

IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF ALASKA

IN RE: §
§
NAKNEK ELECTRIC ASSOCIATION, INC. § Case No. A10-00824-DMD
§ Chapter 11
THE DEBTOR §

THIRD SUPPLEMENT TO MOTION FOR APPROVAL OF TRANSACTION
[Relates to Dkt. #s 366, 373, 375]

The Debtor seeks approval of the Collateral Disposition and Settlement Agreement attached hereto and supplements the Debtor's Motion For Order (1) Approving Sale Of Drill Rig & Accessories Free & Clear of Liens or Other Claims and (2) Approving Use of Sale Proceeds To Plug & Abandon Well ("Motion")(D.E. 366, 373 and 375) as follows:

BACKGROUND

1. The Debtor owns equipment known as Rig #7 which it purchased to drill an exploratory geothermal well. National Rural Utilities Cooperative Finance Corporation ("CFC") has a UCC lien against the rig. CFC's lien is second in position to the liens of various vendors who have mining liens or whose mechanics liens against the rig and rig-related assets compromised in amount and agreed as to efficacy in adversary proceeding no. 11-90007 and pursuant to main case order (D.E. 387).

2. CFC's lien extends to the assets comprising the rig itself, which are all of the assets listed on **Exhibit A** on pages one through three (the "CFC Rig Collateral"). BHO and the Non-Baker Hughes M&M Lien claimants have liens on the CFC Rig Collateral which have priority to CFC's lien. These liens are in the approximate amount of \$5,500,000 and are further described in the Order entered at Docket Entry 387. The Baker Hughes M&M Lien Claim constitutes approximately 83% of the total M&M liens and is in the approximate amount of \$4,500,000. The M&M lien claimants's liens also extend to certain machinery and equipment

related to the rig and the geothermal operations and not covered by CFC's UCC lien, which assets are listed on page four of **Exhibit A** (the "Residual Rig Related Assets").

3. As set forth in the Motion and the two supplements filed by the Debtor, the Debtor has been negotiating with Baker Hughes Oilfield Operations, Inc. ("BHO") for a transaction in which the rig and related equipment would be transferred to BHO or its assignee in return for valuable consideration from BHO for the Debtor and its estate. Other parties in interest have participated in the negotiations since the motion was filed. These include CFC and the other secured creditors with liens against the rig assets. The negotiations have resulted in substantial changes to the form of the transaction that is the subject of the Motion and some changes to the economics, including increased benefits to be received by the Debtor and its estate. The purpose of this supplement is to explain the revised transaction in some detail and to analyze the compromises therein pursuant to Rule 9019.

DESCRIPTION OF THE TRANSACTION

4. The Purchase and Sale Agreement outlined in the original Motion has been rewritten and is now titled "Collateral Disposition and Settlement Agreement" ("CDSA"). A true and correct copy of the CDSA is attached as **Exhibit B** and incorporated herein. The CDSA is discussed in more detail below, but it can be summarized as consisting of five things: (1) Debtor acknowledgement of basic facts associated with the rig and need to plug the well; (2) foreclosure subsequent to the lifting of automatic stay of CFC's security position in the CFC Rig Collateral; (3) sale to BHO of the Residual Rig Related Assets; (4) authorization to plug the well and incur the associated expenses; and (5) settlement of disputed claims.

A. Acknowledgements And Disposition of CFC Rig Collateral

5. As announced at the August 10, 2012 hearing on the Motion, the Debtor, CFC, BHO, and the other secured creditors have revised the transaction such that BHO will exercise CFC's UCC lien rights to acquire the CFC Rig Collateral. The Debtor acknowledges that CFC has a valid and perfected UCC lien on the CFC Rig Collateral,¹ and CFC's lien is subordinate only to the Baker Hughes M&M Lien Claim and the Non-Baker Hughes M&M Lien Claims. By separate agreed motion, CFC and BHO have sought a lifting or modification of the automatic stay in order to permit the foreclosure of the CFC lien.

6. Upon approval of this Motion, Baker Process, Inc. ("BPI") shall publish in the Anchorage Daily News the Notification Of Public Disposition Of Collateral contained in the attached CDSA and shall copy same to all persons who have given written notice of interest in buying the rig, namely Nordaq Energy and Cook Inlet Energy. The foreclosure sale will be conducted on the 17th day after notice (the UCC provides that ten days notice is commercially reasonable). The foreclosure sale will be held at the offices of Burr, Pease & Kurtz, 810 N Street, Suite 300, Anchorage AK 99501. BPI will be entitled to credit bid in accordance with the CFC/Baker Hughes Intercreditor Agreement. Others desiring to bid will need to cash bid and start at \$7,500,000, in view of all the consideration BHO is giving and the Debtor is receiving under the proposed CDSA transactions.

7. Pursuant to the CFC/Baker Hughes Intercreditor Agreement, BPI, a BHO affiliate, has been assigned the rights under the CFC Security Agreement solely with respect to the CFC Rig Collateral. The Approval Order will provide that CFC's transfer to BPI of rights under the CFC Security Agreement solely with respect to the CFC Rig Collateral is in

¹ Capitalized terms have the meanings set forth in the CDSA.

compliance with, and sufficient notice has been given in accordance with, Bankruptcy Rule 3001(e), and CFC waives any requirement that the Clerk send CFC 21 days notice of the transfer and any objection to the transfer made in accordance with the CDSA and the CFC/Baker Hughes Intercreditor Agreement. Further, the CDSA contains the Debtor's agreement to the provisions governing the transfer of the CFC Security Agreement to BPI and the transfer of any deficiency from BPI to CFC. The CDSA establishes commercially reasonable foreclosure sale procedures, form of notice of foreclosure and foreclosure notice period in compliance with the Alaska UCC (AS 45.29.601 – 628).

8. As requested in the Motion, the effect of such foreclosure sale shall vest the purchaser, whether BPI by credit bid or some third party bringing at least the minimum cash bid starting at \$7,500,000, with title free and clear of liens, encumbrances and interests other than the Baker Hughes M&M Lien Claim and the Non-Baker Hughes M&M Lien Claims. There are, however, Intercreditor Agreements between BHO and CFC (the CFC/Baker Hughes Intercreditor Agreement) and among secured creditors with liens against the rig assets (the Secured Creditors Intercreditor Agreement). These Intercreditor Agreements provide rights to CFC and the other Secured Creditors and duties upon BHO and BPI, as more fully set forth below and in the CDSA and Intercreditor Agreements. Three of the holders of Non-Baker Hughes M&M Lien Claims have not, thus far, joined in the CDSA. Their rights will not be affected, as set forth below.

9. The debtor acknowledges that the liens encumbering the CFC Rig Collateral greatly exceed the value of the CFC Rig Collateral. The CFC Rig Collateral is not necessary for reorganization of the Debtor pursuant to chapter 11 of the Bankruptcy Code. The Debtor, however, is not waiving the redemption rights, nor is BPI acknowledging that the Debtor has redemption rights..

10. The transaction described in this Motion -- foreclosure upon the CFC Rig Collateral by BPI pursuant to the CFC Security Agreement and the settlement of issues between the Debtor and the Participating M&M Lien Claimants -- is in the best interest of the Debtor and the bankruptcy estate because it will result in the Debtor receiving all of the consideration set forth herein and saving administrative expenses which would otherwise be incurred. The savings include, but are not limited to, saving the money to be spent on a plugging and abandonment plan and the P & A work, saving marketing expenses in connection with the rig, saving the transactional costs associated with selling the rig and obtaining bankruptcy court approval (if that could be obtained over the objections of the secured creditors), obtaining plan support from key creditors as to particulars of the CDSA transaction, reducing CFC's claim against the estate by \$500,000, and other valuable consideration. While the Debtor is not happy that it is losing the drill rig, the Debtor will lose that rig anyway and without the benefits of this settlement the Debtor has negotiated if the Debtor does nothing.

B. Sale of Residual Rig Related Assets

11. The Residual Rig Related Assets are the assets ancillary to the rig upon which CFC does not have a lien. Such assets are identified on page 4 of **Exhibit A** (and the original purchase and sale agreement). It should be noted that there were extensive negotiations between the Debtor and BHO, CFC, and the other M&M lien creditors concerning what ancillary assets are subject to the mining liens of the secured creditors. BHO and the other mining lien creditors have made significant concessions in the negotiations in the Debtor's favor as to valuable rolling stock assets totaling approximately \$250,000 (if the mining lien creditors were to prevail and obtain an order that they did have liens in all of that machinery which was used in connection with the geothermal operations) which will not be included in the Residual Rig Related Assets.

12. Consistent with the original Motion, the Residual Rig Related Assets are to be sold to BHO or its assignee BPI pursuant to 11 U.S.C. § 363, free and clear of any liens, liabilities, interests, or encumbrances of any kind.

C. Non-Participating M&M Lien Claimants

13. BC Contractors, Inc. (“BC”), Centrifuge Services, LLC (“Centrifuge”), and Tecton Geologic, LLC (“Tecton”) have not thus far joined in the transactions contemplated by the CDSA. By Agreed Order, their secured claims are: BC at \$61,801, Centrifuge at \$67,323.21, and Tecton at \$136,041.81. (see D.E. 387).² This represents 4.86% of all the M&M liens against the Subject Assets. The CDSA provides that the liens of BC, Centrifuge and Tecton are preserved. Assuming the Non-Participating M&M Lien Claimants pursue a judicial foreclosure of their liens, the Agreed Order to which the Non-Participating M&M Lien Claimants are parties requires them to marshal and sell the Residual Rig Related Assets first before any sale of the CFC Rig Collateral. *See* Docket Entry 387 at paragraph 5. The Non-Participating M&M Lien Claimants will not receive a distribution of 50% of their secured claims from BHO like the Participating M&M Lien Claimants will. The Non-Participating M&M Lien Claimants are not receiving releases from the Debtor, will not be allowed to credit bid at the foreclosure sale, and are not participating in any other aspects or receiving any other benefits of the CDSA transactions. Their lien rights are preserved as set forth in the CDSA.

² The agreed order arose out of the fact that BC, Centrifuge and Tecton failed to file mining liens, failed to name the rig as being subject to their mechanics liens, and also suffered from the Court’s finding that M&M liens do not encumber the rig because it is not a fixture. BHO settled their dispute by agreeing to allow those M&M liens at 50%.

D. Plugging and Abandonment

14. The sale of the Residual Rig Related Assets, and indeed the entire transaction, is conditioned upon the Debtor's P&A Plan being approved by the AOGCC and any other applicable regulatory authority and the proper permits being issued to allow the Debtor to proceed with the plugging and abandonment of the G-1 well. A P&A Project Management Agreement and the Rig Utilization Agreement must be executed by NEA and the P&A Project Manager before the Closing Date scheduled by BPI. These agreements will obligate the Debtor and its Project Manager to conduct the plugging and abandonment operations in accordance with their terms but paid for by the money BHO contributes to the P&A Escrow under the transaction as well as the in-kind services BHO will provide at no cost to the Debtor. Alaska's Oil and Gas Regulation 20.25.105 provides:

(b) A well drilled onshore or from a fixed offshore platform must be abandoned before removal of the drill rig unless the well is completed as an oil, gas, or service well or is suspended, or unless well operations are shut down in accordance with 20 AAC 25.072. Each well drilled from a fixed offshore platform must be abandoned before the platform is removed or dismantled.

The Debtor argues that this regulation may require that the well be plugged and abandoned before the rig can be removed from the well site, even if lien creditors have completed foreclosure of their liens against the drill rig.

15. With the exception of weather or road conditions which make commencement impossible, if the Debtor fails to commence the plugging and abandonment operations within 15 days of the first barge into Naknek in 2013 containing the remainder of all equipment and material necessary for the P&A Operation, then BHO and BPI have the right to make a Substitute Equipment Election whereby they can provide an alternate drilling rig or coil tubing

unit and associated equipment capable of plugging and abandoning the subject well and remove the CFC Rig Collateral and Residual Rig Related Assets.

16. The Debtor, not BHO, is conducting the P&A operations and fulfilling the Debtor's regulatory obligations to the State. Under the CDSA, Baker Hughes does not assume and shall in no event be liable for any liabilities, debts or obligations of NEA, whether accrued, absolute, matured, contingent or otherwise, including, without limitation, (a) any foreign, federal, state, county, or local taxes, including, without limitation, excise taxes, or documentary transfer taxes, which in each case arise from the ownership of the Subject Assets on or prior to the Closing Date or from the consummation of the transactions contemplated by this Agreement; (b) any obligations or liabilities arising from any Environmental Laws or hazardous substances, or any other obligations or liabilities of any type relating to ownership or operation of any property either directly or indirectly by NEA or the ownership or operation of any business property or assets utilized by NEA arising prior to or on the Closing Date; (c) any obligations or liabilities whatsoever which may be imposed upon Baker Hughes as a successor to NEA either directly or indirectly or otherwise by any Environmental Laws; (d) any obligations or liabilities arising out of, relating to, or in connection with any action, suit, proceeding, or investigation pending or threatened against NEA or any of its shareholders, officers, directors, employees, or agents; (e) any labor or employment-related claims, obligations, or liabilities which accrue or arise from events occurring prior to the Closing Date, including, but not limited to, any claim of obligation or liability relating to wages, employee benefits, severance pay, workers' compensation, including insurance premiums, unemployment insurance, breach of employment contract, wrongful discharge, employment discrimination, or unfair labor practice; (f) any claims, obligations, or liabilities arising under or relating to any alleged violation of the Worker

Adjustment and Retraining Notification Act of 1998, as amended; (g) any liabilities for fees or expenses incident to the preparation of this Agreement or the consummation of the transactions contemplated hereby (including, without limitation, counsel or accountant's fees of NEA); or (h) trade payables or expenses, debt, contracts, agreements, leases or other obligations of NEA.

17. The Debtor filed the P&A Permit Application with the AOGCC on August 14, 2012, and is diligently monitoring its progress at the AOGCC. BHO has agreed that, as part of Closing, funds BHO places in the P&A Escrow Account will be used to reimburse the Debtor for the costs of hiring an engineer to prepare the P&A Plan and pursue the permit. All parties to the transaction desire to conclude the P&A Operations this fall. However, the CDSA recognizes there could be matters beyond the parties' control which prevent timely completion. Therefore, the Debtor's obligation is to cause the P&A Operations to be completed in accordance with the P&A Plan as soon as practicable, but in any event the P&A Operation shall be commenced no later than 15 days from the barge arrival date described above. Commencement cannot be delayed except for weather or road conditions which render commencement impossible.

18. The CDSA provides that the Debtor will not terminate the P&A Project Management Agreement or change the P&A Project Manager without Bankruptcy Court approval in advance. A Rig Utilization Agreement will allow the Debtor use of the rig for the P&A Operations despite the transfer to BHO. The same agreement obligates the Debtor to provide Debtor-owned materials and equipment toward completing the P&A Operations. The Debtor will (i) contribute materials and supplies (such as the cement at the geothermal site) that the Debtor currently owns to performance of the P&A Operations, and (ii) allow the use of equipment which it currently owns (other than the Subject Assets) in connection with

performance of the P&A Operations. The Debtor will not be entitled to any additional compensation for the contribution and usage provided for in this section

19. The Baker Hughes P&A Contribution consists of in-kind services and equipment, namely (i) the materials, equipment, and services within BHO's product line as of the date of the CDSA, identified by the parties to include in the P&A Plan, at (ii) the then current price for such services, equipment, and material within the subject market area as established by BHO and agreed upon by NEA.

E. Other Conditions to the Transaction

20. Other notable conditions to BHO's performance of the proposed transaction include that a Lift Stay Order in a form acceptable to BHO shall have been entered in the main case no later than September 14, 2012 and shall have become a Final Order fourteen days thereafter. Also, title to the Subject Assets must transfer from NEA pursuant to the foreclosure sale and the 363 sale pursuant to the CDSA on the Closing Date free and clear of all liens, claims, and encumbrances and the delivery of the Subject Assets on the Closing Date must be free and clear of all liens, claims, and encumbrances. The Debtor shall deliver all closing documents and must perform all of its obligations under the CDSA and related agreements. The representations and warranties of the Debtor must be true and correct when made and as of the Closing Date in all material respects. Documents of transfer satisfactory to BHO must be delivered by the Debtor. The Subject Assets must not be materially damaged or destroyed before the Closing Date. There must not be any litigation or injunction which would prohibit or restrain consummation of any of the actions to be taken under the transaction documents or court orders. The asset inventory will have to be verified.

21. The Debtor must deliver at Closing the following:

The Bill of Sale and Assignment duly executed by NEA;

The Rig Utilization Agreement duly executed by NEA and the P&A Project Manager;

The P&A Project Management Agreement duly executed by NEA and the P&A Project Manager;

The P&A Escrow Agreement duly executed by NEA;

Certificates of title to the applicable Subject Assets endorsed over to BHO;

The MSA duly executed by NEA and the P&A Project Manager;

The Storage and Surface Lease Agreement duly executed by NEA;

Any and all other affidavits, certificates, documents, or agreements required by any federal, state, or local governmental or administrative body or authority necessary to pass title to the Subject Assets to BHO, together with such operation manuals, engineering drawings and specifications, technical documentation and copies of certificates pertaining to the Subject Assets as NEA may possess. Some of these documents are not finalized and may not have been reviewed by all parties, but shall be completed by the hearing date.

22. The Debtor will deliver such other documents and instruments, and take such other actions, as may be necessary to carry out NEA's obligations under this Agreement that are required to be performed on or before the Closing Date.

23. BHO will deliver within five business days of BPI acquiring free and clear title to the Subject Assets and executed originals of all of the documents to be delivered by the Debtor at Closing:

The sum of \$500,712.73 shall be delivered by BHO to the P&A Escrow Agent for deposit into the P&A Escrow Account;

The Rig Utilization Agreement duly executed by BHO; and

The Storage and Surface Lease Agreement duly executed by BHO.

24. Then, within five (5) Business Days of the Closing and BPI acquiring free and clear title to the Subject Assets, BHO shall pay a sum equal to 50% of the stipulated allowed secured claim amount of Participating M&M Lien Claimants in accordance with the Secured Creditor Intercreditor Agreement.

F. Payments to Creditors

25. The secured creditors with liens against the rig or rig related assets shall be paid in accordance with a waterfall as specified in the CDSA. First, in accordance with the Secured Creditors Intercreditor Agreement, within 5 days of (i) the Baker Hughes Affiliate acquiring title to the CFC Rig Collateral pursuant to the foreclosure sale, and (ii) Baker Hughes acquiring title to the Residual Rig Related Assets pursuant to this Agreement, Baker Hughes would pay Participating M&M Lien Claimants 50% of their stipulated allowed secured claim amount. The Debtor reserves any setoff right it may have to withhold payment, if any, to Centrifuge Services, LLC due to the preference avoidance adversary pending between those parties.

26. Second, in accordance with the Secured Creditors Intercreditor Agreement, Baker Hughes would pay a sum up to 50% of the stipulated allowed secured amount of Participating M&M Lien Claimants pro rata out of 17% of the Net Subject Assets Resale Proceeds.

27. Third, in accordance with the CFC/Baker Hughes Intercreditor Agreement, a sum up to \$500,000 shall be paid to CFC out of 83% of Net Subject Assets Resale Proceeds, if any.

28. Fourth, in accordance with the CFC/Baker Hughes Intercreditor Agreement, Net Subject Assets Resale Proceeds, if any, in excess of the sum of the following: (i) the payments described in item Second above, plus (ii) the payment described in item Third above, plus (iii)

50% of the Adjusted Baker Hughes M&M Lien Claim Amount (i.e., the remaining 50% of the amount of the Baker Hughes M&M Lien Claim), plus (iv) the Baker Hughes P&A Contribution, shall be paid to CFC.

G. Settlement and Releases

29. The CDSA provides for mutual releases by and between BHO and the Debtor. Specifically, effective as of the Closing Date, the Baker Hughes Parties will forever release and discharge NEA, together with its officers, directors, employees, agents and attorneys, from all claims, obligations, liabilities, causes of action, demands, and controversies whatsoever (whether known or unknown, liquidated or unliquidated, absolute or contingent, acknowledged or disputed), including, but not limited to, those relating to or arising as a consequence of any of the following: (i) any services, materials, or equipment furnished to NEA by Baker Hughes Oilfield Operations, Inc., BJ Services Company U.S.A., or any other Baker Hughes Party, and/or (ii) any event, occurrence, omission, action, relationship, agreement or transaction which occurred prior to the Closing Date. The obligations of NEA under the CDSA, the Transaction Documents and the CFC Assigned Claim are not hereby released. In addition, the CFC Assigned Claim is not hereby released.

30. Effective as of the Closing Date, NEA and its bankruptcy estate will forever release and discharge the Participating M&M Lien Claimants, together with their officers, directors, employees, agents and attorneys, from all claims, obligations, liabilities, causes of action, demands, and controversies whatsoever (whether known or unknown, liquidated or unliquidated, absolute or contingent, acknowledged or disputed), including, but not limited to, those relating to or arising as a consequence of any of the following: (i) any services, materials, or equipment furnished to NEA, and/or (ii) any event, occurrence, omission, action, relationship,

agreement or transaction which occurred prior to the Closing Date. The Debtor will not release any potential avoidance actions under Section 544, 547 or 548 of the Bankruptcy Code against such persons. Although the Debtor is not obtaining general releases from the Participating Lien Creditors, such creditors are releasing any claims to liens against rolling stock and other personal property which are not included in Subject Assets.

31. In exchange for the contractual commitment by Baker Hughes to provide the Baker Hughes P&A Contribution, effective as of the Closing Date, NEA and its bankruptcy estate will forever release and discharge the Baker Hughes Parties, together with their officers, directors, employees, agents and attorneys, from all claims, obligations, liabilities, causes of action, demands, and controversies whatsoever (whether known or unknown, liquidated or unliquidated, absolute or contingent, acknowledged or disputed), including, but not limited to, those relating to or arising as a consequence of any of the following: (i) any services, materials, or equipment furnished to NEA by Baker Hughes Oilfield Operations, Inc., BJ Services Company U.S.A., or any other Baker Hughes Party, (ii) any event, occurrence, omission, action, relationship, lien filing, agreement or transaction which occurred prior to the Closing Date; (iii) all claims or potential claims set forth by the Debtor in D.E. 375; and/or (iv) the Judgment on Confession signed August 16, 2010, in Case No. 3AN-10-8750CI, styled *Baker Hughes Oilfield Operations, Inc., d/b/a Baker Hughes Christensen, Baker Drilling Fluids, Baker Atlas, Inteq, and Baker Oil Tools v. Naknek Electric Association, Inc.*, in the Superior Court for the State of Alaska, third Judicial District. The obligations of BHO under the CDSA will not be released.

32. Effective as of the Closing Date, NEA and its bankruptcy estate will forever release and discharge CFC, together with its officers, directors, employees, agents and attorneys, from all claims, obligations, liabilities, causes of action, demands, and controversies whatsoever

(whether known or unknown, liquidated or unliquidated, absolute or contingent, acknowledged or disputed), including, but not limited to, those relating to or arising as a consequence of any of the following: (i) any loans furnished to NEA, and/or (ii) any event, occurrence, omission, action, relationship, agreement or transaction which occurred prior to the Closing Date. The Debtor will not release the obligations of CFC under the CDSA or for any potential avoidance actions under Sections 544 or 547 of the Bankruptcy Code, if any.

H. Resale of the Subject Assets

33. It is contemplated that BPI will make every effort to resell the Subject assets acquired in the CDSA transactions in order to make the payments required under the waterfall and hopefully to realize enough value that the contingent payments could be made, though that is very uncertain. In this regard, the Debtor is aware of BPI's desire to resell the Subject Assets to a third party post-Closing. Cook Inlet Energy has expressed interest in acquiring the Assets for \$7,500,000 and has travelled to King Salmon to examine the rig and inventory. Cook Inlet Energy is being given notice of this Motion and the hearing and will also be given notice of the foreclosure sale. The Debtor has been advised of negotiations between BHO and Nordaq Energy, Inc., which has also traveled to King Salmon to examine the rig and inventory. Nordaq Energy is also being given notice of this Motion and the hearing and will also be given notice of the foreclosure sale. Due to (i) the shortness of time to complete the P&A Operations in time for the Subject Assets to be mobilized and barged to a new location prior to the winter freeze, (ii) the current uncertainty as to whether an acceptable definitive agreement with Nordaq Energy, Inc. can be reached and timely closed, (iii) the ongoing cost of preservation of the Subject Assets, and (iv) the assignment of Net Subject Assets Resale Proceeds provided for in this Agreement, the Debtor has determined that a transfer of the Subject Assets to BHO is in the best interest of the

bankruptcy estate. BHO shall provide NEA with a copy of any written proposal to purchase the Subject Assets which BHO intends to accept.

I. Representations, Warranties of the Debtor

34. To induce BHO to enter into the CDSA transactions, the Debtor has made representations and warranties. The Debtor has represented and warranted that at the September 4, 2012 hearing, conditioned upon resolution of remaining issues between them, it will have full authority to enter into and carry out the transactions, that its board of directors will have approved the transactions, and that entry into and performance by the Debtor will not contravene any agreement, statute, rule, regulation, or formation document. The Debtor further represents and warrants that the Debtor has good and marketable title to the Subject Assets and will deliver title to the Subject Assets free and clear of any and all liens, claims and encumbrances if the Motion is granted and the transaction proceeds. Further, that no claim, action, suit, or other proceeding is pending or, to the best of the Debtor's knowledge, has been threatened, against the Debtor or the Debtor's predecessor in interest to the Subject Assets with respect to their respective interest in and to the Subject Assets.

J. Representations, Warranties and Disclaimers of BHO

35. To induce the Debtor to enter into the CDSA transactions, BHO has made representations and warranties. These include that BHO has full authority to enter into the transactions and they will be valid and binding obligations of BHO, that no further consents or approvals are needed, that entry into and performance of the transactions will not contravene any agreement, statute, rule, regulation, or formation document. As for disclaimers, the Debtor acknowledges that the Baker Hughes P&A Contribution (in-kind) will only cover a portion of the total cost of the P&A Operations. Other costs will have to be paid out of the P&A Escrow. NEA

further acknowledges that although the P&A Operations are anticipated to be performed post-Closing, the Subject Assets (other than potentially casing) and their operations are not included within the Baker Hughes P&A Contribution. No duty, express or implied, shall be owed by Baker Hughes and/or BPI to any person or entity, including NEA, or NEA's creditors, to maximize the Net Subject Assets Resale Proceeds. The terms under which Baker Hughes and/or BPI resell the Subject Assets will be in their sole discretion. No warranty or representation, express or implied, is made by Baker Hughes as to the use, maintenance, preservation, and marketing of the Subject Assets subsequent to the Closing Date. The terms, conditions and disclaimers contained in the MSA (between BHO and the Debtor) are incorporated into the CDSA with respect to the Baker Hughes P&A Contribution. The P&A Plan and P&A Budget were not prepared by Baker Hughes. No representations, express or implied, are made by Baker Hughes as to either the P&A Plan or the P&A Budget. No representation, express or implied, is made by Baker Hughes as to the P&A Project Manager. No representation, express or implied, is made by Baker Hughes as to the condition of the Subject Assets as of the time of performance of the P&A Operations. The Subject Assets will be available for usage under the Rig Utilization Agreement on an "AS IS, WHERE IS, WITH ALL FAULTS BASIS." Baker Hughes has no express or implied duty to repair or replace any component of the Subject Assets which may be defective. If the P&A Operations cannot be completed in time for all Subject Assets and equipment used in connection with the P&A Operations to be barged to Anchorage before October 15, 2012, then the P&A Operations will be performed as soon as practicable in Spring 2013.

K. Covenants of the Debtor

36. As part of the transactions, the Debtor covenants to comply with the terms of the Transaction Documents, to cause the G-1 well to be plugged and abandoned in accordance with the P&A Plan, to maintain insurance policies in full force and effect before Closing, and after Closing if paid out of the P&A Escrow, and to preserve, maintain, and protect the Subject Assets. The Debtor further agrees to indemnify and hold harmless BHO and its successors and assigns from and against any and all claims, demands, losses, damages, liabilities, costs, expenses, and deficiencies (including attorneys' fees) caused by, arising out of, or resulting from, and to pay BHO any sum that BHO pays or becomes obligated to pay on account of, (a) the ownership of the Subject Assets by NEA prior to the Closing Date, (b) the use and/or operation of the Subject Assets prior to the Closing Date (but with the understanding that there is no indemnity which could be called upon to improve the Subject Assets from their current condition), (c) any breach or default in the performance by NEA of any covenant or agreement of NEA contained in this Agreement or in any other instrument delivered by or on behalf of NEA pursuant hereto, (d) any breach of a warranty or an inaccurate or erroneous representation made by NEA herein or in any other instrument delivered by or on behalf of NEA pursuant hereto, or (e) any and all actions, suits, proceedings, claims, demands or judgments incident to any of the foregoing. The Debtor must notify BHO of certain occurrences. The Debtor gives a further assurance clause in case additional documents or further actions need to be taken reasonably to carry out the transaction.

BENEFITS ANALYSIS

37. The costs of not proceeding with the transaction are many. The Debtor recognizes that it has an obligation to plug and abandon the well and that it will become much more difficult and expensive to satisfy that obligation once the rig has been moved away from the location or has been foreclosed upon. The Debtor believes that under applicable state regulations, quoted

above, it is unlikely that the rig can be moved (even after foreclosure) until the well has been plugged and abandoned, and the secured creditors recognize the uncertainty and litigation which could result from that. Delays in completing plug and abandonment of the well will be borne by the Debtor. Delays in completing the plug and abandonment of the well also may impede the confirmation of a plan of reorganization. The Debtor recognizes that the lien creditors have been patient thus far but desire to realize on their collateral. The lien creditors have the right to foreclose their liens and/or to have the rig sold free and clear of liens because the Debtor cannot offer them adequate protection. But the lien creditors also recognize that their sale of the drill rig may be delayed until the plug and abandonment of the well is completed or until litigation determines the regulatory question.

38. The Debtor has not been able to market the rig on its own and has not received any contract proposals for the rig. Even if the Debtor could hold off the secured creditors in an effort to market the rig, the Debtor, not BHO, would incur all the transactional costs associated with such an effort and likely a broker would have to be paid. There is no broker's commission to be paid in connection with the CDSA transaction.

39. The benefits of the transaction to the Debtor are the lien creditors' release of claims against rolling stock and other assets they assert liens in but which Debtor disputes, which could be worth more than \$250,000 to the Debtor, \$500,000 paid into a plug and abandonment escrow, which plug and abandonment is required by state conservation rules, services provided in-kind by Baker Hughes, a huge reduction in claims against the estate, elimination of a huge administrative expense (for plugging and abandonment) which the estate would otherwise have to incur, payment by BHO of insurance premiums as to the collateral and payment by BHO of the costs to prepare a P&A Plan and to obtain the permit therefore through the P&A Escrow, and

the discontinuation of approximately 50% of the \$20,000 per month in costs the estate continues to incur with respect to the rig, until it is plugged and abandoned.

40. If the transaction were not approved, the Debtor would have to amass enough cash to perform the plugging and abandonment on its own, which the Debtor estimates would take at least two years. The inability to pay this administrative expense would be a hindrance to plan confirmation.

41. A division of the geothermal assets is agreed upon in the transaction but will not be if the sale is not approved. As stated above, the Debtor is benefitted by this transaction because close to \$250,000 worth of rolling stock (vehicles, forklifts, etc.) are freed from disputed claims of mining lien creditors as a result of the negotiations.

42. If the sale transaction is approved, the Debtor will have the ability to propose a confirmable plan. If not, the Debtor would have to generate the funds necessary to plug and abandon the well and would have to litigate with the lien creditors concerning their foreclosure or sale rights and whether the rig can be removed from the geothermal site before the plug and abandonment operations are conducted. This issue has not been litigated previously to the Debtor's knowledge and the Debtor would prefer to avoid this litigation. BHO, CFC, and most of the other creditors with liens against the rig have agreed to support the provisions of a plan which fulfill this transaction, though reserving their rights as to other plan provisions.

43. The economics as to CFC have changed from the earlier version of the proposed sale, to the benefit of the Debtor, in the following manner. CFC is to be paid \$300,000 out of initial proceeds from the rig sale if certain contingencies are met, and CFC has a residual interest in further proceeds if additional contingencies are met. This was accomplished by adjusting the

BHO allowed claim downward by \$300,000. The economics of the original deal have been preserved for the other Participating M&M Lien Claimants, also to the benefit of the Debtor.

44. The CDSA also addresses concerns expressed by the other secured creditors with liens against the rig assets. The other Participating M&M Lien Claimants will still be paid as before; however, consistent with their comments, the one-year limitation on getting repaid out of rig re-sale proceeds has been removed. The Participating M&M Lien Claimants also desired for BHO not to have the ability to re-sell the rig for too low a price. They now have a right to object to and seek to enjoin any re-sale for a consideration of less than \$7,500,000.

MERITS OF SETTLEMENT AND TRANSACTION

45. The Debtor believes the terms of the proposed transfer of the rig are in the best interest of the Debtor and of the estate after consideration of the factors set forth in *Protective Committee for Independent Stockholders of TMT Trailer Ferry v. Anderson*, 390 U.S. 414 (1968). These factors include:

- a. The probability of success in the litigation;
- b. The difficulty in collecting any judgment which may be obtained;
- c. The complexity of the litigation involved, and the expense, inconvenience and delay necessarily attendant to it; and
- d. The interests of creditors and stockholders and a proper deference to their reasonable views of the settlement.

46. **Probability of Success in Litigation.** It is unclear what the outcome would be if the Debtor tried to block a motion to sell the rig or a motion to lift stay and foreclose on the rig by the lien creditors. AS 10.25.390 provides:

The board of directors of a cooperative may, without authorization by the members of the cooperative, authorize the execution and delivery of mortgages or deeds of trust of, or the pledging or encumbering of, the property, assets, rights, privileges, licenses, franchises and permits of the cooperative, whether acquired or to be acquired, and wherever situated, as well as the revenue therefrom, upon the terms and conditions the board of directors determines, to secure an indebtedness of the cooperative.

47. Given that the Debtor's board can encumber its property without a vote of the members then it must also be possible for the lien holder to foreclose its lien without a vote of the members. Otherwise, the statute would be a nullity. Likewise, the mining lien statute allows mining lien claimants to foreclose their liens and no exception is made for liens against assets owned by cooperatives.

48. The other hurdles to opposing action to foreclose or sell the rig assets by the lien creditors are many. The Debtor cannot provide adequate protection, cannot afford to fight over these issues, and cannot afford to market the rig itself. Even assuming the Debtor could prevail in such litigation despite the creditors' lien rights, the Debtor still would be faced with an inability to plug and abandon the well and to continue to pay for maintenance of the rig. The Debtor would also have to litigate with the lien creditors the issue whether they can remove the rig before the Debtor has performed its P&A obligations, an issue on which there is no precedent known to the Debtor.

49. With respect to the releases to be provided to BHO and the other lien creditors, BHO has provided the Debtor with its detailed factual contentions addressing any potential claim the Debtor believes it may have against BHO. Among other things, BHO has submitted documentation to support its position that the Debtor and its consultants, not BHO, decided when and how to pump Barite drilling mud into the well, that the Debtor and its consultants decided not to follow BHO's recommendations concerning use of loss circulation material ("LCM") to protect the formations in the well. BHO has also provided the Debtor with documentation that the Debtor and its consultants decided when and how to run various equipment in the well and that the drill bit and mill failures were not attributable to any defects in that equipment. Likewise, BHO maintains that the records on this well will prevent the Debtor from proving it suffered any damages as a result of any actions or inactions of BHO. The Debtor does not agree with all of BHO's factual contentions but acknowledges that it cannot assure its members that there is a likelihood that it would succeed in litigation with BHO over responsibility for the damage to well.

50. BHO has further pointed out the many contractual defenses it would assert to any claim by the Debtor. The Debtor executed a Master Service Agreement with BHO prior to the commencement of work and the Debtor also agreed to BHO's Terms and Conditions for all work. These agreements contain detailed and conspicuous limitations of warranty, limitations on damages, releases from liability, disclaimers, and indemnification of BHO by the Debtor. BHO has submitted authority to the Debtor that such limitations can be enforced. *See S.M. Wilson & Co. v. Smith International, Inc.*, 587 F.2d 1363, 1364-75 (9th Cir. 1978); *Ledgens, Inc. v. Kerr*, 91 P.3d 960, 963 (Alaska 2004); *Armco Steel Corp. v. Isaacson Structural Steel Co.*, 611 P.2d 507, 515-519 (AK 1980); *Idaho Power Co. v. Westinghouse Electric Corp.*, 596 F.2d 924, 925-

28 (9th Cir. 1979) (by ordering the goods buyer agreed to limitation of liability in seller's terms and conditions); *Ins. Co. of N. America v. NNR Aircargo Service (USA), Inc.*, 201 F.3d 1111, 1113-15 (9th Cir. 2000) (court enforced limitation of damages to \$50 contained in terms and conditions on reverse side of invoice).

51. Without the release of BHO's \$4,500,000 lien claim under the proposed transaction, the Debtor, even if it could prove some claim against BHO, would be subject to a very large offset. Thus, the Estate would not benefit unless a judgment was for in excess of \$4,500,000 plus attorneys' fees and costs. The releases are mutual and therefore also benefit the Debtor.

52. **Difficulty in Collecting Judgment.** This element of a 9019 analysis is only marginally applicable here. Certainly if the Debtor could finance the litigation and were successful in obtaining a judgment against BHO, it would be a collectible judgment. In another context, that of settling lien issues, even if the Debtor were able to block foreclosure or sale of the rig, the obligation to perform the plugging and abandonment of the well would remain. By litigating, the Debtor would merely postpone the inevitable plugging and abandonment and lose all of the value from the proposed transaction involving the rig, including the paid-for plugging and abandonment.

53. **Complexity of Issues, Expense and Delay.** Litigating with the lien claimants and the AOGC could be very expensive and time consuming. It also might require a change of forum under *Stern v. Marshall*. The delay would necessarily keep the rig out of service for another drilling season and also cause the debtor to be exposed to \$20,000 per month maintenance charges. The lien creditors have stated they will seek substantial adequate

protection from the Debtor, as well, a threat the Debtor discounts because it acknowledges that the lien creditors can foreclose their liens and takes the position that it is the Alaska regulation which would force the lien creditors to leave the rig on the well until after plug and abandonment is complete. If the lien creditors do foreclose their liens before P & A is completed they will have to negotiate with the Debtor to maintain and store the rig until it can be shipped into Cook Inlet or elsewhere, but the Debtor will have to continue to monitor the well, and the Debtor believes it is unclear which, Debtor or lien creditors who then own the rig, have responsibility for which expense. The proposed settlement eliminates some of these uncertainties.

54. With regard to the potential of making a claim against BHO, the Debtor developed its drilling program for this well based on input from several engineers, geothermal experts, and drilling experts hired by the Debtor. BHO followed orders from the Debtor and its consultants in connection with BHO's work on the well. Opinions can vary widely about drilling mud programs and equipment utilization, especially in an exploratory well, and the issues are highly technical. Trying to make a case would necessitate the hiring of multiple expert witnesses. In addition there are many fact witnesses, mostly located in other parts of the country and not employed by the Debtor. The Debtor would also have to prove that but for some negligence on the part of BHO, the well would have been a good geothermal well. Litigation of such a case will cost several hundreds of thousands of dollars, an expense the Debtor cannot afford.

55. Mutual releases plus all the other monetary and non-monetary consideration BHO is giving the Debtor if the rig sale transaction is approved, plus all the money and time the Debtor will save, justify the transactions sought to be approved. Tremendous estate resources as well as judicial resources will be saved. Failure to resolve these issues now may mean the loss of another season for getting the plugging work performed and the rig moved. It will reduce the

value of the rig to the estate. Even if the rig cannot be moved until a plug and abandonment operation is completed in April, 2013, the transaction is of benefit to the Debtor because it compromises claims, provides substantial monetary and non-monetary contribution to plug and abandonment, releases lien claims against certain of Debtor's rolling stock and provides sufficient certainty about how plug and abandonment will be paid for, to allow for the filing of a confirmable plan of reorganization.

56. **Interests of the Creditors and Members.** The Creditors will benefit greatly from the proposed settlement because it funds the plug and abandonment of the well (required by state conservation rules) which permits the construction of a plan which pays creditors sooner than the plan currently filed with the Court. It also results in a reduction of claims against the estate, avoidance of administrative expenses for the estate, avoidance of brokerage costs, willingness of a major vendor to provide plugging and abandonment services and equipment to the Debtor, avoidance of potential adequate protection claims, and ability to propose a plan.

SUMMARY

57. At the conclusion of the contemplated transactions, BPI will end up owning the rig assets free and clear of all liens, claims, and encumbrances. BHO will be obligated to provide all the P&A Obligations to the Debtor. BHO will also have obligations under the Intercreditor Agreements which will benefit the Participating M&M Lien Claimants, CFC, and the Debtor. Mutual releases will have been exchanged. The Debtor will have parted with a fully-encumbered asset but will have realized material and tangible benefits from that asset which will not be realized other than through this transaction.

WHEREFORE, PREMISES CONSIDERED, the Debtor respectfully prays that the Court grant the Motion, enter the order submitted herewith, and grant such other relief to which the Debtor is entitled.

DATED: August 29, 2012

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** Signed by Ross Spence with permission*

CERTIFICATE OF SERVICE

I certify that on August 29, 2012, a true and correct copy of the foregoing Third Supplement to Motion for Approval of Transaction was served upon the parties receiving ECF service:

Via Electronic Mailing:

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Donna Vukich, as General Manager of the Debtor, will also promptly mail this document to each member of the NEA Cooperative and thereafter will file an affidavit regarding such mailing.

/s/ Erik LeRoy