 decade from 1992 through December 2007, the price has
7 been flat. Moreover, the price of redwood has
8 experienced a recent decline due to the slowdown in the
9 economy and the presence of competitor products on the
10 market. This is significant because a likely buyer of
11 the timberlands will look at a short-term business cycle
12 in evaluating log prices. As Mr. Yerges concedes, his
13 inflated price increased results in a \$150 to \$200
14 million increase in his valuation price."

15 All right. Judge, and I said earlier
16 that, again, I think from our perspective this is all
17 about history, a subsection of that is integrity of the
18 process and then, of course, value. And what we have
19 attempted to do with this screen is just to show you
20 your findings, and they're all the findings that I just
21 went through. On the left-hand side and how they relate
22 to the proposed findings that MRC/Marathon is requesting
23 in connection with the order that you ultimately -- the
24 findings, I should say, that you ultimately entered.
25 And the only conclusion that anybody can draw from this

1 slide is that with the exception of, I think, one
2 sentence that they have proposed in a finding you
3 adopted basically on your read of the testimony all
4 these findings that were proposed by Marathon and MRC.

5 I think that's really important, Judge,
6 again, from a history standpoint. Again, from an
7 integrity of the process standpoint because what you're
8 going to hear them say is that value -- the value of
9 these redwoods, the value of these timberlands went up
10 between the petition date and the confirmation date.
11 And frankly, based upon these findings that they have
12 proposed, based upon your findings, we think, A -- well,
13 we think, Judge, that under the doctrine of judicial
14 stopple, they are precluded from coming in here and
15 trying to say that.

16 THE COURT: I guess the question I would
17 ask, though, just right off the bat is am I supposed to
18 decide the value at the beginning of this case based on
19 how someone who didn't know what the future held would
20 have determined the value to be? Or now that we've
21 already had the case, am I supposed to look at the value
22 and take into consideration what I know to happen in the
23 period following -- in other words, most of the
24 valuation testimony is predictions of future.

25 MR. STRUBECK: Correct.

1 THE COURT: Part of the future at the
2 time of filing, we know what happened. So is there any
3 case law on the issue of how you determine a value at a
4 date -- not the date now where we're always looking into
5 the future and everybody's crystal ball, but a value at
6 a date in the past.

7 MR. STRUBECK: You definitely have to go
8 back in time and it's a tricky proposition. And
9 coincidentally, Judge, that is something that is being
10 done or was done before Judge Hamen and the Asarco
11 litigation that was sent his way. And so what you have
12 to do is go back in time and try to figure out what
13 values are, I think, at least this is the argument I
14 made in that situation, based upon what was known or
15 expected to happen at that time.

16 And what you're going the hear
17 Mr. Radecki say, Judge, and I think what we told you at
18 the confirmation hearings, at least based upon the
19 transcripts I read and the motions that were filed, is
20 we thought we were oversecured at the beginning of the
21 case, but we thought that values were going down. And I
22 think that's a story that we have consistently told to
23 the Court. And you know, we were surprised come
24 confirmation time when you came up with the value that
25 you did. But since we're not here today to reargue

1 those values, again --

2 THE COURT: Well, I mean -- well, let's
3 don't go there. Continue on.

4 MR. STRUBECK: So Judge, that's what
5 we're trying to show here. We know that you're going to
6 start with the values you concluded and you've got to
7 back in time and figure out what the values were on the
8 petition date. And perhaps even times in between, but
9 overall you're going to frame value in the petition date
10 versus value that you end up with on the confirmation
11 hearing date and you're going to come up with the number
12 that you believe represents a diminution of value of our
13 claim.

14 We think we don't have to do as much
15 effort with that as we might otherwise have to do
16 because we have findings from you that talk specifically
17 about the decline in value from October until the
18 confirmation hearing date. So it may be all we're
19 urging you to do, Judge, is to go back in time from
20 September of 2007 to January and try to figure out if
21 there is any further diminution. We think you've
22 already framed the diminution that you believe existed
23 from October until the confirmation hearing date so we
24 have to go back a little farther.

25 THE COURT: We didn't have a valuation

1 hearing early in the case, did we? We had cash
2 collateral hearings.

3 MR. STRUBECK: Correct.

4 THE COURT: But we didn't have experts
5 from each side coming in and testifying as to the value
6 and findings as to values. We all had theories and we
7 all had ideas of what everything is worth. Go ahead.

8 MR. STRUBECK: I'm just looking at my
9 watch, Judge, and I think I've used up about 30 minutes
10 of my time if I am correct and I don't want to deprive
11 my colleagues of an opportunity, but I just wanted to
12 let you know how we view this case and we don't think
13 it's that complicated for you. And I appreciate the
14 Court's time and I'll talk to you again during closing.

15 THE COURT: All right. So now we have
16 Mr. Pachulski.

17 MR. PACHULSKI: Thank you, Your Honor.
18 First, if I may, I would like to start actually out of
19 order and try to amplify the answer to the question you
20 asked about valuation. Since the whole purpose of
21 adequate protection is to protect someone from what they
22 lost, had this property been valued on the petition
23 date, what's been lost is the opportunity that the
24 secured creditors would have to sell the property at
25 some point. So you have to ask yourself how would

1 someone have valued the property at that time. In
2 addition, I believe that you'll find it in the
3 fraudulent conveyance LBL cases where somebody is trying
4 to determine the value of the debtor for purposes of
5 figuring out whether there was a fraudulent conveyance,
6 you don't get to go and say, well, look at what really
7 happened. The test is based on what was known at the
8 time or what you could have found out at the time, what
9 are the values.

10 So I really think what you have to do is
11 put yourself in the position of how this property would
12 have been valued on petition date. But going back to a
13 main point that Mr. Strubeck made, which I think has to
14 be a central theme of this hearing. This hearing, more
15 than any other I have seen really is about the integrity
16 of the Court's prior orders. This Court entered
17 multiple orders that specifically provided for a super
18 priority administrative claim for diminution in value.
19 This provision was not negotiated in the dead of night
20 in a dark room.

21 Nobody -- it was done on the record.
22 Marathon didn't object, the creditor's committee didn't
23 object. These orders are final. And what you have
24 really, Marathon's entire thing if you look at their
25 brief, is they say to the Court, you need to stand on

1 your prior orders. For example, they want to start from
2 scratch and say, okay, what is the test for super
3 priority claim? And they say well, let's start from
4 scratch, you don't meet that test. You took care of
5 that here, Your Honor. And let me give you a couple of
6 examples of the kinds of arguments they made that are
7 completely precluded by this.

8 One of their arguments is that we
9 shouldn't be compensated for the diminution of the
10 collateral because we didn't seek relief from the
11 automatic stay. Well, to begin with, the Indenture
12 Trustee didn't sit on its hands, saw the determination
13 that this was a single asset real estate case and lost.
14 Now, what they're saying is we shouldn't have -- we
15 should have moved for relief from the stay even though
16 it's very clear from the way the Court ruled on cash
17 collateral that we had zero chance of getting relief
18 from the automatic stay.

19 But the most important point of all is
20 that in this order, in these series of orders, Your
21 Honor gave the Noteholders everything they would have
22 gotten in the way of adequate protection on a motion for
23 relief from the automatic stay. You already told the
24 Noteholders that you have a claim not just for the
25 diminution and cash collateral but for the diminution

1 and value of all your collateral, and that's what this
2 order says. And I don't know what thought processes
3 people have, but orders mean what they say. And this
4 order is crystal clear.

5 Similarly, Marathon makes the argument
6 that we shouldn't have an administrative claim because
7 the estate didn't benefit from using the timberlands.
8 Now, that's kind of a bizarre argument since the estate
9 controls them, operated them and they were basis of the
10 estate's attempt to reorganize. Marathon's argument as
11 well, you only harvested 2 percent of the timber that
12 was on the timberlands so it was no real benefit to the
13 estate. Number one, that argument is absolutely
14 precluded by the language of this order.

15 But number two, that may be the silliest
16 argument that anyone makes in this case because, as we
17 all know, you don't harvest timber by helicoptering in
18 and removing the logs. You have to have access. You
19 have to have the entire timberlands so you can go back
20 and forth, so that you can take the timber in and out,
21 so that people can get in and out. And so the argument
22 is silly and it's good cocktail conversation, but that
23 argument is also precluded by your order.

24 Your order basically said this is how we
25 measure the claim, and all -- the only issue before Your

1 Honor today as a matter of -- because of what has been
2 done in this case is how do we measure the diminution in
3 value. Now, to argue there's not a diminution in value
4 Marathon and MRC now have to attack the integrity of
5 your findings, and I would like to highlight the way
6 they've done that. We present an appraisal of the value
7 of the property as of the petition date by Mr. Fleming.
8 They say, well, Your Honor disbelieves Mr. Fleming.

9 And why did Your Honor not find Mr.
10 Fleming credible? You didn't find he was a bad guy or
11 anything. You said gee, he only did this as of October
12 2007 and Mr. LaMont and the debtors have convinced me
13 that he made a mistake because since 2007, the value of
14 the timberlands has gone down between \$100 and \$150
15 million because of the decline of log prices. So what's
16 basically going on here is they're trying to discredit
17 Mr. Fleming because of Your Honor's finding that he
18 should have taken into account that the collateral went
19 down in value by between \$100 and \$150 million. And
20 then they're saying, by the way, the value of the
21 collateral didn't go down. That may work, you know, in
22 1984 or something, in the book 1984 by George Orwell
23 where people could hold two contradictory thoughts
24 simultaneously, but it doesn't work in a court.

25 Now, in terms of diminution value,

1 there's only one other point I'd like to address because
2 there's a piece of conventional wisdom in this case
3 that's absolutely wrong. The piece of conventional
4 wisdom is that the growth in the forest during the case
5 increased value. It's wrong because it's double
6 counting.

7 And I think Your Honor can quickly grasp
8 why it's double counting when you remember how the
9 people did the appraisals in the confirmation hearing.
10 Everybody who did an appraisal said you take into
11 account the growth in timber in your appraisal, and this
12 is projected growth, either in your discounted cash flow
13 because you're harvesting the timber in the future and
14 generating cash or in your terminal value for the assets
15 because if the forest is bigger when you sell the forest
16 in ten years or 50 years, you get more money.

17 In other words, any buyer, any appraiser
18 who would have calculated the value of this asset in
19 January of 2007 would have taken into account the
20 projected growth in the forest as part of the valuation.
21 So if you're going to say, well, the forest was worth X
22 on January 2007 but we're going to add the growth in the
23 forest, you have double counted. And it's kind of
24 interesting. Mr. LaMont does this double counting
25 because he doesn't really give you an appraisal of what

1 the property was worth in 2007. He said well, you
2 should increase it here, you should increase it there.
3 And one of his increases is for the growth in the
4 forest. But had he done an appraisal in January 2007
5 and had he figured out a discounted cash flow and a
6 terminal value, he would have already imbedded the
7 projected growth in the forest in that value and
8 terminal cash flow. And unless someone is going to
9 argue that the forest grew faster than would have been
10 projected in January 2007, and that's not in any
11 proffer, but unless there's that argument, the growth in
12 the forest is completely irrelevant because any buyer as
13 of January 2007 would have assumed the forest grows
14 because we all know forests grow and if you're
15 experienced in this industry and you buy a forest,
16 you're going to assume the forest grows. So that
17 argument goes by the wayside. And if you take away that
18 argument, what you're left with essentially is a huge
19 drop in log prices that is established by Your Honor's
20 findings from October of 2007.

21 There's no -- I don't think there's going
22 to be any argument that log prices went up between the
23 petition date and October of 2007. So your prior
24 findings are basically a binding predicate for the floor
25 of measuring the diminution in value that Your Honor

1 ordered. And so for that reason as a matter of law
2 we're entitled to a claim, the only issue is how much.
3 Thank you.

4 THE COURT: Okay. Yes, sir, Mr. Gibbs.

5 MR. GIBBS: I wasn't certain I was close
6 enough to a mic back there to tell the Court that I
7 think that I was going through my notes for what to talk
8 to you about in opening remarks, but my colleagues
9 Mr. Strubeck and Mr. Pachulski has covered all those.
10 I'd rather not dogpile and reserve my time for the end
11 of the hearing. I do echo their comments. We are
12 vitally concerned about the integrity of the process and
13 if those orders mean what they say, it's only a matter
14 of establishing the amount of our claim today.

15 THE COURT: All right. Who's on first?

16 MR. JONES: Your Honor, I apologize. I
17 said before I wasn't going to speak. I would like to
18 ask for one minute.

19 THE COURT: Okay.

20 MR. JONES: Literally one minute. I
21 don't care if it's at the end or at the beginning now.

22 THE COURT: Well, he's closer to the mic
23 so go right ahead.

24 MR. JONES: Thank you, Your Honor.

25 MR. NEIER: Good afternoon, Your Honor.

1 David Neier on behalf of Marathon. Your Honor, this
2 claim should be denied for three principle reasons.
3 One, there's no decline in assets that has taken place
4 in this case. You heard from Mr. Pachulski, their
5 entire case is really based on one fact and one fact
6 alone. A fact we do not dispute, a fact that was in the
7 findings of this Court, which is that there was a huge
8 drop in log prices since October 2007, since October 1,
9 2007. And all of the Court's findings that were flashed
10 on the screen show that there was a huge drop in log
11 prices since 2001 -- since October 1, 2007.

12 However, Your Honor, this case did not
13 begin on October 1, 2007. It began in January of 2007.
14 And since January of 2007, there has not been such a
15 decline in assets. In fact, assets have substantially
16 increased. Second, the Indenture Trustee has not stated
17 an allowed administrative claim. And third, the
18 Indenture Trustee never moved to lift the automatic
19 stay. It was granted and you saw on the screen several
20 times it was granted cash collateral for one thing and
21 one thing only. It was a motion under 363 for use of
22 cash collateral. There was no motion for adequate
23 protection under 362, meaning lifting the automatic
24 stay. And there was no motion for adequate protection
25 with respect to a 364 motion; that is, priming DIP lien

1 or a priming of the Noteholders collateral. And so you
2 have to look at the use of the collateral. And the
3 problem with the Noteholders argument, of course, is
4 that this is a unique property, unlike almost every case
5 they have in bankruptcy, the assets appreciate because
6 they grow, there is a biological term.

7 In almost every case we have in
8 bankruptcy, property is used and therefore it
9 depreciates. That is not this case. The trees grow.
10 That makes this case different. That's why there are
11 more trees today than there were before and in fact,
12 there is more cash and cash equivalents than there were
13 before.

14 Specifically with respect to the decline
15 of assets, you're going to hear testimony and it's
16 unrefuted testimony, it's absolutely the case, that the
17 trees grow faster than they were cut. In fact, you
18 heard that several times during the cash collateral
19 hearings that you had. There were 74 million board feet
20 that were harvested in 2007. There are going to be 74
21 million board feet harvested in 2008. In each one of
22 those years, the trees grew faster than they were cut.
23 And the unrefuted facts that will be presented to Your
24 Honor show -- and they were presented before, this is
25 not new testimony, that there were 55 million more board

1 feet in the forest, in growth than was harvested. So a
2 total of 140 million board feet in total was grown in
3 2007 and another 140 million were grown in 2008. And so
4 there's 55 million board feet each year, a total of over
5 100 million board feet since this case began have been
6 added to the forest. And of that 100 million board
7 feet, approximately 70 million board feet is what we
8 call conifer or the soft woods or the valuable woods or
9 the redwood and the Doug fir. So the trees grow faster
10 than they are cut.

11 Well, what about working capital?
12 Working capital is really a combination of the cash and
13 the cash equivalents and there was a very clever chart.
14 Maybe we can have a picture of the operation part that
15 Mr. Strubeck put on the screen. Mr. Strubeck pointed
16 you to the cash and he showed you that \$48 million
17 became \$5 million. Actually, he had \$48,000. I sort of
18 like that number. But let's say it was \$48 million and
19 it became \$5 million.

20 What he didn't point to you was the total
21 current assets going from \$54 million to \$51 million.
22 Just a \$3 million decline according to the monthly
23 operating reports that were defined in this case. And
24 why is that? Because as in every bankruptcy, cash at
25 the beginning of the case gets turned into working

1 capital. It gets turned into account receivables.
2 There's now \$11 million in the account receivables. It
3 gets turned into inventory. There are prepaid expenses,
4 capital improvements. There are now the investments
5 which are listed separately. There was no investment in
6 auction rate securities when this case began. That
7 investment was made in March of 2007. There is now \$26
8 million in auction rate securities. So when you add it
9 all up it's not 48 to 5, it's 54 to 51 when you're
10 looking at the non-timberland assets.

11 Let's look at the background on this
12 claim. The Indenture Trustee filed this claim, as the
13 Court may remember, on the night before the very last
14 day of testimony before the Court closed the record. It
15 was clearly an attempt to derail the MRC/Marathon plan.
16 And you know, Mr. Strubeck says well, we knew our
17 collateral was declining, we certainly knew there was a
18 problem since October 1, 2007, since we had all of this
19 evidence that there had been a large price decline since
20 October 1, 2007. Okay. But that wasn't just known when
21 we got here in court, that was known in March 2008 when
22 the parties signed a disclosure statement.

23 There's not a single word in the
24 disclosure statement about the Indenture Trustee having
25 a super priority administrative claim or suffering a

1 massive diminution. It is they who created this claim
2 at the last minute to try and derail the MRC/Marathon
3 plan, and it may very well be successful but they had a
4 duty and obligation to this Court and to the creditors
5 and since the Court approved the disclosure statement as
6 having adequate information to say that they had in fact
7 suffered diminution. They did not do so. Why didn't
8 they do so? Because they don't have such a claim.

9 In fact, when they filed the claim, when
10 they filed the claim, their own expert, Mr. Fleming, who
11 you're going to hear testimony, was not even consulted.
12 He wasn't even asked whether there had been a decline
13 since the petition date. That was all done afterwards.
14 They filed the claim at the last minute to try and
15 derail it and then they proved it up later, or they
16 attempted to.

17 Now let's talk about the forest. That's
18 the main asset of this. You have the forest and the
19 working capital.

20 THE COURT: We're going to get to that.
21 Your legal issue.

22 MR. NEIER: I have several legal issues.

23 THE COURT: I know. But one of your
24 legal issues is that they're not entitled to
25 administrative claim, and yet it is true that any

1 diminution in the value was in the orders, wasn't it?
2 Those orders, if -- I mean, normally there is a motion
3 to lift the stay and then the value or differences.
4 Here we have the SAR, which is similar to a motion,
5 let's say. It basically shortens the stay, it shortens
6 everything. But regardless of that fact, if we did
7 those cash collateral, and we put that language in there
8 and everybody got a hack at it. I mean, everybody
9 looked at that. I mean, if you were thinking that
10 somehow because they didn't file a motion to stay, why
11 didn't you object to that language earlier in this case?

12 MR. NEIER: Well, I probably would have
13 been shot down as having no interest in Scopac in the
14 first place.

15 THE COURT: Maybe not you then. What
16 about the committee? The committee agreed to it.

17 MR. NEIER: You know, I think the
18 committee deeply regrets what happened with respect to
19 that cash collateral. They certainly didn't expect to
20 be surprised. And Your Honor, I think you're going to
21 find that the law is a little bit different than what
22 the Noteholders would ask you to believe. What the
23 Noteholders asked you to believe is on day one of this
24 case, Scopac came into the court and they asked you for
25 consent to use cash collateral under Section 363, not

1 under 362 or 364, and they put in this diminution
2 language and later on the Indenture Trustee agreed to
3 that language and Bank of America agreed to that.

4 But does that mean that they have an
5 allowed administrative priority claim on that civil
6 date, no need for any proof, it's all been done, it's a
7 final order of the Court? Of course not.

8 Can you go to our brief for a second.
9 Your Honor, there are numerous, numerous cases that talk
10 about the fact that when a Court grants in an order a
11 super priority administrative claim, that does not mean
12 that the claim does not have to be proven. That somehow
13 the secured creditor gets more rights than they would be
14 entitled to under the code simply because they had an
15 allowed quote unquote super priority administrative
16 claim.

17 Your Honor, I've been representing
18 secured creditors for virtually all of my career. And I
19 put in every cash collateral order for a bank that there
20 must be an allowed super priority claim. And if you
21 read the DIP order on the Palco side, you will see that
22 there's an allowed super priority administrative claim
23 for Marathon. Okay. What is that about? That's the
24 debtors acknowledging that if there is diminution, there
25 will be an allowed super priority administrative claim.

1 And that is -- and that is noticed to --

2 THE COURT: So in this case,
3 acknowledged.

4 MR. NEIER: Right.

5 THE COURT: But you're suggesting that a
6 third-party isn't bound by that?

7 MR. NEIER: And there is notice to all
8 the parties because you put it in the order, okay, that
9 there could be by virtue of use of cash collateral or
10 dip or priming dip, there could be an allowed super
11 priority claim.

12 But as all these courts found, simply
13 because there was a stipulation that allowed a super
14 priority claim does not mean you don't have to prove the
15 claim. The claim still needs to be assessed. If I say
16 well, Judge, if I do anything wrong in my book or if I
17 say to the extent that there is diminution, I'm allowed
18 a super priority claim, that's true. You still have to
19 prove your claim.

20 THE COURT: Okay. One of your arguments
21 is that because they didn't file a 362 motion, they
22 can't have a super priority claim.

23 MR. NEIER: For market loss. For market
24 loss. Okay. They can have --

25 THE COURT: A value of the --

1 MR. NEIER: They certainly are entitled
2 to a super priority administrative claim for any use of
3 the debtors' collateral, absolutely. If the debtor uses
4 the collateral, okay, under this order, they should be
5 allowed a super priority administrative claim. So if
6 there's any diminution as a result of the use of the
7 collateral, they should be allowed a claim. But that's
8 different from saying -- this's different from saying
9 that, well, the forest declined in value, okay.

10 The forest declined in value and
11 therefore -- and even though I didn't move to lift the
12 automatic stay to ask for my collateral back and
13 foreclose on it, I don't think you'd get a higher value,
14 but they could try. Because they didn't do that, you're
15 not stopped. You're not allowed to go back in time and
16 say, well, if we had known that there was going to be a
17 market loss, we would have moved to lift the automatic
18 stay. They were here the entire case. They knew where
19 everything was going.

20 They saw the change in business and they
21 saw what was happening since October 1, 2007. Are you
22 telling us that we can just sit there with an order, lie
23 back in our chair, do absolutely nothing since October
24 1, 2007 when \$150 million gets burned up and I have no
25 responsibilities because the Court signed an order on

1 January 17, 2007? That doesn't make any sense.

2 THE COURT: Why would it make any more
3 sense then if at the time they filed the SAR motion that
4 said in the alternative lift the stay and I would have
5 denied the motion to lift the stay and denied the SAR
6 motion. I don't know that they would have appealed the
7 motion to stay to the Fifth Circuit but they appealed
8 the SAR motion and I was upheld so I probably would have
9 been upheld on the other two.

10 MR. NEIER: We didn't address this in our
11 brief but the Second Circuit in LMC versus Fidelity has
12 said it's an open question. It's an open question
13 whether the denial of a motion to lift the automatic
14 stay can result in a super priority administrative claim
15 because a denial of a lift stay motion is not a granting
16 of adequate protection. So to answer Your Honor's
17 question, that would not necessarily result in a super
18 priority administrative claim, and be glad you don't
19 have to get into that tricky legal issue.

20 Your Honor, with respect to the forest,
21 you know, Mr. Fleming did his valuation at the very
22 height of the market in October of 2007. He looked at
23 the trees and he said they were worth \$600 million in
24 October 1, 2007. And this Court has seen lots of
25 evidence since October 1, 2007, these debtors have been

1 in peril and that there has been a decline in prices and
2 that affects their cash flow. But, you know, the test
3 is not October 1, 2007. And you know, the Court rightly
4 found that Mr. Fleming should have valued the collateral
5 as of the time of confirmation. That's the standard,
6 not six months before confirmation. And that's why the
7 Court, in part, did not attribute much value to
8 Mr. Fleming's testimony.

9 But diminution in value is not from the
10 highest point in the market to when confirmation
11 happened. It's from the petition date or whenever there
12 was a grant of adequate protection until June of 2008.
13 And I'm confident when you see the evidence, not only
14 are there more trees because they grew fast and they
15 were cut, there were also more harvestable areas. And
16 the unrefuted testimony in front of you is going to be
17 that the debtors have done watershed analysis and as a
18 result of that watershed analysis, millions of board
19 feet have been now cleared for harvesting that were not
20 previously available for harvesting. And that increases
21 the value of the property.

22 So you know, that's one of the points.
23 But another point is I take exception to what
24 Mr. Pachulski says about use of collateral. It is only
25 the collateral that you use, of course, that can be

1 subject to a motion with respect to a super priority
2 claim. There is no case, there is no case, I challenge
3 anybody to find a case which says that collateral that
4 simply sat there and was not used can be the subject of
5 a super priority administrative claim.

6 THE COURT: There were 74 million board
7 feet cut each year.

8 MR. NEIER: And there are 4 billion board
9 feet in the forest. 74 million board feet equals two
10 percent of the forest, less than two percent. So less
11 than two percent of the forest was used in 2007. We're
12 halfway through 2008.

13 THE COURT: I should look to the 74
14 million or the 148 million board feet that were cut and
15 if that was devalued during this period, if it was
16 sitting there and went down because it burned up in a
17 big fire out there, that that would be a diminution
18 because it was used but the part that grew, assuming it
19 did not burn up was not used.

20 MR. NEIER: And it grew faster. There is
21 now more trees than there were. There were 74 million
22 board feet cut in 2007 in harvestable timber, but there
23 was 130 million board feet that actually grew or 140
24 million board feet that actually grew on that property
25 in 2007. And the same thing is happening in 2008. The

1 debtor is going to testify that they -- that they expect
2 to cut about the same in 2008 as they cut in 2007 and
3 the trees are once again growing faster than they were
4 cut. So the courts have consistently held, and I have
5 never seen a case to the contrary where a debtor simply
6 does not use collateral, simply retains the collateral,
7 nobody moves to lift the automatic stay, that's not
8 diminution. It's just sitting there, it's not being
9 used, it's not being depreciated. In fact, here the
10 collateral is being appreciated.

11 There are also capital improvements to
12 the forest. There were roads added, there was
13 maintenance done, there were bridges added. There were
14 all sorts of things that were done that are reflected on
15 the debtor's books and records as an increase, as a
16 capital improvement in the property. And once again,
17 that is unrefuted testimony that all that value was
18 added. As you know, Your Honor, one of the things that
19 are going to happen under the MRC/Marathon plan is we're
20 going to do a lot of road building, a lot of capital
21 improvements. But there's already been some of that
22 done because that has to be done for state regulatory
23 reasons. So that counts to increase the value of the
24 property, just as any capital improvement on any real
25 estate counts towards increase in the property.

1 What's really going on here is this
2 timing game. I mean, Mr. Strubeck said well, you should
3 look at the petition date and the confirmation date but
4 maybe some dates in between. And Mr. Pachulski says
5 well, you really should look at October 1, 2007 because
6 there has been a big decrease since then. But they
7 don't talk about what happened between January 17th and
8 October 2007, and they don't talk about the increase in
9 the trees.

10 I mean, this is very much like a stock
11 drop case. I go to the height of the market in October
12 2007, I look at where it is today, it's vastly lower
13 because I went from the height of the market down to the
14 low of the market and I somehow think I've got a claim
15 without looking at the entire bankruptcy period. That
16 is, the entire bankruptcy case from January 17th to June
17 2006 -- 2008.

18 I'm just sort of skipping ahead, Your
19 Honor, just give me a second. In addition, Your Honor,
20 you know, a lot of the professional fees that were paid
21 in this case to the Noteholders, that would not
22 constitute an administrative claim. That would simply
23 constitute the Noteholders using their own collateral.
24 And the Noteholders also agreed to a car vouch in their
25 collateral to pay the committee and Bank of America, and

1 that should also not be part of any super-priority
2 administrative claim because that was done by the
3 Noteholders. They consented to that from their own
4 collateral.

5 So we think that you've heard testimony
6 that Scopac's business is cash flow positive excluding
7 professional fees. Well, you saw the figures before, 54
8 to 51. Guess what? If you look at how much the
9 Noteholders have been paid, this estate is cash flow
10 positive, this estate is asset positive, even without
11 regard to the forest which increased in size, increased
12 in every way, shape or form. The same is true with
13 professional fees if you except out the professional
14 fees that are not the debtors because if the debtors do
15 use the collateral that should result in the diminution
16 claim but if you take out the other professional fees
17 that were paid from the collateral, there is no claim.

18 And although Mr. Strubeck didn't mention
19 it, Your Honor saw that there was now, you know, a
20 decline in cash but an increase in investments and the
21 investments are two things, one, the timber notes and
22 two, the auction rate securities. Well, the auction
23 rate securities, I didn't hear any mention of that from
24 Bank of New York because, of course, that's an account
25 that they have at their institution and that's an

1 investment that they recommended to the debtors to be
2 invested in. The fact that the investment has become
3 illiquid cannot be valued but, of course, the forest is
4 also an illiquid investment. And if you did buyer sale
5 liquidation of any illiquid investment, of course you
6 would have a decline in value. But that doesn't mean
7 the auction rate securities have a decline in value but
8 if they do, that really is the Noteholders problem and
9 they should just be returned their cash equivalent
10 investment and used as how they would.

11 It shouldn't hurt the Noteholders if the
12 Noteholders have a claim against somebody at the debtors
13 or somebody at Maxxam that provide management services
14 to Scopac or against Bank of New York as the Indenture
15 Trustee that recommended this investment. That would be
16 their claim.

17 Your Honor, you're going to hear a lot of
18 testimony about this October 1 date. I thought I'd show
19 you some of the evidence that's in the marketplace with
20 respect to the decline in values since October 1.

21 Everything that we've done for you is entirely
22 consistent, contrary to the argument that the
23 Noteholders are trying to make that somehow that we've
24 missed over value or that we're changing our mind.
25 There was a decline since October 1, 2007 but since the

1 beginning of this case, there's actually been an
2 increase.

3 If we can have the market presentation.
4 Your Honor, there is the S&P global timber & forestry
5 index. And it's hard to see in this case just because
6 the screen is a little fuzzy, but this index is made up
7 of some of the leading timberland companies in the
8 United States and around the world. And Plum Creek,
9 Rayonier, top latch oil companies that the Court has
10 heard testimony are part of the S&P Global Timber &
11 Forestry Index. If you can go to the screen that shows
12 the index. Your Honor, this is at the beginning of the
13 case. This is from January 17, 2007 through June 6,
14 2008. And as you can see, this is where the index was,
15 the Standard & Poor's Global Timber & Forestry Index in
16 January 17, 2008. This is where it is today. It's up
17 12 percent. But look where October 2007 was. This is
18 October 2007. So yes, since October 1, 2007, there has
19 been a big decline.

20 THE COURT: What does this chart show?

21 MR. NEIER: This is the Standard & Poor's
22 Global Timber Forestry Index, which is made up of the 25
23 largest timberland companies.

24 THE COURT: Prices of timber?

25 MR. NEIER: Stock prices.

1 THE COURT: Stock prices of timber
2 companies during that period?

3 MR. NEIER: Yes, S&P, like the S&P 500,
4 they have other indexes.

5 THE COURT: Okay. All right. I got you.

6 MR. NEIER: Okay. So we have the
7 beginning of this case, we have a sharp run up, we have
8 a sharp decline, we have a sharp run up in October
9 2001 -- October 1, 2007, which is the height of the
10 market when Mr. Fleming did his valuation. And then we
11 have June 6, 2008. There has been a sharp decline but
12 we're still 12 percent ahead of where we were on January
13 17. So this is not a phenomena unique to this
14 particular asset. It was all timberland assets.

15 Can we go to the next slide. Your Honor,
16 there's another index, it's called the Studer global
17 forest and timber something. It's maintained by Studer
18 funds and by Deutsche Bank. Go to the next slide. That
19 index in the beginning in January 17 and through today
20 is up 18 percent. But once again, in October 2007,
21 there was a height of the market and it's declined since
22 then. But the measure is not points along the way. The
23 Noteholders don't get the benefit of a market loss.

24 THE COURT: What is this based on?

25 MR. NEIER: This is now an index of

1 timberland companies that's run -- that's maintained by
2 Studer funds, which is managed by Deutsche Bank.

3 THE COURT: So this is the values of the
4 companies or this is the stock prices?

5 MR. NEIER: Stock prices.

6 THE COURT: But you're comparing stock
7 price -- I mean, no where --

8 MR. NEIER: I'm using comps.

9 THE COURT: It's a figure that we can
10 look at but I don't believe I ever evaluated the value
11 of the company by virtue of stock prices.

12 MR. NEIER: Absolutely, Your Honor, but
13 we're showing you comps and we're showing you that this
14 is not a unique situation that somehow the Noteholders,
15 you know, claim that we're somehow not showing you
16 something that didn't occur in this case. It occurred
17 in every case.

18 THE COURT: Okay.

19 MR. NEIER: You are going to hear a lot
20 of this market forest testimony from Mr. Radecki so
21 we're showing you what it's all about.

22 THE COURT: Got you.

23 MR. NEIER: There's a National Council
24 of Real Estate Investment Fiduciaries. They maintain
25 indexes both for the West, the Pacific Northwest and the

1 timberlands. Can you go down like three pages to the
2 first chart. Go to the next chart. Next chart. Your
3 Honor, this is -- NCREIF is one of the leading people
4 that maintains -- and this is based on property value,
5 not only per acre, and it's done by appraisals. All of
6 these timber management companies, they do appraisals
7 and those appraisals are reported to NCREIF.

8 And as you can see, in 2008 first
9 quarter, both in the Pacific Northwest, which is this
10 dark red column here, there's been an increase, small
11 increase. In 2007 over the year there was a pretty
12 large increase. This is indicating the total market
13 value per acre. As you can see, since 2007, this is the
14 first quarter, second quarter, third quarter, fourth
15 quarter of 2007. There has been a slight increase in
16 the market per acre.

17 Go to the next slide. You may remember
18 we had testimony by Houlihan. Houlihan represented four
19 different comps for Your Honor. We disagreed with those
20 comps but those were the comps they presented. They
21 presented Rayonier, Plum Creek, Pope Resources and
22 Potlatch. Can you go to the first slide. Plum Creek
23 was a company that was 47 percent timberland. Go to the
24 next slide. It is up 12 percent since the petition
25 date. Once again, October, big increase. Coming down.

1 But since January, it's been up 12 percent.

2 Next slide. This is right out of the
3 Houlihan report, as you can see. This is Rayonier. You
4 can see a large portion of this is really performance
5 fibers and only 18 percent is timber. But if you can go
6 the next slide, you can see that this company is also up
7 7 percent since the petition date, January 17. So once
8 again, big spike, October, sharp drop, going down, but
9 overall from the petition date, up 7 percent.

10 Next slide. This is Potlatch. Potlatch
11 has very little of its business in timber, but as you
12 can see, pulp and paper board and consumer products make
13 up a large part of the company. But also they have a
14 real estate section. Next slide. This company is down
15 one percent from the petition date. Once again, there
16 was a spike in value right there, I think it is, in
17 October. But overall, since the petition date, down one
18 percent.

19 Next slight. This is Pope Resources.
20 Now, Pope Resources has a large real estate division
21 that has not done too well. We didn't agree with this
22 comp either. But if we can go to the next slide, it's
23 down 22 percent. There was a spike in October and since
24 then it has gone down. If you can turn to page 10 and
25 11 and of their 10K. This is some of the real estate

1 properties that are in this company that they developed.

2 Go to 11. There's the commercial properties that they
3 are developing. Go to 23.

4 23. Okay. Well, you can see that
5 from -- this is their 10K that's published in March of
6 2008. You can see that feet timber, which is the
7 timberlands they own, you know, revenue in 2006 was \$35
8 million revenue and 2007 was \$35 million. Their real
9 estate division is 50 percent off, goes from 27 to 15.
10 That's where their problem is. That's why their stock
11 dropped 22 percent. If you were to adjust this comp and
12 just look at their feet timber it would not have
13 suffered a decline in value.

14 Then you go to the last slide. Your
15 Honor, these are the timber notes in this case. And
16 you've seen this data before. In the beginning of this
17 case, as you know, after the petition was filed and just
18 on the eve of the petition filed, there was a huge run
19 up in the -- in the price of the timber notes. And
20 today, based on Your Honor's ruling, it's about the same
21 as it was prior to that run up. And yes, there was a
22 sharp decline since October 2007. And that's this case,
23 Your Honor. That's the trading price of the timber
24 notes in this case. Your Honor, you may recall
25 Ms. Keller, my former partner who stood up in front of

1 Your Honor representing one of the Noteholders and she
2 told you basically the market price has priced in the
3 MRC/Marathon plan and that's why the notes trade where
4 they trade today. You may remember that testimony from
5 the argument -- not testimony but argument at the
6 confirmation hearing.

7 Well, isn't it interesting that Your
8 Honor's ruling is about the same. This is where the
9 prices were when this case began. This is also
10 important, Your Honor, because of course, one of the
11 assets that's on the books of the debtors on Scopac's
12 books is about two and a half million dollars of the
13 timber notes face and that asset hasn't changed in value
14 either since the beginning of this case.

15 Your Honor, I think when you hear the
16 testimony in this case, you're going to be convinced
17 that this claim really is what we said it was. It's a
18 specious claim. It was meant to derail the MRC/Marathon
19 plan and it may be successful in doing so if Your Honor
20 finds that there is \$170 million administrative claim
21 that Mr. Strubeck asked you to find. But the mere fact
22 that there was a drop since October 1, 2007 is
23 irrelevant. The Court's job is to look at and determine
24 what the administrative claim is through use of the
25 collateral of the Noteholders. And if you look at the

1 use of the collateral of the Noteholders, it's
2 increased, not decreased. Its value is the same as it
3 was on the petition date. The fact that there was a big
4 run-up and then a big decline, and we question
5 Mr. Fleming as to why he decided to do his valuation at
6 the very height of the market instead of taking into
7 account the changes that occurred in the six months
8 following that valuation date. That was some of the
9 evidence that we used against Mr. Fleming because we
10 felt it was wrong to use a valuation at the height of
11 the market in October 1, 2007 when prices hadn't
12 declined, and we felt it was wrong to support a
13 valuation of \$600 million on that basis.

14 But since the beginning of this case to
15 today, there has been not only an increase in the
16 harvest rates -- sorry, an increase in the harvestable
17 timber, not only has there been approximately the same,
18 a slight decline in the cash and cash equivalents, the
19 working capital of the company and if you were to
20 exclude the Noteholders fees, there has actually been an
21 increase. This business has always been cash flow
22 positive when you exclude the professional fees and it's
23 actually positive when you exclude the Noteholder fees.

24 But in addition to that, there's
25 something else that happened between January of 2007 and

1 this confirmation hearing, which the Court is well aware
2 of. And that was there was a substantial decrease in
3 lending rates. And that was because the federal funds
4 dropped, all the federal fund rates dropped. So Your
5 Honor, you're also going to hear testimony that the
6 discount rate, the discount rate, of course, was higher
7 as of the petition date than it was when this Court
8 ruled. It was substantially higher. And each one
9 percent of the discount rate equals \$70 million in this
10 case. And as Your Honor is aware, the federal
11 government has been dropping interest rates and the cost
12 of capital has declined, and as you know, discount rates
13 are made of the cost of capital and the risk associated
14 with a particular asset.

15 And this is a risky asset, as we
16 presented evidence. It's in California, it has all
17 sorts of regulatory restrictions compared to other
18 timberland properties. But there's no question that the
19 discount rates, it really cannot be questioned that the
20 discount rates from the petition date until today, based
21 on simply the cost of capital, have declined. And when
22 you consider the discount rates in addition to the fact
23 that there are more trees today than there were when
24 this case began, there is really no question that the
25 forest and the timberlands are worth more today than

1 they were and that the Noteholders claim should be
2 denied. Thank you, Your Honor.

3 MR. BRILLIANT: Your Honor, Alan
4 Brilliant on behalf of Mendocino Redwoods. I'm just
5 going to take a couple of minutes. I know that
6 Mr. Fiero has time. I just want to tell you a little
7 bit, you know, of what the evidence that Your Honor is
8 going to hear. You're going to hear two expert
9 witnesses put on by the Indenture Trustee's Noteholders.
10 The first, as I told you, is Mr. Fleming and he's going
11 to give you a valuation now on January 17th or 18th of
12 2007 as to what he thinks the timberlands value was.
13 And Your Honor, he's going to use or has used the same
14 methodology that Your Honor has already rejected when
15 Your Honor valued the company, you know, on June 6.

16 And he's using the exact same
17 methodology. The only thing that he's going to change
18 is two issues of substance. One, is he's going to
19 increase the harvest rate. Yes, Your Honor, he's going
20 to increase the harvest rate even though there's less
21 trees at that date and even though two of the
22 watersheds, two of the WAAs that the company didn't have
23 the right to harvest in didn't occur until some time
24 later than that. So he's going to do that and increase
25 the harvest rate and that's going to increase the value

1 somewhat, but obviously that's methodologically incorrect.
2 In addition to that, he's going to, you know, change the
3 log, you know, pricings based upon what he viewed they
4 would be at that time using the same, you know, mistakes
5 that we believe that he used in his October appraisal.

6 The second expert you're going to hear
7 from the Noteholders is Mr. Joseph Radecki who is an
8 investment banker. He knows nothing about timber at
9 all, never done a timber valuation in his life and I
10 believe, Your Honor, he's not going to tell you that he
11 has. What he's going to tell you is that there has been
12 sub prime prices and, you know, asset classes generally
13 have gone down. And he's going to tell you that that's
14 happened, you know, some time -- I think in his proffer
15 he says midsummer and that it's gone down since then.
16 He's not going to tell you anything about what that
17 means specifically for Scopac because he doesn't know
18 anything about Scopac's assets. And he's not going to
19 tell you anything about what that means from the
20 petition date up until the advent of the sub prime
21 crisis.

22 You're also going to hear from Mr. LaMont
23 who is going to testify on what was different between
24 the petition date and what occurred -- and on the
25 confirmation date. And then you're also going to hear

1 from Mr. Dean. Now, the Indenture Trustee, Your Honor,
2 as you probably remember when we had discovery dispute,
3 had asked Mendocino to produce all of its log pricing
4 information. That was something we never would have
5 thought to look at but interestingly enough, Your Honor,
6 Mendocino in January of '07, actually in a board book in
7 February of '07, actually contemporaneously at that time
8 predicted what it thought log prices were going to be
9 over the next three years. When you put that into the
10 Mendocino model, you're going to find, in fact, that
11 based upon the then contemporaneous forecast of what log
12 prices were going to be in 2007 that the timberlands
13 were worth less in January 2007 than they are on the
14 petition date, not more, as suggested by the Indenture
15 Trustee.

16 That's before Your Honor gets into the
17 entire issue as to whether or not discount rates have
18 come down over the two year period prior to the petition
19 date. I believe that the evidence is going to be, you
20 know, uncontested. They are going to challenge the
21 people who testify about it, Your Honor, but there will
22 be no testimony from either Mr. Fleming nor from
23 Mr. Radecki as to what happened with the discount rates.
24 And instead, the testimony from Mr. LaMont is going to
25 be unchallenged in that regard. Discount rates have

1 come down over the last few years and although log
2 prices may have come down, again, keep in mind, Your
3 Honor, that timberlands are valued with a 50 year model.
4 It may be that there's an expectation that log prices
5 are going to be less for a short period of time given
6 everything that was going on in the housing market.
7 Over the big 50 year scheme of things given the fact
8 that timberlands are viewed as inflation hedges and a
9 commodity and have some other attributes, the discount
10 rate has come down during the bankruptcy period for
11 valuing timberlands. And in effect, you know, the value
12 has gone up and not down during the pendency of the
13 bankruptcy case.

14 THE COURT: All right. Mr. Fiero.

15 MR. FIERO: John Fiero for the Committee,
16 Your Honor. Your Honor, the Committee is interested in
17 the integrity of the process. The Committee cares about
18 nothing more than the integrity of this process. But if
19 we're going to do justice to the integrity of this
20 process, then we're going to have to take a look at what
21 the Noteholders have done over the course of this case.
22 And if we're going to do that, we need to start with
23 September 7th, 2007, just a month before October 10,
24 2007, the date that Mr. Fleming picked for his
25 valuation, and we're going to have to recall that on

1 that day Mr. Di Mauro submitted a declaration to this
2 bankruptcy court, a lengthy detailed declaration on a
3 discounted cash flow basis, not very different from what
4 Mr. Fleming does in his own analysis. You'll recall,
5 Your Honor, that Mr. Fleming doesn't look at comparable
6 sales when he values forest timberlands.

7 He likes to figure out what log prices
8 are, project cutting out for ten years, cap the monies
9 in the tenth year and put those two together and come up
10 with a valuation. It has nothing do with what other
11 timber investors might be doing what they buy companies.
12 It has a lot to do with what Joe logger might do if he
13 was buying 1,000 acres to cut all the trees down.

14 What number did Mr. Chris Di Mauro come
15 up with? Well, Your Honor, he told the Court, and he
16 sat right in that box and he withstood the
17 cross-examination, the withering cross-examination of
18 Mr. Fromme and Scopac about evaluation between \$375 and
19 \$460 million. He didn't tell you at that time that the
20 forest had dropped from some other number at the
21 beginning of this case. The notion that the Noteholders
22 believed they were over secured on the first day of this
23 case is not supported by any document in the record
24 anywhere. They were silent, Your Honor. The committee
25 was silent about the values in this case. There's a

1 good reason for being silent. There was a lot of
2 concern about Scopac's numbers.

3 For whatever reason, the Noteholders,
4 Chris Di Mauro and Houlihan chose September 7, 2007 as
5 the date to come out and tell this Court that it wasn't
6 true, that there was not \$758 million worth of value
7 here, that it was significantly less.

8 Now, how is it that the Noteholders just
9 13 days -- I'm sorry, a month and three days later than
10 September 7 put forward a value in this case that is
11 \$140 million higher than at the smallest amount? Well,
12 the committee doesn't know that the committee is
13 concerned, Your Honor. It isn't the kind of thing that
14 anyone should just take at face value. It is bizarre
15 that we have gone through discussion of the falling
16 value of this company but forgot to go back to the
17 petition date to start, forgot to mention what Chris Di
18 Mauro told the Court in telling the Court what the
19 values are, and both of those things need to be
20 considered by this Court when it hears about the falling
21 of discount rates, the increased interest in timber and
22 the changing market, not for timber, Your Honor, but for
23 timberlands.

24 And why are timberlands different from
25 timber? Because there aren't going to be any more

1 timberlands, Your Honor. They aren't making any more of
2 them. The timberlands are what they are. They are a
3 finite resource. They act differently from other kinds
4 of investments. They are a lot more like oil than they
5 are like residential real estate and stocks in
6 California, Your Honor.

7 And for these reasons, when the Court
8 looks at falling log prices, it has to also ask itself,
9 well, what were investors doing? Do investors care
10 whether or not log prices fell over a six-month period
11 or were they solely concerned with what competitors were
12 paying in the market place, what other timber companies
13 were doing. That's the evidence that's going to be on
14 before you by Mendocino, Marathon and the committee and
15 that's the evidence that you need to focus on. The
16 question of falling log prices, everything they put on
17 their charts about the fact that log prices fell, it is
18 true. We agree. Log prices fell. But it didn't change
19 the way investors viewed timberlands over that 18-month
20 period.

21 And what the evidence is going to show
22 you is just like that NCREIF chart which shows in the
23 line increasing, the value per acre increasing, that
24 investors in the marketplace decided for reasons known
25 only to them that they would pay more for timberlands

1 than they had in the past.

2 Your Honor, with regard to the language
3 in the Court's order, you will recall that Scopac's
4 motion was a motion to use cash. It didn't need this
5 Court's authority to do anything else. It only needed
6 the Court's authority to use the Noteholders cash. At
7 no time did the committee, and I'm sure Scopac expect
8 that it would become the guarantor of the value of the
9 timberlands during this case. That is nonsensical. It
10 is outside the scope of what it was that Scopac intended
11 to do. It's outside the scope of what 363 is there to
12 do. 363 is there to provide a mechanism for the use of
13 cash collateral. The 507 remedy is connected to the use
14 of cash collateral and therefore, it shouldn't be
15 expanded regardless of what the precise words appear to
16 mean on the page. Your Honor, the committee did not
17 intend that and we doubt that the Court intended that.

18 Your Honor, just focusing again on the
19 evidence as Mr. Brilliant did. When Mr. Fleming gets on
20 the stand, one of the first things he's going to say is
21 that his valuation of the forest lands as of the
22 petition date was done exactly the same way as the
23 valuation he did as of October 10, which according to
24 every chart you saw, was about the high point in the
25 interest in timber companies in this country and around

1 the world.

2 And so what that means is he didn't use
3 Scopac's GIS database to develop his harvest
4 projections, he didn't know how to use a GIS database
5 and he used an Excel spreadsheet to arrive at its value
6 after he looked at the interest rates paid on corporate
7 BAA bonds. Your Honor, what could corporate BAA bonds
8 have to do with the value of timberlands? Wouldn't the
9 appropriate measure be how investors in the marketplace
10 view their investments in timberlands? Wouldn't that be
11 the way to measure what an appropriate discount rate is?
12 What you'll hear, Your Honor, is that's how Mr. LaMont
13 chose to view the value of the forest on a relevant date
14 but it's not what Mr. Fleming chose to do and that's
15 another reason why you can ignore what it is that
16 Mr. Fleming has to say.

17 Your Honor, the committee doesn't believe
18 that the claim should be allowed in the amount of even
19 \$1. Forest lands, unlike timber and lumber, have
20 actually appreciated in value during the course of this
21 case. In these uncertain economic times, trees continue
22 to grow. The market has recognized this and we'll prove
23 it. The parties opposing the Indenture Trustee's motion
24 therefore request that you deny the motion.

25 THE COURT: Okay. Thank you. Bank of

1 America, you want one minute?

2 MR. JONES: Yes, Your Honor. I'll even
3 walk quickly.

4 Your Honor, everyone seems to agree that
5 the integrity of this process and the Court's order are
6 important so I want to bring one thing to the Court's
7 attention. Every argument that you have just heard from
8 the Indenture Trustee is different from what's in their
9 motion. Their motion is real simple. Their motion says
10 you ruled, we were over secured and we're not, therefore
11 we have a super priority claim. Ms. Coleman actually
12 pulled out the transcript from those hearings, and Your
13 Honor, I was here, Ms. Coleman was here, Mr. Strubeck
14 says he wasn't here.

15 The Court didn't rule they were
16 oversecured. In fact, I urged the Court and the Court
17 repeatedly said, I'm not going to have a valuation
18 hearing today, I don't need to do that. What I need to
19 do is to find out whether I'm preserving their
20 interests, the value of their interests in the property.

21 Your Honor, when they went to actually
22 read those orders, I'm sure someone from the Indenture
23 Trustee's firm discovered, or perhaps Mr. Clement told
24 them because it's in the order. It says I'm reserving
25 the question of whether they are over secured. Drats,

1 they need a new argument. So Your Honor, this morning
2 for the very first time we get this new argument which
3 is, well, the order says we're entitled to a super
4 priority claim to the extent of the diminution of our
5 interest in the collateral. Two things there I want to
6 note about that, Your Honor. That's not in the motion
7 anywhere. Now, I could have objected to the argument
8 and said it goes beyond the motion. I suspect Your
9 Honor is going to let them put in all of that evidence
10 if they want to but I do want the Court to focus on
11 Mr. Strubeck converts the language in the order. The
12 value of their interest in the collateral. He
13 shorthands that to the value of the collateral.

14 It's not the same thing, Your Honor. And
15 when we close and when we have that evidence in here, I
16 will come back and argue to Your Honor that they can't
17 show there is one cent diminution in the value of their
18 interest in the collateral and that language needs to be
19 understood in light of all of the case law that the
20 Marathon folks have put in their pleading. And now,
21 Your Honor, we understand as to be their argument, we
22 will be addressing in a pleading also. And I think Your
23 Honor will find that there has been no diminution of
24 their interest, of the value of their interest in the
25 collateral during this time period. Thank you, Your

1 Honor.

2 THE COURT: All right.

3 MS. COLEMAN: Your Honor, just to avoid
4 confusion, Scopac did file a response to the 507(b)
5 claim but I'm going to reserve until closing.

6 THE COURT: All right. Palco.

7 MR. McDOWELL: Palco will also reserve
8 until closing, Your Honor.

9 THE COURT: All right. Thank you.
10 Anyone else? All right. Let's get started.

11 MR. KRUMHOLZ: Your Honor, before I heard
12 opening arguments, our first witness as Mr. Strubeck
13 indicated, was going to be Mr. Radecki. It's now going
14 to be Sandy Dean. So we call Sandy Dean.

15 THE COURT: Sandy Dean, okay.

16 MR. HAIL: Your Honor, we had a
17 discussion about the order of the witnesses.
18 Mr. Radecki, they have told us for the last day or so,
19 Mr. Radecki is first. We have an issue with Mr. Dean.
20 We were going to call him on our case in chief and
21 there's a proffer for Mr. Dean. And I don't think we
22 have had a witness yet in this case where we have --
23 that's on both sides of the case.

24 THE COURT: Well, here's the deal. They
25 get to go first. They have the burden of proof of their

1 claim. If they want to call somebody in cross, I think
2 they're entitled to do that. What they are not going to
3 be able to do is they're not going to be able to then,
4 after you put on his proffer, cross him on all of this
5 stuff that they already testified on. So to a certain
6 extent, to the extent that you want to cross him on his
7 proffer at the same time, I'd almost prefer you do that.

8 MR. HAIL: That was my concern, Your
9 Honor, not that they get two bites at that apple.

10 THE COURT: Right.

11 MR. KRUMHOLZ: Your Honor, I'll try to do
12 most of that. I may leave a little bit, but I'm not
13 going to try to do --

14 MR. BRILLIANT: Your Honor, this is Alan
15 Brilliant, I hate to step in front of my partner, but I
16 have a different issue. We asked them who their first
17 witness was. They told us it was Joseph Radecki.

18 THE COURT: Okay. They changed their
19 mind.

20 MR. BRILLIANT: I understand that, Your
21 Honor, but I just want to, you know, understand, Your
22 Honor, you know, there's certain amount of fair play
23 that's involved. And if they didn't want to tell us,
24 they shouldn't have told us, but they shouldn't have
25 told us who their witness was and then, you know, change

1 their mind.

2 MR. KRUMHOLZ: What we said was --

3 THE COURT: Are you asking for a
4 continuance because --

5 MR. BRILLIANT: No. I'm just pointing
6 out the fact that, Your Honor...

7 THE COURT: Okay. I understand. That
8 just must mean that somebody's opening statement was
9 effective. That the opening has changed their whole
10 approach. Or maybe it was so ineffective that they now
11 think that they just go straight to -- I don't know.
12 We'll find out. He's got to be sworn.

13 ALEXANDER DEAN, JR.,
14 having been first duly sworn, testified as follows:

15 THE COURT: You can just speak normally.

16 DIRECT EXAMINATION

17 BY MR. KRUMHOLZ:

18 Q. Good afternoon.

19 A. Good afternoon, Mr. Krumholz.

20 Q. Your name is Alexander Lawrence Dean, Jr.; is
21 that right?

22 A. Yes.

23 Q. And you go by Sandy, true?

24 A. Yes.

25 Q. As I understand it, Mr. Dean, you have a

1 bachelor of science degree in engineering; is that
2 correct?

3 A. That is correct.

4 Q. And you have an MBA in finance; is that
5 correct? Or not in finance, you have an MBA and your
6 focus was finance?

7 A. I have an MBA and I took a lot of finance
8 courses.

9 Q. I want to talk a little bit about your
10 involvement in this case. First of all, for the last
11 ten years you have been intimately involved in Mendocino
12 Redwood Company; is that right?

13 A. Yes.

14 Q. You've also been integrally involved in
15 Mendocino Forest Products, true?

16 A. Yes.

17 Q. And are you the chairman of those entities?

18 A. I am.

19 Q. And you help operate those entities?

20 A. I've been the chairman for 8 years. In the
21 first two and a quarter or two and a half years that we
22 owned them I served as the president of the company. I
23 was responsible for all day-to-day operations.

24 Q. And as we discussed in connection with your
25 deposition that we recently took, you, together with

1 various affiliates and entities that you control
2 together with the Fisher family and their controlled
3 entities own both MRC and MFP, true?

4 A. Yes, Mendocino Redwood Company and Mendocino
5 Forest Products are owned and controlled by the Fisher
6 family and myself.

7 Q. And Don Fisher is the father in the ranking
8 members, so to speak, in the Fisher family; is that
9 right?

10 A. He's the oldest living member in the family.

11 Q. That's a much better way to put it. And John
12 Fisher is his son, true?

13 A. Yes, that's true.

14 Q. And they're sort of your partners, right, so
15 to speak?

16 A. Yes. The Fishers are the source of capital
17 for what we do and I'm an investment partner with them,
18 yes.

19 Q. Neither of them are attorneys; is that right?

20 A. Yes, that's true.

21 Q. Never served in any sort of role similar to
22 that; is that right?

23 A. Yes.

24 Q. Now, you followed the bankruptcy for some time
25 before you partnered up with Marathon, true?

1 A. Yeah, when Pacific Lumber Company filed
2 bankruptcy, because of our prior conversations we were
3 paying attention to what happened, yes.

4 Q. You listened in on the phone when there were
5 hearings that were ongoing in 2007, right?

6 A. I did not, but an attorney on our behalf did
7 listen to the hearings, yes.

8 Q. And you also had communications with various
9 of the parties to the bankruptcy, correct?

10 A. Yes.

11 Q. And your initial phone conversations with
12 Marathon started in the summer of 2007, just last year,
13 correct?

14 A. I'd be hard pressed to name the exact date
15 but I think the first call with them was some time in
16 the late spring or early summer of 2007.

17 Q. And then I think you had a meeting in the
18 summer or fall of 2007; is that right?

19 A. We had -- we had a meeting and lunch some time
20 in the summer of 2007, yes.

21 Q. But it wasn't until November of 2007 that
22 Marathon actually called you to possibly participate in
23 the plan, true?

24 A. I've testified about this before.

25 Q. This is right out of your testimony. We can

1 go there if you like.

2 A. In November they called us and asked us would
3 we be interested in purchasing some of their debt and
4 participating in the reorganization of the companies.

5 Q. And in that same time frame, that is, November
6 2007 a confidentiality agreement was signed so you could
7 do just that, have those discussions?

8 A. Yes, we -- some time after that conversation
9 asking me about our interest we worked out a
10 confidentiality agreement with them.

11 Q. And in November 2007, that's when, I think the
12 way you put it, the substantive conversations began with
13 Marathon, correct?

14 A. Yeah.

15 Q. Now, I want to talk to you a little about
16 growth. You've issued a proffer in this case; is that
17 right?

18 A. Correct.

19 Q. You talked about various values at different
20 dates in your view, true?

21 A. In the most recent proffer that I submitted, I
22 did talk about changes in value going back to the 2007
23 date, yes.

24 Q. You talked about log prices?

25 A. Yes.

1 Q. You talked about discount rates?

2 A. Yes.

3 Q. And in part -- and you did a discounted cash
4 flow modeling like we did in connection with your
5 business plan, true?

6 A. Yes, I took the cash flow model that we used
7 in conjunction with the reorganization plan and did some
8 sensitivity analysis on that to go back to a view of
9 2007.

10 Q. And in that plan, you assumed certain growth
11 rates; is that right?

12 A. Our original model has an estimated growth
13 rate for the forest, yes.

14 Q. Okay. And growth rates are important as we
15 heard Mr. Neier talk about it at length and Mr. Fiero
16 talk about at length that growth was important to your
17 analysis in terms of what did the forest do in 2007,
18 right?

19 A. Growth rate is important for the long-term
20 valuation of the forest in particular.

21 Q. Just to be clear, I'm not trying to trick you.
22 But Marathon and MRC have taken the position that growth
23 actually out paced any harvest in 2007, true?

24 A. Yes.

25 Q. Okay. In fact, this whole middle table of

1 attorneys has taken that position now as we heard in
2 opening, correct?

3 A. It's my view and I think it was the attorney's
4 view that the forest grew faster than it was harvested
5 in 2007.

6 Q. And you in March of 2008 actually reviewed the
7 affidavit declaration of Mr. Barrett, right?

8 A. You know, I looked at it some time in the
9 spring and I looked at it recently, yes.

10 Q. And you know what I'm talking about, the
11 declaration that talked about whether there was more
12 growth than harvest in 2007. Do you recall that?

13 A. I do.

14 Q. And so you came to some opinions, I guess,
15 recently on the value of that growth, that net growth,
16 that additional growth in 2007, right?

17 A. I estimated it, yes.

18 Q. And you said it could probably be somewhere
19 between \$5 and \$15 million. That's your testimony?

20 A. Yes.

21 Q. And of course, Mr. LaMont, if you can put
22 Mr. Lamont's proffer on the chart there. Next one. You
23 saw this before it was filed, did you not, Mr. Dean,
24 this proffer of Mr. LaMont?

25 A. I think I saw something before it was filed,

1 yes.

2 Q. And right there in paragraph 26, the second
3 sentence says "I have valued this additional growth at
4 approximately \$5 to \$7 million." Do you see that?

5 A. I do.

6 MR. JONES: Your Honor, I'm sorry, I
7 should have done this earlier. I got discombobulated
8 because they called Mr. Dean first. I mentioned in one
9 my minute I'm going to object to any testimony that goes
10 to what happened to the forest during this time because
11 it's beyond the scope of their motion, as I mentioned.

12 If you read their motion, their motion is
13 very simple. It says you ruled they were oversecured,
14 they're not. And, Your Honor, as I pointed out, in
15 fact, the order says that Scopac reserves its right to
16 argue that they're not oversecured. I just don't think
17 this is proper. They had a chance to bring a motion and
18 to state their grounds. They stated one ground and
19 apparently they realized there's no basis for it.

20 THE COURT: So if -- I mean, you're now
21 wanting to modify, I guess, their grounds for their
22 administrative claim to this devaluation of their cash
23 collateral and their cash as well as their forest; the
24 real estate as well as their other movable assets?

25 MR. JONES: Yes, Your Honor. And we

1 would suggest they shouldn't be permitted to.

2 THE COURT: Is that what you're now
3 doing? So that's your argument?

4 MR. KRUMHOLZ: Your Honor, the reason why
5 this is relevant is twofold. A --

6 THE COURT: You're not going to go with
7 just the notion that I said you're oversecured and now
8 you're not oversecured?

9 MR. KRUMHOLZ: I'm going with the notion
10 that growth matters. And they've said that has some
11 value in '07 and I'm going to demonstrate that --

12 THE COURT: We have a more simple issue.
13 He's now objecting to you raising the issue other than
14 the issue that is in your motion. The only ground in
15 your motion is there was a finding that were
16 oversecured, now there's a finding you're undersecured.

17 Now, that's not your current position.
18 And he's already forecasted what I'm going to rule. I
19 don't know whether he's right, but he's already
20 forecasted I'm going to go with you on the issue that
21 I'm going to let you modify your pleadings, in essence,
22 to your current position in order to litigate this issue
23 now once and for all because we're not going to put it
24 off. I don't know if he's asking for a continuance if I
25 so rule. But are you now asking to orally modify -- I

1 don't know whether you're bound by the terms of how you
2 filed your administrative claim or not.

3 MR. KRUMHOLZ: Your Honor, to the extent
4 it's helpful, I'll ask for a trial amendment and request
5 that we amend the motion to broaden the claim to value
6 it at January 18, 2007 to date.

7 THE COURT: You now have permission to do
8 that. So going on to that. So I'm now overruling your
9 objection.

10 MR. JONES: Thank you, Your Honor.

11 MR. KRUMHOLZ: It takes me a while,
12 Judge, but once I get it, I get it.

13 THE COURT: Now you can do the nuances of
14 why this is important. Go ahead.

15 Q. (By Mr. Krumholz) Okay. Mr. Dean, we talked
16 about -- we were at Mr. LaMont's proffer. You said you
17 saw it before it was filed with the court, right?

18 A. Yes.

19 Q. In fact, you authorized its filing, in part,
20 right?

21 A. I did not authorize its filing, but I did see
22 it.

23 Q. And you did know that Mr. LaMont was now
24 representing to the Court that there was a \$5 to \$7
25 million in increased value; is that right?

1 A. Yes.

2 Q. That's a far different opinion than you had
3 just a few months ago after reading Mr. Barrett's
4 affidavit, wasn't it?

5 A. I don't -- I don't think so, but keep going.

6 MR. KRUMHOLZ: All right. May I
7 approach, Your Honor?

8 THE COURT: Sure.

9 Q. (By Mr. Krumholz) I'm handing you what I've
10 marked as Exhibit 131-A. And for the record, in Exhibit
11 131, it was the last four pages, I just realized that,
12 so I'm marking it Exhibit 131-A. Here's a copy.

13 Mr. Dean, that is a series of -- that Exhibit
14 131-A is a series of e-mails on March 6 of 2008; is that
15 right?

16 A. It appears to be so, yes.

17 Q. The last of which was from Mr. Tedder, an
18 expert of yours and Marathon's, true?

19 A. Are you starting at the bottom or the top,
20 Mr. Krumholz?

21 Q. I'm starting at the top. The last e-mail
22 chronologically is Mr. Tedder's, true?

23 A. Yes, it seems so.

24 Q. Let's go to the first e-mail on this set. Go
25 back one more. All right. It says, "Counsel, attached

1 please find the proffers of Jeff Barrett, together with
2 Exhibits A, B and C thereto and to Steve Zelin." Do you
3 see that?

4 A. Yes.

5 Q. And it was dated March 6 of 2008. That's my
6 marking there. But on the previous page it shows that.
7 Do you see that in the hard copy before you?

8 A. I do.

9 Q. Okay. Let's go to the next page. And just
10 above that, Mr. Neier sends an e-mail to Mike Jani.
11 He's an officer with your company, correct?

12 A. Yes.

13 Q. John Russell, he's another officer of your
14 company, right?

15 A. When you say your company, one is with
16 Mendocino Redwood Company and one is with Mendocino
17 Forest Products, but yes.

18 Q. And then there's some from Mr. Hottenger. Who
19 is he?

20 A. He's been consulting with us on and off for a
21 number of years.

22 Q. And then there is a Mr. Richard Higgenbottom;
23 is that right?

24 A. Yes.

25 Q. He's the guy that you want to run Newco, this

1 new entity that might hold the Palco and Scopac assets,
2 true?

3 A. He's the CEO of our existing business, and he
4 would be the CEO of Newco if we get there.

5 Q. And you're certainly copied here. You see
6 that, right?

7 A. Yes.

8 Q. And Phil Tedder, the expert we talked about
9 before, is copied, right?

10 A. Yes.

11 Q. And Jeff Johnston is copied, right, another
12 one of your experts, true?

13 A. Yes.

14 Q. And a host of other folks are there, including
15 Mr. Breckenridge from Marathon; is that right?

16 A. I don't see him, but I'll take your word for
17 it.

18 Q. And then it says "valuation folks." And this
19 was in part addressed to you, right? "Please review the
20 affidavit of Jeff Barrett and the two attachments to
21 that affidavit." Do you see that language?

22 A. I do.

23 Q. And you responded to that e-mail, did you not?

24 A. I think you're going to tell me I did.

25 Q. Let's go up from there. And do you see from

1 Sandy Dean at 6:32 a.m., do you see that?

2 A. I do.

3 Q. It's to all the same folks, including
4 Mr. Neier, the one who stood up before us just a moment
5 ago and told us how valuable this '07 growth was, right?

6 A. Yes.

7 Q. And it says, "They harvested all of the
8 redwood growth, almost all of the redwood growth for the
9 year." Do you see that?

10 A. I do.

11 Q. "The amount of redwood they did not harvest
12 seems quite small to me." That's what you said, right?

13 A. Correct.

14 Q. "So we are talking about .35 percent." Do you
15 see that?

16 A. I do.

17 Q. "Seems to me like that would be close to the
18 margin of error for estimating what the forest is
19 producing." Did I read that correctly?

20 A. It is what I wrote.

21 Q. In the next paragraph, you go on and say,
22 "significant Douglas Fir was added to the forest." Do
23 you see that?

24 A. Yes.

25 Q. You go on and explain to Mr. Neier and the

1 rest of these folks the same thing that you explained to
2 us during the confirmation trial, which was "the market
3 value of Douglas Fir today is less than the cost to the
4 company of removing Douglas Fir." Do you see that?

5 A. I do.

6 Q. "It is unrealistic to value Fir based on its
7 stumpage contribution since there are large and real
8 costs to get Fir out of the woods beyond log and haul."
9 Did I read that correctly?

10 A. You do.

11 Q. Let's go to the next one. And then it says on
12 the next page: "Adding hardwood to the property adds no
13 economic value." Did I read that right?

14 A. Yes.

15 Q. You go ahead and argue in fact it could
16 detract from it?

17 A. True.

18 Q. And then Mr. Tedder responds to you; is that
19 right? And it's just later in the day at 1 p.m., right?

20 A. That's what it says.

21 Q. And Mr. Tedder is partners with Mr. LaMont.
22 You heard that testimony at confirmation?

23 A. I did.

24 Q. Not only in one business, but in multiple
25 businesses, right?

1 A. I don't know their whole history, but I know
2 they've worked together for a number of years.

3 Q. I only know what he talked about in
4 confirmation. Do you remember that?

5 A. I was absent for some of their testimony, but
6 I'm aware they've been partners in business on and off
7 for quite a while.

8 Q. And that they trust each other, that's your
9 understanding?

10 A. I would assume so.

11 Q. And again, this is to the group, right? And
12 let's go to the next one. It says, "I agree with all of
13 Sandy's comments." And I assume when you received this
14 e-mail, it didn't surprise you or shock you that
15 Mr. Tedder agreed with you, right?

16 A. I don't think I had a reaction one way or the
17 other.

18 Q. Okay. Let's go the next call-out. It says,
19 "harvest was 74 million board feet." And he's referring
20 to 2007, as you understand it, right?

21 A. Yes.

22 Q. And it says redwood minus -- "redwood harvest
23 minus redwood growth is about" what?

24 THE COURT: Let's don't ask questions
25 that way. Zero.

1 Q. "Zero as Sandy pointed out. Therefore, the
2 rest of the growth is Douglas Fir and hardwoods." Did I
3 read that right?

4 A. Sure.

5 Q. Let's go on to the next one. Paragraph eight,
6 talking about paragraph eight of the declaration of
7 Mr. Barrett, right?

8 A. Yes.

9 Q. And it says, "All net additional growth was on
10 stands that currently have no value when logging costs
11 and the market price are considered." Did I read that
12 correctly?

13 A. Yes.

14 Q. Now, nowhere in this e-mail trail is
15 Mr. LaMont, right?

16 A. If you say so, I will take your word for it.
17 I don't see him.

18 Q. Was he intentionally excluded from this e-mail
19 traffic?

20 MR. NEIER: Your Honor, just so you know,
21 Mr. LaMont is on this e-mail. His e-mail address is
22 rei@reiweb.com.

23 MR. KRUMHOLZ: That's helpful. Strike
24 that last question.

25 Q. (By Mr. Krumholz) Regardless, so Mr. LaMont

1 didn't disagree with Mr. Tedder when the made these
2 statements, as far as you saw?

3 A. I don't know. He hasn't commented on this.

4 Q. Did he tell you he did?

5 A. You know, there's been a lot of e-mails in the
6 last seven months for me in this case. I don't remember
7 every one of them. I certainly don't remember if
8 Mr. LaMont responded to every one of them. He and I
9 haven't discussed this e-mail, that I can tell you.

10 Q. You did notice that you didn't respond back to
11 Mr. Tedder somehow telling him that he was incorrect
12 about the growth, right?

13 A. We don't have that here. I doubt it, but I
14 don't know. Look, I've exchanged a lot of e-mails in
15 the case. I just don't think I can say for certain.

16 Q. You still allowed Mr. LaMont to proffer his
17 testimony, right? You didn't tell him stop, it doesn't
18 have any value '07?

19 A. I don't think that I said it has no value in
20 here.

21 Q. What I'm asking you is: Did you stop
22 Mr. LaMont, based upon Mr. Tedder's and your comments?
23 We'll judge what it says. Did you do that?

24 A. No.

25 Q. Okay. And you stated under oath that the

1 additional growth above the harvest had millions of
2 dollars in value, right?

3 A. I stated under oath that I thought it could be
4 between \$5 and \$15 million, yes.

5 Q. That's not the first time, Mr. Dean, that you
6 have said one thing in court and said another thing in
7 private to your attorneys and your experts, right?

8 A. I don't think so.

9 Q. In your deposition you said that Marathon
10 never suggested to you that they thought it was a good
11 idea to combine the Palco mill and the timberlands in
12 some new company to capture the value of the Scopac
13 timberlands. Do you recall that?

14 A. You asked me a very specific question in my
15 deposition. If you want to refer to the deposition
16 question, we can do that.

17 Q. Well, let's -- you agree with that today, I
18 assume, that you've never heard Marathon say that or
19 suggest that?

20 A. Tell me your question again.

21 Q. You've never heard Marathon suggest or imply
22 or state to you that they thought it was good idea to
23 combine the Palco mill and the timberlands in some new
24 company to capture the value of the Scopac timberlands?

25 A. I'm not -- I'm not aware that they ever said

1 that, no.

2 Q. You said that same thing in your deposition
3 that they didn't say that?

4 A. Yeah. I think you used the words tap into the
5 value at the deposition.

6 Q. And you also told me that they never indicated
7 or suggested they wanted to tap into the value of the
8 Scopac timberlands?

9 A. Correct.

10 Q. They never suggested that to you in any way,
11 shape or form?

12 A. Correct.

13 Q. You also denied that it was your impression of
14 Marathon's motives in that regard to tap into the value
15 of Scopac timberlands?

16 A. Correct.

17 Q. And you denied that Marathon ever suggested to
18 you that they wanted to combine the mill and the
19 timberlands to make up for any undersecurity they had in
20 place at the Palco level?

21 A. Correct.

22 Q. And you still hold those beliefs to be true;
23 is that your testimony?

24 A. It is. It was the testimony at my deposition,
25 it's my testimony now.

1 Q. The truth is Marathon made it clear to you in
2 the fall of 2007 that they would proceed with the sham
3 appraisal just for this purpose; isn't that right?

4 A. Marathon has never suggested to me a sham
5 appraisal.

6 Q. Or a bogus appraisal, did they ever suggest
7 that to you?

8 A. Certainly not that I can recall, no.

9 Q. You do -- you did believe in September 2007
10 that Marathon was undersecured; is that right?

11 A. Yes, I have felt that Marathon was
12 undersecured for some time.

13 Q. But it's your position that Marathon has never
14 stated or suggested that they want to access the value
15 of the timberlands to make up for any deficiency they
16 might have in that security, true?

17 MR. JONES: Your Honor, I'm going to
18 objection. What does this have to do with the 507
19 motion?

20 MR. KRUMHOLZ: We'll get to it.

21 MR. JONES: He seems to want to reargue
22 the confirmation.

23 THE COURT: I don't know where we're
24 going. I'm not sure.

25 MR. KRUMHOLZ: Your Honor, we'll get

1 there.

2 THE COURT: Well, let's get there.

3 MR. KRUMHOLZ: We are.

4 Q. (By Mr. Krumholz) Mr. Dean; is that right?

5 A. Mr. Krumholz, the idea that Marathon would
6 suggest that somehow we would combine the companies and
7 tap into or capture or take the value that belonged to
8 the Scopac creditors, I do not believe was ever
9 suggested. I will say that --

10 MR. KRUMHOLZ: I'll object to the
11 nonresponsive answer. You're already answered the
12 question.

13 THE COURT: Well, I'm not sure what
14 question you're asking him then because I thought that's
15 what you were asking, was whether or not they had some
16 sort of scheme to steal the assets of the company.

17 MR. KRUMHOLZ: That's exactly asked what
18 I asked him, and he answered it. I didn't want him to
19 explain further.

20 THE COURT: Okay. He said they didn't
21 have a scheme. Okay. Go ahead.

22 MR. KRUMHOLZ: Your Honor, may I
23 approach? May I approach, Your Honor?

24 THE COURT: Yes, you may. At this point
25 while there's a little break in the action, I would just

1 mention for those of you who are also in the Asarco
2 case, that I understand that midnight tomorrow is the
3 deadline for me to rule. And we will rule, either
4 orally or in writing before midnight tomorrow in the
5 Asarco case. Probably tomorrow during this hearing at
6 some point I will rule. But I think that the parties to
7 Asarco wanted it to be at a time when everybody could be
8 on the line, so we'll try to let everyone know what time
9 it will be that I rule, if I do so orally, all right? I
10 don't know how many people here are in Asarco, but you
11 are, and you're in it. I don't know if -- Judge Pate
12 was in the courtroom a minute ago, but I guess he's
13 gone. All right. Go ahead.

14 Q. (By Mr. Krumholz) Mr. Dean, I have handed you
15 an exhibit marked 160. Do you see that?

16 A. I do.

17 Q. And it's an e-mail that you sent to Mr. Fisher
18 dated 9/14/07; is that right?

19 A. Yes, it is, yes.

20 Q. Do you recall sending this e-mail?

21 A. I don't recall it specifically, but it looks
22 to be something that I wrote. And I do recall that I
23 wrote something after I had a meeting with Marathon.

24 Q. This is in connection with a meeting you had
25 with Marathon in September of 2007; is that right?

1 A. It would seem so, yes.

2 Q. It's from you to -- is that John Fisher?

3 A. Yes.

4 Q. And Mr. Higgenbottom, we talked about him, and
5 Mr. Russell, correct?

6 A. Yes.

7 Q. And the subject is meeting with Marathon. Go
8 forward, please. And it's a summary of that meeting
9 with Marathon. And it says, "Richard Ronzetti and Gary
10 Lembo." And those are Marathon folks, correct?

11 A. Yes.

12 Q. And it says that meeting occurred in September
13 13, 2007. Do you see that?

14 A. Yes.

15 Q. And those folks are actually officers of
16 Marathon; is that what you understand?

17 A. I don't know what their position is, but they
18 seem to be senior people at Marathon.

19 Q. Okay. Let's go to the next call-out. It says
20 "spent 90 minutes in our office and then you had 90
21 minutes outside for lunch, things were frosty, and then
22 they got a little more humorous and good-spirited." Do
23 you see that?

24 A. Yes.

25 Q. Let's go to the next call-out. "It was not

1 our first statement, but as we talked about specifics, I
2 was clear that the comments we were making were based on
3 publicly available info. Later in the day they made the
4 same reference." So what you-all discussed was public
5 as far as you were concerned, right?

6 A. We were very careful in all of our
7 conversations with anyone around the case to limit
8 anything we said to what was publicly available
9 information because we had the best information that we
10 received from the 2006 conversations.

11 Q. Let's now go to the next call-out. It says,
12 "they talked about how they think one of the main things
13 the company needs to do is better integrate the
14 functioning of the lands and the mill." Do you see
15 that? And this is, I think, in the third or fourth
16 paragraph on the first page.

17 A. Yes.

18 Q. The last paragraph. And you said, "we took
19 some exception to this." Do you see that?

20 A. Yes.

21 Q. And then it states at the bottom, "as we
22 talked on this point, it became clear that they see a
23 need to combine the mill and the lands." We talked
24 about combining the mills and the lands earlier, do you
25 recall that?

1 A. Yes.

2 Q. "Because they want to access what they see as
3 land values to bolster their collateral position." Did
4 I read that correctly?

5 A. That's what the words say.

6 Q. Let's go to the next call-out. This is on the
7 third page, I believe, of that document, Bates number
8 17685. And in the middle there it talks about "most
9 important discussion of whole day." And down a little
10 bit it says, "they believe that Palco and Scopac cases
11 are not going to be separated; and therefore, even if
12 they are undercollateralized at Palco, they can tap into
13 equity at Scopac to get made whole." Is that what it
14 says?

15 A. Yes.

16 Q. And then down below you said, "I said wait a
17 second, if I'm a noteholder and I objected to the DIP
18 and I'm being impaired, I just want my timberland. He
19 conceded that the noteholders could prove impairment
20 that they would not have to share with Marathon, but he
21 thinks the valuation argument will get so muddied (three
22 sets of appraisals, hearings, etcetera) that noteholders
23 will never prove impairment." Did I read that
24 correctly?

25 A. Yes.

1 Q. Let's go to the next call-out. Down just
2 below there it says, "it would seem like perhaps our job
3 is to convince the noteholders of the train wreck that
4 is coming." Did I read that correctly?

5 A. Yes.

6 Q. The lasts sentence. "We knew this before
7 Marathon meeting, but Marathon shows that the debtor and
8 Marathon think they can proceed with a bogus appraisal
9 and cram down to leave noteholders in a very bad place."
10 Did I read that correctly?

11 MR. JONES: Your Honor, I'm going to
12 renew my objection. This goes to the plan. He may
13 think he's found a scheme to confirm a plan that the
14 Court has already decided on. This doesn't go to
15 whether they have a super-priority claim or not.

16 MR. KRUMHOLZ: Your Honor, may I respond?

17 THE COURT: Yes.

18 MR. KRUMHOLZ: Same experts. This is all
19 part of the same exact -- this is all according to the
20 plan, Your Honor. The same thing I've been telling you,
21 that everybody has been telling this Court since day
22 one. The Palco creditors from day one manufactured
23 evidence to tap into value at Scopac. We said it over
24 and again. This witness just told you it wasn't true.
25 And now you know the truth. And it's for the world to

1 see while Mr. Neier laughs.

2 MR. JONES: Your Honor, if it was
3 material, it was material at the confirmation hearing.
4 They apparently had it then. I don't know why we're
5 waiting until after that.

6 THE COURT: Well, let's move on. What
7 else?

8 Q. (By Mr. Krumholz) And what you meant by bogus
9 appraisal, I assume it's the same thing that most of us
10 mean, right? False?

11 MR. JONES: Objection, calls for
12 speculation.

13 Q. (By Mr. Krumholz) Scam?

14 MR. JONES: He doesn't know what --

15 THE COURT: I think he's entitled to ask
16 him what he means by bogus.

17 MR. JONES: He can ask him, but the
18 question is what most of means. He doesn't know what --

19 MR. KRUMHOLZ: That's a fair point.

20 Q. (By Mr. Krumholz) Let's go to what the
21 English speaking world means when they say bogus. Does
22 that apply when you write e-mails to Mr. Fisher?

23 A. You know --

24 Q. I want to know that answer.

25 A. I don't know what the definition of the

1 English speaking --

2 MR. KRUMHOLZ: May I approach, Your
3 Honor?

4 THE COURT: Why don't we just ask him
5 what he meant by it.

6 MR. KRUMHOLZ: Because, Your Honor, I
7 want to show what it means in the dictionary.

8 THE COURT: You're welcome to put on --
9 if you don't believe --

10 MR. KRUMHOLZ: If they want us to ask him
11 what he meant now looking backwards, that's fine, Your
12 Honor, but I'm entitled to ask him what he meant and if
13 the English language applies to it.

14 MR. JONES: Your Honor, objection. If he
15 wants to ask does he mean what he's reading from the
16 Oxford English dictionary, that's fine, but --

17 THE COURT: Ask him that. We don't have
18 a jury here. Just read the definition and ask him if
19 that's what he meant.

20 Q. (By Mr. Krumholz) Well, did you mean one of
21 these things. Did you mean that it was a sham, that's
22 what they were intending to do?

23 A. No.

24 Q. Did you mean that it was fictitious?

25 A. No.

1 Q. Is that what you meant, it was a fictitious
2 appraisal?

3 A. No.

4 Q. Did you mean that it was a spurious appraisal?

5 A. No.

6 Q. Did you mean that it was counterfeit?

7 A. No.

8 Q. Did you mean that it was going to be a fake
9 appraisal?

10 A. No.

11 Q. A false appraisal?

12 A. No.

13 Q. Or the last one, according to the Oxford
14 dictionary, a fraudulent appraisal?

15 A. No. Would you like me to say what I thought
16 it meant?

17 THE COURT: He doesn't have to ask you
18 that. They can ask you that on redirect. If he wants
19 to, he can.

20 Q. (By Mr. Krumholz) I also want to talk to you
21 about one other item in this e-mail. And go ahead and
22 call that up. We talked about this paragraph. It's in
23 that paragraph that starts "most important discussion of
24 whole day." Do you see that?

25 A. Yes.

1 Q. It says, "I asked about what happens if Scopac
2 is undercollateralized and first said that cannot be."
3 Did I read that right?

4 A. Yes.

5 Q. Marathon was telling you it can't be that
6 Scopac is undercollateralized as of September 2007?

7 A. I think that was their belief at that time.

8 Q. So if what Marathon said was true in September
9 2007 and the timberlands are worth \$510 million, then
10 there has been over \$200 million of diminished value
11 since that day, according to their assumption, right?

12 A. They were wrong.

13 Q. Am I right, if they -- if that's what they
14 believed to be true and if that were true?

15 A. That would be true. Of course, they have no
16 qualification to make an estimate of the value of the
17 Scopac timberlands.

18 Q. You don't think so?

19 A. No.

20 Q. Let's go to the next line. And this one is
21 really -- I just wanted to know what you meant. "We
22 complimented them on the move to get Scopac to pay for
23 logging and hold inventory, and he said that was a nice
24 sleight of hand." What did you mean by nice sleight of
25 hand?

1 A. That's what he said to me.

2 Q. How did you take that?

3 A. I took that to mean that Maxxam had done a
4 good job in court of pushing the cash burden of Palco
5 onto Scopac temporarily.

6 Q. I went ahead and looked that up, too. And
7 sleight of hand means "carefully executed trick or
8 deception." Is that what you meant?

9 A. No.

10 Q. I want to talk to you a little bit about
11 harvest rates. But first I want to -- I guess I want to
12 discuss the UBS offer that you made back in 2006. You
13 made an offer to UBS for the Palco stock for \$20
14 million; is that right?

15 A. In -- over the course of several months in
16 2006 we had discussions with Maxxam that resulted in us
17 making an offer to buy their stock for \$20 million, yes.

18 Q. It included the Scopac stock, correct?

19 A. It did.

20 Q. It included the Scopac timberlands, right?

21 A. Yes.

22 Q. And the timber notes were also part -- were
23 subject to the timber notes?

24 A. Yes.

25 Q. And you performed substantial due diligence in

1 connection with those negotiations, right?

2 A. As we talked about at my deposition, we
3 performed significant due diligence on Palco, some due
4 diligence on Scopac, but certainly not complete on
5 Scopac.

6 Q. And this due diligence went on for five to six
7 months; is that right?

8 A. Yes, although the focus of the due diligence
9 was mostly Palco, not Scopac.

10 Q. Let's go to Exhibit 34. In December of 2005,
11 you actually visited Scotia; is that right?

12 A. Yes.

13 Q. You got an opportunity to talk to all the
14 officers of Scopac and Palco to the extent you desired;
15 is that right?

16 A. Yes.

17 Q. And go to the next slide. This is a
18 presentation, I guess, that was given to MRC at the
19 time; is that true?

20 A. I think so, yes. We made many visits there.
21 Most of the times when we visited, we were given a
22 presentation.

23 Q. It says here in the second slide "why are we
24 here today? It's to explore possible areas for
25 partnering with MRC and potential areas for investments

1 into the Pacific Lumber Company." Did I read that
2 correctly?

3 A. Yes.

4 Q. And then it talks about -- and then it says
5 agenda. Do you see that?

6 A. Yes.

7 Q. It says 2005 review and it says 2006 looking
8 forward, review of project 10P. What was that, do you
9 remember?

10 A. I think that was a project they had to sell
11 ten parcels of some period of time.

12 Q. And then they went through the Scopac
13 strategic review, right?

14 A. Yes.

15 Q. And then the Palco/Britt strategic review,
16 right?

17 A. Yes.

18 Q. And the 2006 business plan for both of the
19 companies; that is, Palco and Scopac?

20 A. Yes.

21 Q. And then go to the next one. They give
22 opening comments and they go into similar detail about
23 all of these subjects; is that true?

24 A. Yes.

25 Q. And Mr. Barrett, the current, as I understand

1 it, CEO of Scopac, was the one presenting this
2 information to you, right, in part?

3 A. You know, I don't remember who presented us
4 the information, but it could have been.

5 Q. Do you remember that they provided you a
6 projected harvest?

7 A. We've been provided lots of harvests by
8 Scopac. It wouldn't surprise me if they provided one
9 then.

10 Q. Let's go forward. See that harvest at the
11 bottom, it says 2004, 2005, 2005 estimate, 2006 plan.
12 Do you see that?

13 A. Sure.

14 Q. And those are various harvest levels that they
15 provided to you in that time frame, correct?

16 A. Yes.

17 Q. 144 for 2004, 165 million board feet for 2005
18 plan, 2005 estimate was 145 million board feet, and then
19 for 2006, they estimated 108 million board feet, true?

20 A. Yes.

21 Q. And then go one more. One more. And then
22 2006 resources goals, achieve harvest of 108 million
23 board feet. That's what we talked about just a moment
24 ago; is that right?

25 A. I guess that was their goal, yes.

1 Q. Okay. Go ahead and go to the January 25th
2 2006 presentation. Let's go back a little bit, I guess.
3 You had some opportunities to e-mail questions and get
4 responses, is that correct, during this time frame?

5 A. Yeah, there was an ongoing dialogue.

6 Q. And I assume there were a host of questions
7 you would need to ask in connection with doing due
8 diligence of this magnitude for Palco and for Scopac,
9 given that you were getting all of that assets as well
10 as the debt, right?

11 A. We were trying to learn the most we could, but
12 we had a much greater emphasis on Palco than Scopac.

13 Q. But regardless, here's an e-mail and it's
14 dated January 4, 2006. Go ahead to the next call-out.
15 It says, "Paul and Tom, thanks for the follow-up calls
16 about Palco just before Christmas. We appreciate the
17 presentation that was assembled to update us." And
18 you had a list of questions that needed answered, right?

19 A. Okay. Yes.

20 Q. And go to the next. And it talks about
21 overall. It talks about the sawmill. Go forward. It
22 talks about forestry, it talks about the lands for sale,
23 it talks about the HCP, right?

24 A. Yes.

25 Q. If you go forward, then you had a New York

1 presentation in January of 2006; is that right?

2 A. I think that this was forwarded to us or given
3 to us. We weren't in New York for this presentation.

4 Q. But regardless, it was information that was
5 provided to you?

6 A. Yes.

7 Q. If you go to the agenda, there was a 2005
8 review, there was a business plan for Scopac and for
9 Palco, correct, both of them?

10 A. Yes.

11 Q. And there was a proposal that was attached to
12 it; is that right?

13 A. Well, I don't remember, but it looks like
14 that's true, yes.

15 Q. And then if we go on to the next document,
16 it's another e-mail and you're asking questions
17 throughout this period and you're getting answers. You
18 even had an Excel spreadsheet of questions and answers,
19 remember that?

20 A. Yes, yes.

21 Q. Go forward. Keep on going. Keep on going.
22 Keep on going. And these are all e-mails in the
23 February 2006 time frame where you're asking questions
24 and they're providing answers, true?

25 A. Yes.

1 Q. And then -- keep on going until you get to the
2 term sheet. Then you actually started exchanging term
3 sheets, right?

4 A. Yes. There was a number of term sheets that
5 were exchanged over time.

6 Q. By my count, there was almost a dozen. Does
7 that ring a bell?

8 A. There might have been more. It was a lot.

9 Q. So you went back and forth in a great level of
10 detail in terms of organization and liabilities and
11 assets that would be included. Do you recall all of
12 those details?

13 A. I do. I should say I recall the term sheets
14 covered all of those things. I don't remember all the
15 details.

16 Q. And in looking at the UBS file, I didn't note
17 an e-mail or letter or anything of that nature that
18 suggested you didn't receive all of the information you
19 needed to make this \$20 million offer to buy this stock.
20 Do you recall any such letter?

21 A. No.

22 Q. Now, in April of 2006, this is the last or
23 next to the last month of negotiations in 2006. And I
24 guess it's just about seven or eight months before the
25 petition date, right?

1 A. Yeah.

2 Q. All right. And let's go to Exhibit 34. And
3 this is an e-mail from you to Ron Kurtz. Is he with
4 Maxxam? Do you recall?

5 A. I don't remember who Ron Kurtz is.

6 Q. But regardless, you copied both Mr. Keenan
7 from UBS and Brian from Sansome; is that right?

8 A. Yes.

9 Q. And Sansome is your entity that actually owns
10 parts of MRC; is that right?

11 A. Yes, Sansome is our investment partnership.

12 Q. It says, "Ron, good to talk to you this
13 afternoon. Thanks for helping on the model." You had
14 done DCF modeling, hadn't you?

15 A. You know, I asked me about this at my
16 deposition at length. I don't recall doing any DCF
17 modeling. I've told you we produced all that we had.

18 Q. What you do know is you haven't found it and
19 you haven't produced any discounted cash flow modeling
20 that you did in this time frame, right?

21 A. Yeah. I've told you that I think that we
22 forwarded you all that we have from the 2006 time frame.

23 Q. Then it says, "as we discussed, we think a
24 reasonable starting cost structure, the 200 per million
25 board feet -- per thousand board feet of non-log and

1 haul expenses and a \$5 million cap ex number per year
2 and a 90 million foot harvest rate." Did I read that
3 right?

4 A. Yes.

5 Q. Those are your words, right? 90 million is
6 the starting point, right?

7 A. Yeah, I think that's -- yes.

8 Q. And then you said, "We would expect after five
9 years the harvest rate could rise modestly, perhaps to
10 100 million board feet and then be set as a function of
11 the percent of inventory." Did I read that right?

12 A. Yes.

13 Q. And inventory is going up, what, 3 and a half
14 percent a year? Three percent a year?

15 A. I don't know if we calculated at that time,
16 but we probably would have picked something in that
17 range.

18 Q. So it would be a function of that over and
19 above the 100 million board feet?

20 A. That specific phrase, I think, says that at
21 the time, having not completed significant due diligence
22 on Scopac, which I've described before, we were running
23 a model at 90 million feet. This was a model that was
24 being done in a very broad way. And we were saying that
25 we would make a specific projection of harvest rate for

1 a five-year period and then eventually we'd peg it to
2 some percentage of inventory, yes.

3 Q. Let's go to the next. And then there is an
4 attachment, of course, that has this modeling that we
5 can't find, right? That DCF model that you used Excel
6 to prepare?

7 A. As I previously said, we think we provided you
8 everything we have from 2006.

9 Q. It's a far different harvest rate than what
10 you suggested to this Court just a month ago, isn't that
11 right, or less than a month ago?

12 A. Sure. And I think I testified to this.

13 Q. And you admit that if a 90 to 100 million
14 board feet harvest rate was used, the value of the
15 timberlands would be well over \$600 million, right?

16 A. If the 90 million board foot harvest rate
17 could be achieved, it would make a big difference.

18 MR. NEIER: Your Honor, unless he's
19 attacking his own claim, this isn't relevant to anything
20 involving a super-priority claim. It has to do with a
21 declining value between -- presumably between the
22 petition date and the confirmation date. But now we're
23 talking about increasing value. I'm not sure why this
24 is relevant and whether we're going to just retry the
25 entire confirmation hearing over again.

1 MR. KRUMHOLZ: See, when we talk about
2 value, Your Honor, in 2006, what Mr. Neier is not
3 realizing is that six months later is the petition date.
4 And so if the value is well over \$600 million, as this
5 modeling suggested, as Mr. Dean prepared and had input
6 into it, then it would be something along the order of
7 what Mr. Strubeck suggested would be the diminishment of
8 in value, and that's the relevance.

9 MR. NEIER: I'm looking at an e-mail
10 that's dated April 7. You're saying this is six months
11 before the petition date, not eight months? Is that
12 what you're saying?

13 MR. KRUMHOLZ: I said eight months, I
14 thought.

15 MR. NEIER: You said six.

16 MR. KRUMHOLZ: I apologize. I didn't
17 mean to say six. Fair enough.

18 THE COURT: Go ahead.

19 Q. (By Mr. Krumholz) And these negotiation with
20 UBS went all the way almost to June 1, did they not?

21 A. Roughly.

22 Q. Okay. Six months before. You didn't change
23 the acquisition price, did you, that you offered?

24 A. The \$20 million?

25 Q. Yes. Did you change it?

1 A. No. This was not a factor in the
2 determination of the \$20 million.

3 MR. KRUMHOLZ: Object as nonresponsive.

4 Q. (By Mr. Krumholz) Now, I want to talk to you
5 a little bit about discount rates. Well, first of all,
6 from an investment perspective, is it your view that the
7 Scopac timberlands have any particular increased
8 investment risk today that they did not have in January
9 of 2007?

10 A. Any specific increase in investment risk?

11 Q. Yeah.

12 A. I don't think so.

13 Q. Okay. We talked about your two opinions in
14 your proffer, one was discount rates, one was log
15 prices. Your testimony is that discount rates for the
16 Scopac timberlands have decreased since January of 2007;
17 is that right?

18 A. I believe discount rates have decreased
19 materially in the last 18 months, yes.

20 Q. Even though the risk hasn't changed a bit, the
21 investment risk, true?

22 A. I think it's a reflection of the investment
23 climate, not the risk.

24 Q. And you had this opinion about decreased
25 discount rates despite the downturn in the economy. And

1 we talked about that at your deposition, correct?

2 A. Yes.

3 Q. Despite the housing crisis, right?

4 A. Yes.

5 Q. Despite the credit crisis, right?

6 A. Yes.

7 Q. Despite the subprime prices, right?

8 A. Yes.

9 Q. Despite all of this increased market risk or
10 macro risk, right?

11 A. Timberland investors --

12 Q. No. I want an answer to that question.

13 A. Yes.

14 THE COURT: What's the question?

15 Q. (By Mr. Krumholz) In other words, we talked
16 about investments that are going to stay the same, but
17 general macro risk went way up.

18 A. The things that you've cited are true.

19 Q. Is that right?

20 MR. HAIL: Wait, Your Honor.

21 Q. (By Mr. Krumholz) I want to know the answer
22 to that question.

23 MR. HAIL: He's entitled --

24 MR. KRUMHOLZ: He is not entitled to
25 answer a question I did not ask.

1 THE COURT: We can be specific and ask
2 specific questions and get specific answers, and you're
3 entitled to them. However, I don't think there's
4 general macro risks is a defined term that somebody
5 would then say, oh, yes, well, then the answer would be
6 X. I mean, I think that's a term that people would
7 understand, but I think he's entitled to explain his
8 answer.

9 MR. KRUMHOLZ: Well, I think I already
10 got my answer anyway, so I'll go on.

11 MR. HAIL: I object, Your Honor, because
12 he interrupted the witness.

13 THE COURT: Well, you're going to get a
14 chance to redirect him.

15 MR. JONES: Your Honor, I object to the
16 question because it's vague, what he means by macro
17 risks.

18 THE COURT: I understand that. And
19 that's what I was saying. But what he was saying is it
20 is true that the housing market has gotten bad, it's
21 true that we've had a spike in oil prices. It's true,
22 you know, depending on whether you listen to CNN or Fox
23 of how the economy is doing. You know, there are lots
24 of things to be concerned about. Go ahead.

25 MR. JONES: Your Honor, if he wants to

1 ask him about those three specifics things, I have no
2 problem.

3 MR. KRUMHOLZ: I already did.

4 MR. JONES: He did. He attached a
5 general term and says -- very well, Your Honor.

6 THE COURT: Move on.

7 Q. (By Mr. Krumholz) What we can agree on is in
8 the summer of 2007 you had discussions with Mr. Di Mauro
9 at Houlihan, do you recall that?

10 A. Yes.

11 Q. And you stated that MRC might like to own the
12 timberlands at a 6 percent yield, do you remember that?

13 A. I think that we were trying to entice them
14 into a conversation and suggested a 6 percent yield
15 would be an appropriate valuation.

16 Q. And today your view of an appropriate discount
17 rate, I guess, according to your proffer, is the 8
18 percent number?

19 A. I just want to make the distinction between
20 yield versus discount rate.

21 Q. I promise you we'll get to that. I promise.
22 You can hold it against me. You can even tell me and we
23 can start discussing it.

24 THE COURT: Let's just ask questions.

25 Q. (By Mr. Krumholz) So in connection with that

1 8 percent discount rate, you used the discount cash flow
2 model, right?

3 A. You're referring to 8 percent as of January
4 2007?

5 Q. You used 8 percent as of January 2007; is that
6 right?

7 A. Yes. In my proffer I suggested that I think
8 the proper discount rate was -- at January 2007 was 8
9 percent.

10 Q. Okay. And, again, this isn't what you were
11 telling colleagues outside of this courtroom in
12 September 2007, was it?

13 A. I don't know.

14 Q. Let's go to the next one. We're going back to
15 the Exhibit 160. Next call-out. It says, "somewhere in
16 here we started talking about REIT valuations." Do you
17 see that? "And we talked about this is not really our
18 world, but that we thought that Scopac deserves a
19 premium yield due to California regulation, political
20 baggage and track record." Do you see that?

21 A. I do.

22 Q. And it says, "I guessed at 7 to 8 percent,"
23 which I exactly what you say in your proffer for January
24 of 2007, correct, 7 to 8 percent?

25 A. Yeah, I think I said 8 percent in my proffer.

1 Q. And said it would have been lower six months
2 ago. Did I read that right?

3 A. Yes.

4 Q. Six months ago would have been March of 2007,
5 correct?

6 A. Yes.

7 Q. Did you think it was 6 percent?

8 A. I don't know. This was part of a general
9 conversation at lunch with Mr. Ronzetti.

10 Q. Mr. Neier said that for every percentage it's
11 \$70 million in value. That was his position at opening,
12 right?

13 A. Yes.

14 Q. Now, you mentioned yield versus discount rate.
15 I promised you we'd get into that. You read
16 Mr. LaMont's deposition, I think you indicated; is that
17 right?

18 A. I did.

19 Q. And I asked Mr. LaMont what was an
20 authoritative book when it came to real estate appraisal
21 or appraisal generally for timberlands. And do you
22 remember that he provided some information in that
23 regard?

24 A. I don't, but okay.

25 Q. The Appraisal of Real Estate is what he told

1 us of The Appraisal Institute. Do you remember that at
2 all?

3 A. Is this from his deposition, you're saying?

4 Q. Yes, the one you told me you read.

5 A. I thought you asked if I read his proffer, I'm
6 sorry.

7 Q. I did, I meant his deposition. You did read
8 his deposition, correct?

9 A. I did.

10 Q. Before your deposition?

11 A. Yes.

12 Q. Let's go to the Appraisal of Real Estate for a
13 moment, which is Exhibit 12, I believe, our Exhibit 12.
14 We can go on, Chapter 24, the second page of that
15 chapter. And it has a box talking about this. And it
16 says, "discounted cash flow analysis is a procedure in
17 which a yield rate is applied to a set of income
18 streams." Did I read that right?

19 MR. JONES: Your Honor, this isn't a
20 proper question. If he wants to ask him a question, he
21 can. But to question the witness's ability to read this
22 thing is not --

23 THE COURT: It may be a question of his
24 own ability to read it.

25 MR. KRUMHOLZ: That's exactly right.

1 A. Yes, you read it correctly.

2 MR. JONES: But Your Honor, Mr. Krumholz
3 is --

4 THE COURT: Now what is the objection?

5 MR. JONES: The objection is the question
6 is not material. Mr. Krumholz' ability to read that nor
7 the witness's ability to read that are not material.
8 What he's trying to do is get this into evidence through
9 the back door. This witness hasn't said he's an expert
10 on whether that's a good source or not. He says, but
11 some third person says it was a good source, so I'd like
12 to start reading it. Your Honor, if he has a question
13 of the witness, he should ask the question.

14 THE COURT: I'm not sure what the
15 question is.

16 MR. KRUMHOLZ: What Mr. Dean wanted to
17 know in that last e-mail that it said 78 percent yield
18 and he wanted to talk about it, I said we'll get to that
19 in a second instead of discount rate.

20 THE COURT: So ask him the question.

21 Q. (By Mr. Krumholz) I'm just saying it's -- all
22 I'm saying, Mr. Dean, is that in the world of
23 valuations, discounted cash flow modeling, yield rate is
24 synonymous with discount rate, true?

25 MR. NEIER: Objection, Your Honor.

1 That's not what that says. That's not what that says.

2 MR. HAIL: It's also an improper question
3 of world valuations.

4 A. So we talked about this in my deposition.

5 Q. You can say no if you want, that's fine.

6 A. I'll just say no.

7 Q. I'll move on then. Let's talk about log
8 prices. You believe that lumber prices for redwood has
9 been steady in 2007, in 2008 despite the housing
10 subprime and credit crisis that we talked about earlier,
11 right?

12 A. I think we should qualify that to say retail
13 lumber prices, but yes.

14 Q. But you do know that the Court in its findings
15 in several places said that log prices have declined by
16 10 to 15 percent?

17 A. Sure.

18 Q. And you agree with that, do you not?

19 A. I do.

20 Q. And all other variables being equal, that is,
21 discount rates and all the other modeling that you did
22 for the March 2008 here, that would mean the value
23 actually declined over 2007, if all the other variables
24 were equal?

25 A. If all else is held equal and log prices

1 decline, there will be a decline of value; the question
2 is how much.

3 MR. KRUMHOLZ: Now, Your Honor, the next
4 area involves a proprietary document.

5 MR. HAIL: Tell me what it is real quick.

6 MR. KRUMHOLZ: It's the only one in the
7 whole list, the transition document.

8 THE COURT: Show him the document.

9 MR. KRUMHOLZ: It's this one. You can
10 put it on the screen if you want. You know which one it
11 is.

12 MR. HAIL: Your Honor, there is a series
13 of documents that we produced in this case that relate
14 to potential issues involving transitions from the
15 current Palco, Scotia, Scopac issues to what might
16 happen under an MRC/Marathon plans; time lines,
17 different things like that about that transition
18 takeover. I don't have any idea why that's relevant.
19 We produced it in connection with any potential stay or
20 bond issue, not in connection with 507(b).

21 THE COURT: So why do we need to go into
22 that area?

23 MR. KRUMHOLZ: Can I just ask him one
24 question and see? If he answers it a certain way, it
25 won't be relevant. If he answers another way, it will.

1 THE COURT: Well, what's the question?

2 Q. (By Mr. Krumholz) The question simply is: I
3 just want to know if Palco -- if your true intent -- it
4 there was a substantial risk that Palco was going to be
5 closed down, shutdown, you think that Scopac would be
6 much less valuable, right?

7 A. Yeah, I think that I talked about that. To
8 the extent you do not have the mill at Palco, it's a big
9 supply of logs on the market that does not have a lot of
10 ability to absorb that many logs, and I think that the
11 log prices will go down.

12 Q. So the value of Scopac will decrease
13 significantly if Palco goes away?

14 A. I think there's a risk of that, yes.

15 Q. That's what you believe.

16 MR. KRUMHOLZ: Your Honor, I think it's
17 relevant because we believe this is one document in a
18 number of pieces of evidence, frankly, that are going to
19 be presented -- that may be presented that will show the
20 true intent here is to close the mill.

21 MR. JONES: Your Honor, this is --

22 THE COURT: Well, I don't see how that
23 has anything to do with -- I mean, in other words,
24 you're saying he wants to -- he's going to purchase
25 Scopac and then devalue it by closing the mill?

1 MR. KRUMHOLZ: I think he's going to
2 purchase Scopac, and according to his own testimony, if
3 it closes, it's going to devalue.

4 THE COURT: I think the issue of whether
5 he's going to close Scopac -- I mean, Palco is an issue
6 we could have discussed. I don't think it's relevant to
7 this case, so let's move on.

8 MR. HAIL: Thank you, Your Honor.

9 MR. KRUMHOLZ: Your Honor, I'll save the
10 last two exhibits then.

11 THE COURT: Okay.

12 MR. KRUMHOLZ: Can I take a two-minute
13 break and just go off the record for two to five minutes
14 to make sure I don't have any follow-up before I pass?

15 THE COURT: All right. We'll take a
16 short break.

17 MR. KRUMHOLZ: Your Honor, before we go
18 off the record -- I'm sorry -- can I sequester the
19 witness so he can't talk to his Counsel before I finish?

20 THE COURT: I think he's always entitled
21 to talk to his Counsel.

22 MR. KRUMHOLZ: Okay.

23 THE COURT: We didn't impose the Rule
24 here, but --

25 MR. NEIER: Your Honor, he won't talk --

1 THE COURT: Look, I don't want lawyers
2 now telling this witness how to answer his questions.
3 If you do that, you're violating my order.

4 (A recess was taken.)

5 THE COURT: Any other questions?

6 MR. KRUMHOLZ: We move for admission of
7 Exhibit 131-A, Exhibit 160.

8 THE COURT: We haven't talked about all
9 the exhibits, but has everybody seen all the exhibits
10 for both sides?

11 MR. JONES: Your Honor, I have not. If
12 those folks don't object, I'm not going to object.

13 THE COURT: I mean, I would prefer to
14 just get them all admitted.

15 MR. KRUMHOLZ: In fairness, we have been
16 running as fast as we can.

17 THE COURT: I understand. So hold off
18 on -- you're not going to get messed up, keeping the
19 numbers that you know you want because it may well be
20 that all of them get admitted.

21 MR. KRUMHOLZ: Well, at least the ones we
22 read from.

23 THE COURT: But what's going to happen is
24 we're going to onesy, twosy's and then we're going to
25 forget one. These series of e-mails, is that what you

1 are asking me to admit now?

2 MR. KRUMHOLZ: I actually want you to
3 admit all of what I used, but if you want me to --

4 THE COURT: Is there any objection to
5 those e-mails and the exhibits that he put on the board?

6 MR. HAIL: Your Honor, we haven't really
7 looked at them. I don't think we have an objection, but
8 I'd like a chance to look at them.

9 THE COURT: Has everybody got all their
10 exhibits together now so that the other side could have
11 them and we can go over them in the morning?

12 MR. KRUMHOLZ: Each side has exchanged
13 exhibits.

14 THE COURT: So in the morning we'll go
15 over the admissibility of exhibits.

16 MR. FIERO: Your Honor, I think the
17 problem is with exhibits like the ones Mr. Krumholz came
18 up with, which are laying in wait for witnesses as they
19 make their way to the stand.

20 MR. NEIER: We don't have any of these
21 exhibits, Your Honor.

22 MR. KRUMHOLZ: That's not true. That's
23 false.

24 MR. NEIER: They're not on the list.

25 MR. KRUMHOLZ: Let's bet on it.

1 THE COURT: Never mind that. Tomorrow
2 let me know if they're admissible. Are you through with
3 the witness?

4 MR. KRUMHOLZ: I pass the witness.

5 THE COURT: Okay. Are you going to take
6 him on direct now or are you going to take him on
7 direct --

8 MR. HAIL: Your Honor, I was going to
9 reserve my direct in our case in chief. I was just
10 going to address the issues that Mr. Krumholz brought
11 up, with your understanding that we get to call him
12 again.

13 THE COURT: But his direct is the
14 proffer.

15 MR. HAIL: That's correct.

16 THE COURT: So that would be a direct.
17 So you want to now also ask him about anything that he
18 brought up right now? Okay. Go ahead.

19 MR. HAIL: Your Honor, what I want to do
20 is ask Mr. Dean in direct in our case, get our ten
21 minutes to get Mr. Dean to explain his proffer. I think
22 you said that they are not entitled to cross-examine on
23 the same topics they just cross-examined him on, so I
24 don't think there will be any cross-examination of
25 Mr. Dean from what's in his proffer.

1 THE COURT: Okay. Go ahead.

2 MR. KRUMHOLZ: I just want to make sure
3 that it's clear. We intend to cross-examine Mr. Dean
4 about subjects we did not cover.

5 THE COURT: I understand. What he thinks
6 and what you think are two different things.

7 CROSS-EXAMINATION

8 BY MR. HAIL:

9 Q. Mr. Dean, do you have the documents that
10 Mr. Krumholz put in front of you in connection with your
11 testimony?

12 A. I do.

13 Q. Turn specifically first, please, to number
14 131, which is the document about values and growth. Do
15 you see that document?

16 THE COURT: Can somebody put these up
17 when you talk to them because I don't think I have them.

18 MR. HAIL: I don't know if we have them,
19 Your Honor.

20 THE COURT: Do I have them?

21 MR. HAIL: These are ones that --

22 THE COURT: Could somebody do it.

23 MR. SCHREIBER: Your Honor, this is Carey
24 Schreiber. We were given these at the beginning of the
25 hearing today. Fulbright & Jaworski has IT Exhibits 1

1 to 159. There is no 160 on this disk. In fact, this
2 happens to be blank.

3 THE COURT: Okay. Fine. But why don't
4 you-all put them up?

5 MR. NEIER: This is blank. You're going
6 to pay me \$500 million.

7 MR. KRUMHOLZ: We gave them to you
8 yesterday.

9 MR. NEIER: It's blank.

10 THE COURT: You-all can argue about this
11 later and it can come up in the argument tomorrow about
12 the admissibility of the document. He's going to
13 question him about some documents that I don't think I
14 have a copy of. Do I?

15 MR. NEIER: Nobody here has a copy
16 either.

17 THE COURT: I'm not asking that. Do I
18 have a copy?

19 MR. KRUMHOLZ: You do, Your Honor, I gave
20 them to you, but we're going to put it on the screen.

21 THE COURT: Where did you give it to me?
22 This one here?

23 MR. HAIL: That's one of them.

24 THE COURT: So either get them on the
25 screen as we go through or give me copies of all of them

1 so I can then deal with them as I go and make sure he
2 has a copy on the witness stand.

3 Q. (By Mr. Hail) Mr. Dean, do you have a copy?

4 A. I have a copy of 131-A and 160.

5 Q. That's the two I'm going to talk about.

6 THE COURT: Okay. This is 131-A and 160.

7 The thing that says Jeff Johnston at the stop is one
8 document that I have. Another thing is sent 9/14/07
9 from Sandy Dean on the top is the other one.

10 MR. HAIL: That's correct, Your Honor.
11 Those are the two documents we're going to look at. And
12 we're going to start with the Jeff Johnston document,
13 Your Honor. At the top is 131-A as Mr. Krumholz handed
14 it to me earlier today.

15 Q. (By Mr. Hail) Mr. Dean, Mr. Krumholz directed
16 your attention to a paragraph where you discussed the
17 redwood growth of the forest. Do you recall that
18 testimony?

19 A. I do.

20 Q. And if you look at page MARALIX 6620, do you
21 see that?

22 A. Yes.

23 Q. Can you explain to the Court what you meant
24 when you said that the redwood growth seems quite small?

25 A. Yes. The growth of the forest in 2007 was 100

1 million feet of conifer or something, but when you broke
2 that down, they harvested most of the redwood. And most
3 of the growth that they didn't harvest was Douglas Fir.
4 I would say the words most because there was some amount
5 of redwood that they didn't harvest.

6 Q. And why did you say that that seems quite
7 small to you? And I think you said the margin of error
8 or something like that you calculated at .35 percent.
9 Can you explain that to the Court?

10 A. I can. I wasn't aware that the harvesting --
11 prior to that time, I wasn't aware that the harvesting
12 had been focused on redwood. Maybe I could have known
13 that, but I didn't. And so when I saw that there was 7
14 million board feet of redwood growth that was not
15 harvested, I was commenting that that was a pretty
16 modest amount, and I would stand by that.

17 Q. What is the overall volume of redwood board
18 feet in the forest?

19 A. So it's probably 2.4 billion board feet or
20 something on that range.

21 Q. And you were commenting on the 7 million board
22 feet of growth, correct?

23 A. I was commenting on that the 7 million board
24 feet that wasn't harvested was a pretty small percentage
25 of the total amount of standing conifer volume in the

1 forest.

2 Q. Now, do you believe that that growth had no
3 value or some value?

4 A. I thought it had very modest value.

5 Q. And that's what you testified before?

6 A. It is. And it's what I testified in my
7 deposition also.

8 Q. Moving to the next paragraph on Douglas Fir,
9 please, in the forest. Can you explain for -- can you
10 explain to the Court what you meant when you talked
11 about the Douglas Fir growth in this paragraph?

12 A. Sure. So I commented on the fact that the
13 prices for Douglas Fir, particularly in California
14 relative to the costs of operation for Douglas Fir in
15 California, makes Douglas Fir stands when you have a
16 pure Douglas Fir stand, difficult to expect much value
17 to come out of that. However -- and I comment here that
18 a stumpage is probably not -- I think it's -- I say it's
19 unrealistic to value Fir based on its stumpage
20 contribution since there are also large and real costs
21 to get Fir out of the woods beyond log and haul.

22 And I would stand by that, although I
23 discussed this with Mr. Krumholz in my deposition. I do
24 think that Fir has some amount of value because it does
25 allow for better efficiencies in logging stands that

1 makes a contribution to the fixed cost of operating the
2 forest.

3 Q. When you harvest redwood stands, are there
4 sometimes Douglas Fir trees in those stands?

5 A. Yes. So most often redwood doesn't grow in a
6 pure redwood stand, it grows in a mix of redwood and
7 Douglas Fir, and both because its good forestry, because
8 regulators require it, and also because it defrays some
9 of the fixed costs of operating the forest. People
10 manage the Douglas Fir even when on a -- on a pure cost
11 basis people might be able to make the argument that it
12 doesn't contribute much, we think it contributes to the
13 fixed cost of the business.

14 Q. And all things being equal, a bigger Doug Fir
15 tree is worth more than a smaller Doug Fir tree?

16 A. Yes. And so that would also add to the value.

17 Q. So when you go harvest these mixed stands,
18 you're going to have bigger Doug Fir trees there, right?

19 A. Sure. As I suggested, I think, in my
20 deposition and in this e-mail, I think that the Fir is
21 of modest value, but not no value.

22 Q. Okay. Turning to the next e-mail, which was
23 the recollection of your conversation with Marathon in
24 September of 2007. Can you briefly set the stage for
25 what you were talking to Marathon about in September

1 2007?

2 A. Sure. You know, I had remembered meeting them
3 for lunch in the summer, but it must have been in
4 September. I think this was the first time that we had
5 met them in person. We had a wide ranging conversation.
6 It started without any real specific expectation of what
7 would occur. And it ended without a specific
8 expectation of what would occur. It was exploratory.

9 When I -- when I first met Marathon, they were
10 of the view -- I think they were mistaken, but they were
11 of the view that the lands were worth more than we
12 thought, perhaps considerably more. And I was -- I was,
13 to some extent, working to educate them about why the
14 lands likely were worth significantly less than the
15 debt. And although I didn't know what the lands were
16 worth, I did know it was worth significantly less than
17 the debt. And so that was the backdrop for this
18 conversation.

19 Q. What kind of a business deal did you have with
20 Marathon at that point in time?

21 A. None. In fact, this was really just an
22 opportunity for us to get to know them, them to get to
23 know us to determine if there might be any common
24 interest over time. And in fact, although we had this
25 lunch, we didn't have any substantive conversations

1 about working together for a couple of months. What we
2 discussed at the lunch I don't think had any bearing on
3 how we ultimately came to work together. It was a wide
4 ranging conversation that was where we got to know each
5 other, but nothing came out of it that was actionable.

6 Q. Okay. And if you turn to -- I don't know if
7 it's numbered, but I have it as the third page. This --
8 I will say paragraph begins about third from the bottom.

9 THE COURT: Still on Jeff Johnston?

10 MR. HAIL: No, I'm on 160.

11 THE COURT: The top says Sandy Dean,
12 9/14?

13 MR. HAIL: Yes, Your Honor. It is the
14 third page, which is 17685.

15 Q. (By Mr. Hail) And it is the third -- I guess
16 the second to the last full paragraph on the page
17 beginning with the bracket. Do you see that, Mr. Dean?

18 A. I do.

19 Q. Okay. And at the end of that you say there's
20 a phrase "a bogus appraisal." Do you see that?

21 A. Yes.

22 Q. Now, do you recall Mr. Krumholz started
23 playing 20 questions with you of did bogus mean this?
24 Do you remember that?

25 A. Yes.

1 Q. Can you explain to the Court what you meant --
2 or what you understood that term -- what did you mean
3 when you wrote that?

4 A. Thank you. You know, we've been involved in
5 timberland appraisals. I've reviewed timberland
6 appraisals from the outside. I think that timber
7 appraisals can have a high degree of subjectivity to
8 them. And frankly, it's been something that we've been
9 talking with the state about on and off now for over a
10 year, the need for greater -- greater quality control in
11 how appraisals are done.

12 And I think that here I was expressing concern
13 that -- I'm going to read the sentence to make sure that
14 I have this in context. I think that there -- I think
15 that Marathon was interested to figure out was there a
16 way to have an appraisal process go forward that could
17 put pressure on the bonds. And it was as simple as
18 that.

19 Q. Did you think that they were somehow proposing
20 to perpetuate a fraud or anything like that?

21 A. No.

22 Q. Did you subsequently think Marathon
23 perpetuated a fraud or a sham or a bogus thing or
24 anything like that?

25 A. No.

1 Q. What was your reaction to Marathon's view of
2 the value of the timberlands at this meeting?

3 A. I thought that there -- the view of the
4 timberlands was quite unrealistically high.

5 Q. And at that point in time, was Marathon a
6 creditor in the Palco case, to the best of your
7 knowledge?

8 A. In the Palco case, yes.

9 Q. I'm sorry, the Scopac case. Were they a
10 creditor in the Scopac case?

11 A. They were not.

12 Q. And did you have more expertise in timberland
13 and timberland valuation, did you think at that time,
14 than Marathon?

15 A. Yeah, I would say that the Marathon folks,
16 while well intentioned, had very little knowledge about
17 Scopac or what its capabilities were, what its value was
18 and what were the regulatory and political constraints
19 that would accompany any ultimate buyer of the property.

20 Q. If we go back up the previous paragraph,
21 there's a line that says "tap into equity at Scopac."
22 Do you see that?

23 A. Is it on the same page? Sorry.

24 Q. It is. I'm sorry. It's on 17685.

25 THE COURT: Where about?

1 MR. HAIL: It is in the middle paragraph,
2 the largest middle paragraph, Your Honor. I have it on
3 the fourth line down and about two-thirds of the way.

4 Q. (By Mr. Hail) The sentence begins "they
5 believe," on the third line, "Scopac cases are not going
6 to be separated; and therefore, even if they are
7 undercollaterized at Palco, they can tap into equity of
8 Scopac." Do you see that?

9 A. Yes.

10 Q. Mr. Dean, what do you recall being said about
11 that?

12 A. You know, I don't -- I don't really recall
13 this. You know, I was asked this in my deposition. I
14 didn't remember it clearly. And I -- I can only assume
15 that what --

16 MR. KRUMHOLZ: Your Honor, calls for
17 speculation. And in addition, it's calling for hearsay
18 from his own side.

19 THE COURT: Well, I don't want the
20 witness to speculate. He can testify to what he knows
21 and what he remembers, but not speculate.

22 MR. HAIL: Good enough, Your Honor.

23 Q. (By Mr. Hail) Subsequent to this meeting with
24 Marathon, was the Marathon/MRC plan designed to take
25 equity or value from Scopac and give it to Marathon in

1 any way?

2 A. Absolutely not.

3 Q. Do you recall any discussion about that at any
4 point in time?

5 A. No.

6 Q. And do you think Marathon's views of the value
7 of timberland evolved after they spoke with you?

8 A. Yeah. In fact, I can speak to that more.
9 Marathon came to our meeting in November, which was the
10 first time we had a substantive business conversation.
11 This was, I think, during a break in mediation. And I
12 think they came out thinking they would convince us that
13 the timberlands were worth \$600 million and that we
14 ought to be prepared to back some kind of reorganization
15 plan at a high level.

16 And we met with them for a day and another
17 half a day after that. And I think when they left, they
18 really had a very different view of the world and went
19 back to the mediation with the proposed plan of
20 reorganization that didn't work in mediation, but then
21 what was what we proposed in December. I think all of
22 that was quite an education for that.

23 Q. Now, if you go up to the top of the page,
24 we're still on 17685, there is a phrase sleight of hand.
25 Do you recall that?

1 A. I do.

2 Q. What did you mean when you wrote that?

3 A. You know, I was really was just commenting on
4 what had been repeated to me. I was surprised -- I was
5 watching the court case from the beginning, and I was
6 surprised when the Court allowed the burden of the log
7 deck to be transferred from Palco to Scopac. It helped
8 Scopac -- it helped Palco's cash flow a lot. I don't
9 think any value was harmed in any way from that because
10 Scopac has logs instead of cash, but it still has value.

11 But I was surprised that it had bought Palco
12 more time after they ran out of money on the DIP. The
13 DIP came in August, \$35 million. And by September they
14 were out of money again, but for this change. And I was
15 surprised by that. And the Marathon fellow commented
16 that he thought that that was a -- he used the words,
17 you know, a good sleight of hand by Mr. Hurwitz.

18 Q. And the Charles referenced in there is
19 Mr. Hurwitz, correct?

20 A. Yes.

21 Q. And who is Mr. Hurwitz again?

22 A. He's the chairman of Maxxam. Now, this was
23 his characterization of what happened. That doesn't
24 mean that -- it was just -- it was done in a joking way,
25 but he said it and I wrote it.

1 Q. Now, Mr. Krumholz gave you a series of
2 documents related to your discussions with Palco in 2005
3 and 2006. Do you recall that?

4 A. I do.

5 Q. And I don't have the e-mail because I haven't
6 been provided a hard copy of it, I don't want to argue
7 with him. I think it was Exhibit 34 where you
8 referenced the harvest rate of 90 million board feet.
9 Do you recall that?

10 A. Sure.

11 Q. In connection with those conversations,
12 Mr. Dean, did you form any value or any opinion as to
13 the value of the timberlands in that case or at that
14 time?

15 A. So this is, I think, a very important thing to
16 clarify. We had five months of conversations with
17 Maxxam, UBS, Palco, not so much Scopac really, although
18 we talked with them a little bit, but it was much more
19 focused on Palco over the course of January to June of
20 2006. And we really focused our energy and effort on
21 what will be paid for the stock of Palco if we valued
22 the Scopac equity at zero.

23 The reason we would value the Scopac equity at
24 zero is that it was very clear to us the Scopac
25 timberlands were worth less than their debt. How much

1 less, we didn't know. We didn't spend a lot of energy
2 on it because it was -- we were spending all of our
3 energy on this literally for five months, we still
4 didn't get across the finish line just to buy the stock
5 with Palco. So we knew that Scopac was going to have to
6 be restructured some day, but we felt like if it had to
7 be restructured -- the degree it was going to have to be
8 restructured wasn't so important for getting something
9 done to try and buy the stock of Palco.

10 So I'm sure -- I now am refreshed by seeing an
11 e-mail that there a model was run at 90 million feet, we
12 probably ran a model at a 100 million feet having seen
13 that, but we never came close to completing our due
14 diligence on the timberlands other than enough to assess
15 that the value would be worth less than the debt.

16 Q. Even -- so what was the results of running the
17 model at 90 million feet and the other assumptions,
18 vis-a-vis the value of the debt at that time?

19 A. So none of us had the benefit of the model,
20 but I'm certain that the result would have been less
21 than the debt.

22 Q. So did you ever try and estimate an actual
23 harvest for Scopac of 90 million feet a year?

24 A. No. I do recall and I think I may have
25 commented on this in my deposition, that we had thought

1 of ranges of harvest as being possible of 70 to 90
2 million feet of Scopac. We might have run 100 million
3 feet. That wouldn't surprise me, having now seen this.
4 But in fact, even as late December of this year,
5 December of 2007, we had hoped that we would conclude
6 that the harvest rate at Scopac could be 70 million
7 feet. And it was only really in the last two weeks of
8 January as we actually completed real timber due
9 diligence that we came to understand the specific
10 binding nature of the water board on the harvest in a
11 couple of specific watersheds, which by no surprise, I
12 suppose in hindsight, have the best and most harvestable
13 timber. And that's what drove the harvest rate down to
14 55 million feet for the first ten years.

15 Q. Now, there was also a fair amount of
16 discussion in your testimony about discount rates. Do
17 you remember that?

18 A. I do.

19 Q. Can you first describe to the Court what you
20 mean when you said a yield rate or a yield?

21 A. Sure. So this was talked about in my
22 deposition the other day. I think different people can
23 ascribe different meanings to this. This is what it
24 means to me. A yield rate is the -- in the way we think
25 about things, is the -- is the current return that you

1 make on an investment in one given year. So if you paid
2 \$100 for an investment, you would yield \$7 that year,
3 that would be a 7 percent yield.

4 Discount rate is the rate at which you would
5 decrease the value of future yields to bring back to the
6 present. And that would be applied across, you know,
7 multiple years. So if you weren't going to get the \$7
8 for three years, you'd divide it by 1.07 and raise it a
9 third and bring it back to today.

10 Q. Now, have you also heard discussions of cap
11 rates in this case?

12 A. I have.

13 Q. And can you describe for the Court how a
14 discount rate relates to a cap rate or a capitalization
15 rate?

16 A. Yes. So for me, to the extent that we're
17 talking about yield in a given year, that could also
18 probably be used synonymously with cap rate, the
19 capitalization rate of something. If it was yielding 7
20 percent, people typically would refer to a 7 percent cap
21 rate. But I think where it's been used more in these
22 proceedings is that at the end of a model -- in our case
23 we used a 50-year model and we had a cap rate at the end
24 of the model that was equal to one over the discount
25 rate. And that was how we made sure that the perpetuity

1 represented by the business would be captured in the
2 model.

3 Q. Now, is a capitalization rate particularly
4 significant for the MRC model?

5 A. It has very little significance in the MRC
6 model because we don't propose that the lands be sold in
7 the model until year 50. And so relatively large
8 changes in that assumption would have a very small
9 change on the net present value that the model produces.

10 Q. How about for shorter discounted cash flow
11 scenarios like one that's ten years, for example, how
12 would a change in cap rate affect that value?

13 A. So we have a changing cap rate in a ten year
14 model would be much more akin to a change in the
15 discount rate. Mr. Fleming in his model uses a
16 different cap rate than a discount rate in his model.
17 So he uses one discount rate for the first ten years and
18 then he uses a lower cap rate for the assumed sale
19 without necessarily really any -- any specific
20 justification.

21 But in that case, the cap rate is much more
22 important because it's only ten years out; and
23 therefore, the discounting of that is -- makes that a
24 much bigger number because it's not discounted as many
25 years as in our model.

1 Q. What is the effect of using a lower cap rate?

2 A. Makes a higher price.

3 Q. Mr. Krumholz asked you if you thought that an
4 8 percent discount rate was appropriate as of January
5 2007. Do you remember that?

6 A. Yes.

7 Q. Can you explain for Court why you think an 8
8 percent discount rate was appropriate then?

9 A. I can. So discount rate is probably the most
10 important investment judgment that gets made here as --
11 that's not timber specific. And it is -- it is the rate
12 that the model in many respects has the most sensitivity
13 to. Small changes in discount rate can have much bigger
14 effects on the model than small changes in log prices.

15 We've -- we've -- through my role at MRC,
16 we've spent a lot of time thinking about what's the
17 right discount rate and concluded, in conjunction with
18 the reorganization plan, that a 7 percent rate was
19 appropriate for our model in conjunction with the plan.
20 That really is based on a 6 percent discount rate for
21 what we would expect properties outside of California
22 that are well -- that are basically well-balanced and
23 without a lot of regulatory burden could trade for, and
24 adding a 1 percent premium for the structural issue that
25 exists in California.

1 In determining what would be an appropriate
2 discount rate for 2007, I have used my knowledge from my
3 time at MRC, my awareness of what other people in the
4 industry are doing, and my view as to what would be an
5 appropriate change given the investment environment, and
6 we've concluded that the discount rates would be 1
7 percent higher, at least at that time.

8 Q. What -- what have you observed in your role at
9 MRC as the trend in discount rates over the years?

10 A. So discount rates on timberlands have been
11 coming down for a number of years. I think really
12 probably the turning point for discount rates was in
13 2003 when treasury rates really troughed. And
14 there's -- there's a number of well-respected forestry
15 experts who track these things. And I think there's,
16 you know, a consensus that discount rates have been
17 coming down significantly over the last several years.

18 Q. What are some of those experts you just
19 referred to?

20 A. Gosh, Goldman Sachs has an investment bank,
21 you know, is one of the leaders in timber sales. They
22 have the view that discount rates have been declining
23 for several years.

24 MR. KRUMHOLZ: This is calling for
25 hearsay, Your Honor.

1 THE COURT: I don't think he can say --

2 MR. KRUMHOLZ: And move to strike the
3 answer.

4 THE COURT: I'm not sure what --

5 MR. HAIL: He's basing what he's talking
6 about his trend on what he understands is going on in
7 the marketplace. He's telling what other people has
8 observed.

9 THE COURT: He is trying to testify as to
10 what other experts -- what experts might have said about
11 discount rates. He's not an expert himself. He's given
12 us his opinion. They haven't objected to that. But I
13 think you can't ask him questions about what other
14 experts that are not here to testify would have said
15 about discount rates.

16 MR. HAIL: Well, he's testifying what
17 they would have said. He's testifying what they have
18 said, what he knows they've said.

19 THE COURT: That's hearsay.

20 MR. HAIL: He's just talking about what
21 he was told, what his understanding is.

22 THE COURT: That's hearsay.

23 MR. HAIL: Okay, Your Honor.

24 Q. (By Mr. Hail) In connection with this overall
25 trend that you've observed, has that influenced your

1 business at MRC at all?

2 A. We haven't sold or bought much property at
3 MRC, but it certainly influenced what we've done in this
4 case over 18 months. I could not have conceived in -- I
5 do not believe I could have conceived in January 2007
6 that we would be as aggressive a discount rate as we are
7 now ready to close.

8 Q. Okay. If we take a look back at, I think,
9 it's Exhibit 160 --

10 MR. HAIL: Which is the 9/14 e-mail, Your
11 Honor.

12 THE COURT: The Jeff Johnston or the
13 Sandy Dean?

14 MR. HAIL: Sandy Dean. There is a page
15 17684. Do you see that?

16 THE COURT: Second page.

17 MR. HAIL: Second page.

18 Q. (By Mr. Hail) And I'm on the fourth paragraph
19 from the bottom beginning "somewhere." Do you see that?
20 Do you see that, Mr. Dean?

21 A. I do, yes.

22 Q. Okay. And in there there's a statement about
23 premium yields and yields. And you said "I guessed at 7
24 percent to 8 percent." Do you see that?

25 A. I do.

1 Q. What did you mean when you said that?

2 A. I think this is a great point to clarify
3 because I was trying to help the Marathon folks
4 understand that the timberlands were worth substantially
5 less than the debt. And I made the argument to them
6 that given the regulatory, political and physical
7 constraints on this property, that a traditional
8 timberland buyer ought to expect not a 7 or 8 percent in
9 discount rate, but a 7 or 8 percent cash yield this year
10 for owning that property.

11 And that was -- I made a particular point to
12 talk to them about the political baggage associated with
13 this property, which I think for people outside of
14 California, Marathon is from York, is hard for them
15 probably to totally appreciate.

16 Q. And does that level -- what does that level of
17 yield imply for a discount rate moving forward, if
18 anything?

19 A. I'm not sure it implies a discount rate. It
20 really was intended to say -- in an effort, again, to
21 educate the Marathon folks on what I thought was the
22 significant difference in value between the debt and the
23 value of the lands, that if an investor was looking for
24 a 7 to 8 percent current yield, hey, we may have talked
25 about what would be estimates of reasonable cash flow to

1 come from the land.

2 If you apply these kind of yields to it, that
3 was going to yield a low number. And whether or not
4 that was the right yield for the buyer or not was not
5 what I was suggesting. It was really my way of working
6 to educate those guys that there was going to be a big
7 valuation gap to be dealt with here.

8 Q. I think the last subject of your testimony was
9 about log prices. Do you remember Mr. Krumholz asking
10 you questions about log prices?

11 A. Yes.

12 Q. Okay. And I believe the question was
13 something like all things being equal, a lower log -- or
14 a higher log price equals a higher value; is that right?

15 A. Yes.

16 Q. Would all things have been equal between
17 spring of 2008, for example, and January 2007 in the
18 valuation model of the timberlands, of the Scopac
19 timberlands?

20 A. I don't believe so. I believe that we -- and
21 I believe that any other investor would have an applied
22 a lower discount rate in the -- in the spring of 2007
23 than they would have applied -- excuse me, in the spring
24 of 2008 than they would have applied in January 2007
25 because of this significant trend of discount rates

1 coming down over time on timberlands.

2 Q. In addition, would you have taken -- do
3 investors look at -- let me start the question over.

4 Would you have taken the spot price or the
5 market price as of January 2007 and just gone with it?
6 How would you have used the January 2007 price in any
7 valuation?

8 A. So for somebody who buys 500 acres or 1,000
9 acres or 2,000 acres, a spot price can work pretty well
10 because you might harvest most of the timber that would
11 be harvested for the next 25 years in one or two
12 seasons. But for investors who are buying 200,000 acres
13 of land, I think most people -- we and most other
14 investors of similar size that I've talked about, all
15 look really at trend lines for log prices because it's
16 very clear in the case of this property regarding 4
17 billion feet of conifer, we wouldn't get all the conifer
18 out this year or next year. We won't ever get it all
19 out.

20 And so we need to make a reasonable estimate
21 of what would -- what will the log prices be over the
22 long-term. So yes, log prices are down today versus
23 where they were in 2007. We could talk about how much.
24 It's been 7 and 10 or 15 percent. But as was shown in
25 the model that was talked about in court the last time I

1 was here, to the extent that log prices are down right
2 now, it would be reasonable -- and what we did is we
3 assumed that they would rebound to a trend price and
4 then all of the long-term trend consisted of how we
5 operate our business.

6 Q. Now, did you go back and look at what MRC
7 thought it's price projections were for log prices in
8 2007?

9 A. I did.

10 Q. Can you describe to the Court what you went
11 back and looked at?

12 A. So -- yes. I understood the conversations
13 about this would involve how could we -- how could we
14 best estimate what we would have done if we were buying
15 the lands on January 17th, 2007. And the best way for
16 me to do -- the best way for me to think through how we
17 would have thought about that as of that moment was to
18 go back and look at our own internal Mendocino Redwood
19 Company estimates of log values as of our February 2007
20 budget meeting.

21 Once a year at Mendocino Redwood Company we
22 have a budget meeting where we make predictions of a
23 whole bunch of things about our business, including log
24 values.

25 Q. And then how did you take that information to

1 look at how it might have affected overall value of the
2 Scopac timberlands?

3 A. So our 2007 budget book contains a three-year
4 outlook for log prices. And I took those prices, which
5 are basically flat, and they're roughly \$950 for redwood
6 and \$435 for Douglas Fir. And I put those into the
7 valuation model that we used in conjunction with the
8 reorganization plan and combined that with our long-term
9 view that log prices will not experience inflation above
10 the general rate of inflation of the economy and look at
11 what would be the resulting value on the timberlands.

12 Q. I'm going to show you what we've marked as
13 Exhibit 205 -- it's 206. Thank you, John. I don't know
14 if that's going to show up. I'm going to work off the
15 screen, Sandy. Can you see it on the screen?

16 A. I can. It's pretty small.

17 Q. Can you describe what this spreadsheet is?

18 A. Sure. So this is the 50-year timber model
19 that we used to come up with our plan of reorganization.
20 And this is a version that I changed myself to reflect
21 what our 2007 board book -- budget board book view of
22 log prices was for 2007, 8 and 9. And then I combined
23 that with our long-term view that log prices would not
24 exceed the general rate of inflation in the economy.

25 Q. Okay. And where did that result in a change

1 in this, if you remember? Do you know which line
2 changed?

3 A. Sure. If you were to look at cell B32, there
4 is a price there that says \$352 million. Now, we've
5 compared to the valuation that we came up with in
6 conjunction with the reorganization plan of \$397
7 million. So it's a \$45 million decrease from what we
8 have in the spring of 2008.

9 Q. And what is the only difference then between
10 this document and the valuation model you ran in the
11 spring of 2008? What is the only variable that you
12 changed?

13 A. The only thing that's changed here is our
14 February 2007 budget view of log prices versus our
15 spring 2008 view of log prices.

16 Q. And did that change only then line 13?

17 A. Yes.

18 Q. Revenue?

19 A. Yes. And I was surprised that this caused a
20 decrease in our valuation. And I think the reasons that
21 it caused a decrease is that in our spring 2008 model we
22 did assume that log prices come down for 2008, 9, 10, 11
23 relative to long-term trend line. But by 2011, 2012, we
24 brought the logs back to trend line at levels that are
25 higher than what we would have possibly imagined being

1 in January 2007.

2 In January of 2007, we were coming off of, you
3 know, some great economic years, and yet we still
4 thought log prices would be flat. And our view has
5 been, you know, log prices would be flat because of
6 lumber markets and because of substitute threats to
7 redwood. So this was a surprising result, but I think
8 it reflects where we were in early 2007.

9 MR. HAIL: Your Honor, I have no more
10 questions. And actually, I think Mr. Dean has pretty
11 much covered it. I'm going to move for the admission of
12 his proffer at this point in time.

13 THE COURT: Okay.

14 MR. KRUMHOLZ: Your Honor, the only
15 objection I have -- I guess I have two objections. A, I
16 would like to object, reurge my previous objection at
17 the confirmation hearing that it is expert testimony.
18 And he hasn't produced any expert documentation. And,
19 in fact, they have refused to do so. And I understand
20 the Judge's -- the Court's thoughts on that.

21 THE COURT: I haven't seen the -- I
22 haven't had a chance to read Mr. Dean's proffer, so I'll
23 read it over the evening and will rule on that when we
24 get back.

25 MR. KRUMHOLZ: I have one our objection,

1 Your Honor. In one of the paragraphs -- I don't have it
2 in front of me -- it goes through a list of hearsay from
3 other companies, much like he was about to testify to
4 with respect to Goldman Sachs. There are five
5 companies. I move to strike all of that paragraph.

6 THE COURT: Okay. I think we probably
7 will put his proffer on at the time of your case.

8 MR. HAIL: Okay, Your Honor.

9 THE COURT: All right. Any other
10 questions for this witness now? Anybody else at this
11 table? This table? Yes.

12 SPEAKER: Your Honor, if I may.

13 MR. HAIL: He's a noteholder. Shouldn't
14 he have gone --

15 THE COURT: Well, I'll let him ask some
16 questions.

17 MR. NEIER: Your Honor, we shouldn't be
18 able to sandwich witnesses like this.

19 MR. HAIL: This is sort of redirect on
20 redirect. He's sitting at the same table. It's
21 something we haven't done.

22 THE COURT: They crossed him directly. I
23 don't know, how many questions are you going to ask? Is
24 this long?

25 SPEAKER: Your Honor, I want to reserve

1 our rights on behalf of our noteholder clients. We've
2 heard some extremely disturbing testimony and extremely
3 disturbing e-mail that I think casts great doubt on the
4 good faith of the proponents with respect to this plan.
5 This is not the way the bankruptcy process ought to
6 function.

7 THE COURT: So you're not asking
8 questions, you want to argue?

9 SPEAKER: No, Your Honor. I want to
10 reserve our rights. We're not asking the Court to take
11 any action now. But I don't want our inaction -- look,
12 we heard in the past that if the Indenture Trustee just
13 went through a trial and didn't raise heck, that it was
14 somewhat a forfeiting of rights. I want to make sure
15 that argument isn't made here with respect to this.
16 It's very troubling. We want to reserve our rights.
17 Thank you, Your Honor.

18 THE COURT: Anyone else? All right. You
19 can step down.

20 MR. KRUMHOLZ: Well, I did have one other
21 question.

22 THE COURT: Okay. Well, let's hear it.

23 MR. KRUMHOLZ: Is this re-redirect?

24 THE COURT: It's re-redirect, so go ahead
25 and ask it.

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REDIRECT EXAMINATION

BY MR. KRUMHOLZ:

Q. Mr. Dean, did you say 2.9 billion in inventory?

A. I think I said 4 billion of conifer inventory.

Q. 4 billion conifer inventory?

A. And 2.4 billion of redwood, give or take.

Q. Do you remember telling the Court --

MR. KRUMHOLZ: For some reason it's showing a shadow. Is there supposed to be a light somewhere?

THE COURT: I don't know. There are lights. They're supposed to be turned on.

MR. KRUMHOLZ: Well, can I approach the witness?

THE COURT: Sure.

Q. (By Mr. Krumholz) Mr. Dean, you told the Court during the confirmation hearing, did you not, that there was 777 million board feet out of the 3.9 billion board feet of total conifer volume, did you not?

A. You know, I can look at the words. The 777 is what's harvestable today. It's our view of the volume of conifer inventory that's harvestable today that we would expect to harvest over the next 15 years. And when you grow it, you'll get more than that over 15

1 years because it will grow.

2 MR. KRUMHOLZ: I think I got the answer I
3 needed.

4 THE COURT: Okay. Thank you. Now you
5 can step down. All right.

6 MR. KRUMHOLZ: Actually, I have one more.
7 I apologize, Your Honor.

8 Q. (By Mr. Krumholz) Did you state that the
9 watershed -- did you say that the watershed has provided
10 more availability, the availability of the Bear-Mattole?
11 Did you mention that?

12 A. The watershed analysis that was conducted by
13 Scopac over 2007 and early 2008 has freed up some
14 availability, yes.

15 Q. Are you talking about the Bear-Mattole area?
16 Is that the same thing?

17 A. The watershed analysis that has freed up
18 volume has freed it up in a couple of areas; I think
19 Bear-Mattole is one of them.

20 Q. And Bear-Mattole is the vast majority of that
21 area, do you know?

22 A. You know, I would have to go back and look at
23 Mr. Barrett's proffer to be sure about that.

24 Q. You're not attributing any value to the
25 Bear-Mattole becoming available, are you?

1 A. Am I attributing value to the Bear-Mattole
2 becoming available where?

3 Q. Where?

4 A. What do you mean?

5 Q. The Scopac forest.

6 MR. JONES: Your Honor, objection. I
7 think it's vague and I think the witness clearly means
8 what analysis. At least I think that's what he's
9 asking. If not, it's vague.

10 Q. (By Mr. Krumholz) Is there a notion that the
11 Bear-Mattole will become harvestable soon?

12 A. Some of the volume that has been freed up
13 through watershed analysis is in the Bear-Mattole, yes.

14 Q. The vast majority of what is going to be freed
15 up is in connection with the Bear-Mattole as opposed to
16 other areas, correct?

17 A. You know, I do recall of the amount of timber
18 that's been freed up in the watershed analysis, most of
19 it is Fir, and I think that has limited value. But
20 that -- there's about 40 million feet of redwood that
21 has been freed up, and that has more significant value.

22 MR. KRUMHOLZ: Thank you. Pass the
23 witness.

24 THE COURT: Now you can step down
25 quickly. Okay. Do we have a short witness?

1 MR. NEIER: He's medium height, Your
2 Honor.

3 MR. KRUMHOLZ: Your Honor, I think it's
4 going to take a little while.

5 THE COURT: Who's the next witness?

6 MR. KRUMHOLZ: It's Mr. Radecki.

7 MR. BRILLIANT: I don't think that we can
8 finish him tonight, Your Honor, but I'm more than happy
9 to start him.

10 MR. KRUMHOLZ: I'd rather start in the
11 morning if we're not going to finish.

12 THE COURT: Who are we talking about?

13 MR. KRUMHOLZ: Mr. Radecki, Joe Radecki,
14 he's the next witness.

15 THE COURT: And is he -- can you at least
16 put on his direct?

17 MR. KRUMHOLZ: Sure, absolutely.

18 THE COURT: And then we'll start with
19 cross in the morning.

20 MR. BRILLIANT: Thank you, Your Honor.

21 THE COURT: Are we operating under the
22 rule that you get ten minutes on direct, is that what it
23 is? I know in the two cases we're doing them
24 differently, but in the this case you're getting ten
25 minutes on direct plus his proffer.

1 MR. KRUMHOLZ: Yes, Your Honor. I wanted
2 to tell you that --

3 THE COURT: But you don't have to use it
4 if you don't want to.

5 MR. KRUMHOLZ: I know. I think it may
6 take two or three minutes longer, but not more.

7 THE COURT: Than ten minutes?

8 MR. KRUMHOLZ: Yes, 10 or 15 is my best
9 estimate. I haven't practiced it or anything, I just
10 think it's about that.

11 MR. FIERO: We agreed to ten. And he's
12 got a proffer, Your Honor.

13 THE COURT: I know. Have you been sworn
14 yet?

15 MR. RADECKI: I have not.

16 THE COURT: Okay. Swear the witness.

17 JOSEPH RADECKI, JR.,
18 having been first duly sworn, testified as follows:

19 THE COURT: And his proffer is what
20 number?

21 MR. KRUMHOLZ: Exhibit 6, Your Honor.

22 THE COURT: Is it 6 of the stuff I that I
23 was given, the two volumes that I was given? Does
24 anyone know?

25 SPEAKER: It's on the other side, Judge.

1 THE COURT: I know you've got all of
2 those, but I was given all the proffers, wasn't I?

3 MR. McDOWELL: It's No. 11, Your Honor.

4 THE COURT: Okay. Got you.

5 DIRECT EXAMINATION

6 BY MR. KRUMHOLZ:

7 Q. Mr. Radecki, can you introduce yourself to the
8 Court.

9 A. My name is Joseph Radecki, Jr. I'm an
10 investment banker currently working for Tre Angeli, LLC.

11 MR. KRUMHOLZ: Your Honor, may I
12 approach?

13 THE COURT: You may.

14 Q. (By Mr. Krumholz) Mr. Radecki, what is
15 Exhibit 6 that I handed you?

16 A. It's a declaration that constituted my
17 proffer.

18 MR. KRUMHOLZ: Your Honor, we move for
19 admission of Exhibit 6.

20 THE COURT: You can read the whole
21 proffer in less than ten minutes. How can you summarize
22 it in more than ten minutes?

23 MR. KRUMHOLZ: That's a very fair
24 question.

25 THE COURT: I have read this proffer,

1 actually, so I'm familiar with it. Go ahead.

2 MR. KRUMHOLZ: I move for the admission
3 of Exhibit 6, Your Honor.

4 THE COURT: Any objections? It's
5 admitted. Again, I've said it's now admitted, but I
6 really want to be able to say every exhibit is admitted
7 other than whatever, so that way we know everybody got
8 everybody's in. So go ahead.

9 Q. (By Mr. Krumholz) Can you summarize your
10 education, Mr. Radecki.

11 A. A bachelor of arts from Georgetown University
12 in 1980.

13 Q. And what do you do for a living?

14 A. I'm an investment banker.

15 Q. Can you give us a flavor for your professional
16 experience.

17 A. I've acted either in the securities business
18 or the investment banker for the previous 28 years since
19 I graduated from college. I spent the first three years
20 of my career at Merrill Lynch, Pierce, Fenner & Smith on
21 the security side of the business. For the past
22 approximately 25 years I've been on the investment
23 banking side of the business, first starting in 1983
24 with Drexel Burnham Lambert in their high yield and
25 convertible bond trading business, first in a management

1 role and later on in their international capital markets
2 desk out in Beverly Hills.

3 When Drexel went bankrupt, myself and others
4 started the corporate finance and investment banking
5 effort at Jeffries & Company where I spent the next
6 eight years running primarily their financial
7 restructuring group, as well as group working on
8 recapitalizations.

9 In 1998 I left Jeffries to basically perform
10 the same function at CIBC Oppenheimer, which later
11 became CIBC World Markets, Corp. I was there through
12 the end of 2005, again, running their financial
13 restructuring and recap group, special situations
14 advisory team. From 2006 through the beginning of 2008
15 I was with Piper Jaffray & Company, again, running their
16 restructuring group. And since March of 2008, I have
17 been in my own business.

18 Q. Now, I just recently read your deposition and
19 I noticed a whole lot of questions, to me like over half
20 of them were in connection on whether or not you're a
21 timberland expert. Are you a timberland expert?

22 A. I am not.

23 Q. You don't consult with or for timberland
24 companies, do you?

25 A. No, I do not.

1 Q. Do you specialize with respect to your work in
2 connection with timberland companies at all?

3 A. No, I don't specialize.

4 Q. So just -- that should take a lot of
5 tomorrow's cross. But I wanted to ask you this: Do you
6 understand that one of the issues in this proceeding is
7 the difference between the value at January 18, 2007 and
8 now?

9 A. I do.

10 Q. Can you tell the Court how you help him make
11 that decision.

12 A. I believe I was called to opine upon the
13 manner in which the economic conditions in our economy
14 in general, as well as the -- how that has impacted
15 various markets from real estate to financing
16 opportunities has changed the environment. And in turn,
17 changed and roughly devalued many situations.

18 MR. KRUMHOLZ: I tender Mr. Radecki as an
19 expert in financial markets for distressed and stressed
20 assets, as well as other assets.

21 THE COURT: Any objection? I guess not.
22 Okay.

23 Q. (By Mr. Krumholz) Mr. Radecki, how would you
24 go about assessing the value of stressed or distressed
25 assets generally from a macro perspective and from an

1 assets perspective?

2 MR. JONES: Your Honor, I'm going to
3 object at this point. Your Honor made the point, I
4 think jokingly, but the proffer is three pages long.
5 Counsel could read the whole thing in less time than he
6 has. I don't think the rule -- or the procedure we have
7 here is intended to permit Counsel to go beyond what he
8 put in his proffer during this ten minute introduction.
9 We've already had Counsel, you know, attempt to preempt
10 impeachment, which is improper. And now we're going to
11 go into stuff that isn't covered in the proffer, and I
12 don't think that's the procedure Your Honor adopted.

13 MR. BRILLIANT: Your Honor, Alan
14 Brilliant on behalf of Mendocino. I actually
15 have partly the same objection. You know, this is not
16 something that's covered in the proffer at all. There's
17 nothing in the proffer about how you go about, you know,
18 valuing financially distressed assets. That's not even
19 the nature of what's even covered in the proffer. The
20 proffer talks about occurrences in the economy and an
21 opinion as to what effect that has on timberlands
22 generally since midsummer. That's all the proffer deals
23 with. It does not deal with how financially distressed
24 assets are valued.

25 MR. KRUMHOLZ: Your Honor, this is really

1 all ado about nothing. All I was going to ask him is
2 what's the difference between asset specific analysis
3 and market. What did you do? Market.

4 THE COURT: So now let's move on.

5 Q. (By Mr. Krumholz) Okay. Did I just describe
6 it correctly? You did a market analysis, macro economic
7 analysis in terms of the timberlands?

8 A. Correct. I did not value the specific Scopac
9 assets. I took a look at the market and how the factors
10 that are in the market may have impacted those assets.

11 Q. And tell the Court what your opinion is in
12 that regard.

13 A. My opinion is that there has been a
14 significant deterioration in the macro economic climate
15 that since roughly the end of 2006 and the beginning of
16 2007, first evidenced by what's been called the subprime
17 crisis, that there have been a domino series of events
18 in those markets and in the financial markets that have
19 caused significant liquidity to leave the markets and a
20 significant devaluing of assets, in addition to
21 significant credit crisis that has caused primarily
22 credit for all assets to be either unavailable or more
23 expensive.

24 To sort of break it down into its component
25 parts, the subprime crisis obviously caused a

1 significant number of commercial and investment banks,
2 as well as other finance vehicles, to not only report
3 losses due to increased default rates and foreclosure
4 rates for subprime loans in their particular conduits or
5 their finance vehicles, but that in turn constricted
6 capital that was available for them to make available to
7 any number of other markets. This, in turn, has
8 impacted the -- both the spreads that we see in the
9 credit markets that has become more expensive, where
10 covenants are back and the like.

11 Additionally, many markets have become
12 completely aliquid. And we're seeing a credit crisis
13 not unlike -- pretty much unprecedented for this
14 particular country. People go back to the Great
15 Depression, but the reality is that the credit markets
16 as they exist today with, you know, 1.2 trillion dollars
17 worth of subprime mortgagees, that market didn't exist.
18 The debt markets in general didn't exist in the 1920's
19 and 30's as they exist today. So this is a crisis that
20 we haven't seen before. Obviously this has led to a lot
21 of other, you know, difficulties in the economy.

22 MR. JONES: Your Honor, I'm sorry, I have
23 to renew my objection. The question apparently was what
24 do you wish we put in your proffer that we didn't.
25 We've now gotten a two-minute narrative, none of which

1 was in the proffer. There's nothing in here about the
2 Great Depression, the unprecedented --

3 THE COURT: He has his ten minutes. And
4 there is information in here about the real estate
5 market collapse, about the foreclosed property, unsold
6 inventory, about reduction of values, about the
7 financial vehicle lending market, increased lending
8 standards, and the toughening up of credit. So again,
9 ask your question.

10 Q. (By Mr. Krumholz) You were answering my
11 question. Go ahead.

12 A. Yeah. I mean, so the financial markets are
13 obviously in fantastic difficulty. The combination of
14 what's happening in subprime has now bled out to other
15 markets including prime mortgages. That has led to the
16 real estate market, you know, essentially collapse as
17 residential construction has dried up to a significant
18 point. A lot of the home builders have been forced to
19 sell land that they had inventoried for potential new
20 residential construction.

21 Obviously there's a lot of unsold or
22 foreclosed property on the market. And now we're
23 starting to see the slow down in non-residential
24 construction, some caused by the general economic
25 conditions, some caused by the lack of credit

1 availability.

2 We've also seen a significant number of
3 players leave -- players, when I say players, credit
4 players, leave the marketplace generally, be they hedge
5 funds or, again, the restriction of capital of certain
6 investment vehicles. The CDO market has become
7 completely aliquid and is no longer available to invest
8 in the marketplace. And that was the significant part.
9 Most people allocate roughly 40 percent of the
10 non-investment trade credit market was due to the CDO
11 market.

12 Q. And then I think you have kind of an ultimate
13 conclusion at the end of paragraph 6. Could you tell us
14 what your ultimate conclusion is in connection with the
15 value?

16 A. We've seen varying degrees of assets be
17 devalued over time. And I guess for the purposes of
18 this trial, the asset class that has become most
19 devalued is that asset class which has traditionally had
20 large asset value. Some people have called it stick
21 value from time to time. Usually that's used in the
22 context of meeting properties. But it's properties that
23 have had good asset value, but generate relatively low
24 current earnings.

25 That is the class that has been most impacted

1 by the credit crisis where it is difficult to get
2 financing for those assets. Those assets have been
3 devalued the most because of the way credit impacts
4 ultimate valuation.

5 Q. And the basis for your valuation opinions,
6 we've marked as Exhibits 9.1 to 9.4. Could you tell us
7 what those are?

8 MR. FIERO: Objection, Your Honor, he
9 hasn't offered any valuation opinions.

10 MR. KRUMHOLZ: Valuation related
11 opinions.

12 THE COURT: There are some exhibits that
13 you are -- that he is using? It's not part of his
14 proffer?

15 MR. KRUMHOLZ: It's all of the analyst
16 reports that he has used as the basis of his opinions.

17 THE COURT: What analyst report?

18 MR. NEIER: Your Honor, just based on the
19 gold and fast rule, maybe we shouldn't allow any other
20 analyst reports to come into evidence.

21 MR. KRUMHOLZ: Actually, he's an expert
22 and Mr. Dean is.

23 MR. HAIL: That doesn't mean it comes in.

24 MR. NEIER: Doesn't mean that it's not
25 hearsay.

1 THE COURT: He is capable of testifying
2 about things that he read, that's true, but you can't
3 independently put in other experts' opinions through his
4 opinion. I mean, he is entitled to talk to other
5 experts or read documents and things of that sort.

6 Q. (By Mr. Krumholz) Did you also form opinions
7 concerning auction rate securities?

8 A. I did.

9 Q. What are those opinions?

10 A. I mean, the auction rate security market is
11 largely frozen right now. There's very little bit of it
12 operating. Most of what is operating relate to
13 municipal securities, and only on the bond side. The
14 auction rate preferred market is completely frozen and
15 not operating. It is largely in default. The major
16 investment banks and the Fed are actually working on
17 trying to figure out a system to get that market going,
18 but there has been a significant devaluation in that
19 market caused by complete collapse of liquidity.

20 Q. Is it your opinion they have virtually no
21 liquidity?

22 A. There is no liquidity, certainly on the
23 preferred side, and extremely limited on the bond side.

24 MR. KRUMHOLZ: Pass the witness.

25 THE COURT: All right. So we'll take his

1 cross tomorrow. You can step down. We're going to
2 start -- do we have anything else tomorrow? So we have
3 a hearing -- so can we start at 8:30 tomorrow? Will
4 that work for everybody? 8:30. Thank you.

5 MS. COLEMAN: Your Honor, I hate to be a
6 pest on the cash collateral.

7 MR. FIERO: Your Honor, the Committee is
8 fine with the ordinary use of cash collateral. There's
9 no reason why any professional needs to get paid any
10 time this week.

11 THE COURT: Well, we already had the
12 agreement, I think, from Mr. Greendyke that we just hold
13 that off and we approve the use of cash collateral and
14 reserving --

15 MS. COLEMAN: Yes, Your Honor, but
16 Mr. Fiero said any professional. There are other
17 professionals that are scheduled to be paid. So I
18 thought your objection was just the Indenture Trustee.
19 You're not willing to not pay any professional?

20 MR. FIERO: Your Honor, I think Gibson
21 Dunn is due \$2 million in the next couple of weeks, I'm
22 not sure exactly when, but I don't see any reason why
23 this is going to wrap up and all of these issues are
24 going to be wrapped up together that that issue can't
25 wait. And that the professionals like the professionals

1 at Palco --

2 THE COURT: I'm not certain that the --
3 and all the professionals wait?

4 MR. FIERO: The professionals at Palco
5 have been waiting since April, Your Honor, no payments
6 going out of Palco.

7 MS. COLEMAN: Your Honor, that's
8 completely irrelevant. We have an agreement from
9 everybody who has an interest in the cash collateral
10 that the budget is to be paid as budgeted. It's simply
11 not fair for the Committee, which has no interest.

12 THE COURT: How much are we talking about
13 in professional fees?

14 MS. COLEMAN: Your Honor, I apologize, I
15 don't have the budget in front of me.

16 MR. LITVAK: I have it, Your Honor.

17 THE COURT: How much is it.

18 MR. LITVAK: It's \$4.6 million in
19 professional fees going to just the end of this month.

20 MS. COLEMAN: No. The end of this month
21 is today.

22 MR. LITVAK: The problem, Your Honor, is
23 if Scopac is permitted to make those professional fee
24 payments, then they're going to go negative on cash, and
25 that's going to require them to borrow money from Lehman

1 and the Committee has objected to that. It's not
2 necessary if Scopac is --

3 THE COURT: Well, I haven't approved the
4 Lehman borrowing.

5 MR. LITVAK: No, haven't.

6 MS. COLEMAN: Your Honor, four hours ago
7 we had an agreement that everybody said they were fine
8 with that if the Indenture Trustee would agree that they
9 would reserve their rights to go back to the second cash
10 collateral order, which is what we have asked for, then
11 Scopac would have authority to write checks and pay us.
12 And this is just a retrade after a difficult hearing,
13 and it's ridiculous.

14 MR. LITVAK: We had a legal objection.

15 THE COURT: I will allow you to use cash
16 collateral tonight, if you can do it, for anything but
17 professionals. We'll discuss the professionals
18 tomorrow.

19 MS. COLEMAN: Thank you, Your Honor.

20 THE CSO: All rise.

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THE STATE OF TEXAS:

COUNTY OF NUECES:

I, SYLVIA KERR, Certified Court Reporter in and for the State of Texas, do hereby certify that the above foregoing contains a true and correct transcription, to the best of my ability, of all portions of evidence and other proceedings requested in writing by counsel for the parties to be included in this volume of the Reporter's Record in the above-styled and numbered cause, all of which occurred in open court and were reported by me.

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