

FIRST AMENDED DISCLOSURE STATEMENT FOR PLAN OF REORGANIZATION

INFORMATION CONCERNING THE DEBTOR AND THE
PLAN OF REORGANIZATION

NAKNEK ELECTRIC ASSOCIATION, INC.

Debtor in Chapter 11 Case
No. 10-00824-DMD
United States Bankruptcy Court
District of Alaska

Honorable Donald MacDonald IV

June 28,2012

ERIK LeROY, P.C.
500 L St., Ste 302
Anchorage, Alaska 99501
Tel. (907) 277-2006
Fax. (907) 277-2243
Attorney for the Debtor

This Disclosure Statement contains information concerning the Debtor and the Plan of Reorganization proposed by the Debtor. The Disclosure Statement and the proposed Plan are being distributed to you, pursuant to 11 U.S.C. § 1125, to enable you to make an informed judgment before voting to accept or reject the Plan. The Bankruptcy Court has reviewed this Disclosure Statement and has approved it as containing adequate information. The approval of the Disclosure Statement, however, does not constitute a recommendation or endorsement of the Plan by the Bankruptcy Court.

TABLE OF CONTENTS

I. INTRODUCTION. 1

 A. General Information. 1

 B. Source of Information. 2

 C. Representations. 2

II. DEFINITIONS. 2

III. ORGANIZATIONAL AND OPERATIONAL BACKGROUND. 2

 A. Organization. 2

 B. Operations. 2

 C. Debtor’s Utility Rates History. 4

 D. Debtor’s Statement of Factors Leading to Petition. 4

IV. POST-PETITION EVENTS. 5

 A. Initial Orders. 5

V. ASSETS AND LIABILITIES. 7

 A. Assets. 7

 1. Diesel Plant. 7

 2. Drilling Rig. 8

 3. Geothermal Property. 8

 4. Additional Personal Property. 9

 5. Construction Work in Progress. 9

 B. Administrative Expenses. 9

 C. Discussion of Significant Claims and Interests. 9

 D. Claim summary. 9

VI. LITIGATION AND DISPUTED CLAIMS. 9

VII. DESCRIPTION OF PLAN. 11

 A. Summary. 11

 B. Financial Projections. 14

VIII. CONFIRMATION.	15
A. <u>Bests Interests of Creditors / Liquidation Analysis.</u>	15
B. <u>Fair and Equitable / Cramdown.</u>	15
C. <u>Risk Factors.</u>	16
D. <u>Voting.</u>	16
IX. AFTER CONFIRMATION.	17
A. <u>Tax Consequences.</u>	17
B. <u>Discharge.</u>	18
C. <u>Modification of the Plan.</u>	18
D. <u>Final Decree.</u>	18
X. CONCLUSION.	18

I. INTRODUCTION

A. General Information.

The Debtor is an electric utility cooperative serving approximately 700 members and 1,100 meters in the vicinity of the cities of King Salmon and Naknek in Western Alaska. It makes its electricity by burning diesel fuel in its generators. Between 2005 and 2008 the price of diesel fuel delivered in Naknek increased from about \$1.20 per gallon to more than \$4.00 per gallon. During the same period, there was a 6 percent decrease in residential load due migration out of the region because of the high cost of living. In response, the Debtor's board of directors decided to pursue a geothermal power solution to its rapidly increasing cost of power generation.

In 2008 through late 2009 the Debtor incurred substantial debt in the process of drilling and attempting to develop a geothermal well. In the process of development of this well the Debtor did not receive the federal and state grants it had anticipated. Unanticipated state regulatory decisions added to the cost of the development. The drilling fluid utilized in the drilling of the well has damaged the flow characteristics of the well and prevented the Debtor from proving the viability of its project. By the summer of 2010 a number of the Debtor's vendors had filed statutory liens against its geothermal assets. In addition, several of the Debtor's largest creditors obtained substantial judgments against it. To retain control of its assets, the Debtor filed its chapter 11 petition on September 29, 2010.

Since its September 29, 2010 petition date, the Debtor has attempted to confirm that its geothermal resource has the temperature and flow characteristics to support a geothermal power plant. The Debtor's experts determined that the Debtor was not going to be able to utilize the geothermal well which was drilled in 2009-2010 to confirm its resource. Consequently, the Debtor investigated obtaining the necessary financing to pay for the required cost-share to drill a sidetrack or second well. The Debtor is the beneficiary of a \$2.4 million Department of Energy grant to drill such a well, if it can pay for 20% of the cost of that well. It has investigated finding the financing to pay for this 20% match so it can utilize the \$2.4 million DOE grant. That pathway has proven difficult. Even if the Debtor is able to drill a new well and confirm its resource, the development of a geothermal power resource will require the development of several additional wells, and the construction of a power plant and distribution lines. It was the Debtor's plan to obtain financing to pay for all of those improvements. The difficulty the Debtor has encountered pursuing the first step of this plan – the drilling of a confirmation well – leads the Debtor to here propose a plan of reorganization in which it plugs and abandons the geothermal well, retains the geothermal property, now burdened with environmental monitoring responsibilities, and continue to generate electricity with its diesel generators. After the costs of plug and abandonment are met, the Debtor will dedicate a portion of the utility rates it recovers from its member to pay its unsecured creditors dividends on their claims.

The Plan of Reorganization which is attached as Appendix 1 to this Disclosure Statement, proposes that the Debtor will pay Class 11, unsecured creditors, \$3 million over six years beginning in August, 2014. Based upon the current claims filed in this case, this will pay unsecured creditors a dividend of about \$.08 on each dollar of claim.

The Debtor requests that you complete and return the enclosed ballot with your vote accepting its proposed Plan of Reorganization.

On _____, the Court approved the distribution of this Disclosure Statement to holders of claims or interests against or in the Debtor or its property. The Court's approval of this Disclosure Statement does not represent an endorsement or recommendation of the Plan.

THE FINANCIAL INFORMATION IN THIS DISCLOSURE STATEMENT HAS NOT BEEN AUDITED. THE PLAN PROPONENTS BELIEVE THE INFORMATION IS ACCURATE TO THE BEST OF THEIR KNOWLEDGE, AND HAVE MADE SUBSTANTIAL EFFORT TO PRESENT THE INFORMATION ACCURATELY AND FAIRLY, BUT NO FURTHER REPRESENTATION OR WARRANTY REGARDING THE ACCURACY OF SUCH INFORMATION MAY BE MADE.

B. Source of Information.

Information presented in this Disclosure Statement has generally been obtained from records of the Debtor.

C. Representations.

The only representations concerning the Plan and the Debtor, which are authorized by the Debtor or the Court order approving this Disclosure Statement, are the representations contained in this Disclosure Statement. Creditors and parties in interest may not rely on any other representation or inducement in determining whether to accept or reject the Plan, and should report any such unauthorized representations or inducements to the Debtor or its counsel for appropriate action.

II. DEFINITIONS

Capitalized terms used in this Disclosure Statement shall have the meanings stated in the Plan of Reorganization.

III. ORGANIZATIONAL AND OPERATIONAL BACKGROUND

A. Organization.

Naknek Electric Association, Inc. was incorporated in 1949 and operates under AS 10.25.010 et. seq., the Alaska Electric and Telephone Cooperative Act. The Debtor is owned by its members. AS 10.25.080. It is operated on a nonprofit basis "for the mutual benefit of its members and patrons". AS 10.25.380. Members of the cooperative are not "liable or responsible for any debts of the cooperative and the property of the members is not subject to execution therefore." AS 10.25.410. The Debtor is managed by the uncompensated board of directors and a general manager described in the following table.

Name	Title	Annual Compensation
Tom Deck	Director & Officer	\$0
Dale Peters	Director & Officer	\$0
Stephen Jones	Director & Officer	\$0
Pete Hill	Director	\$0
Nanci Morris Lyons	Director	\$0
George Wilson	Director	\$0
Jason Lazore	Director	\$0
Donna Vukich	General Manager	\$151,595

B. Operations.

1. Diesel History

King Salmon and Naknek are located on the shore of Bristol Bay. Bristol Bay is the site of one of the largest commercial salmon fisheries in the world. Between June and August more than 30 million sockeye salmon return

to rivers that run into Bristol Bay. There are now eight land based processing plants, and a number of small scale processing operations, located in the Debtor's service area.

The Debtor began distributing electricity in 1960. The Debtor started with three diesel generators and in the 1970's added four more diesel generators. In the 1980's it added three more diesel engines. In 1980 the Debtor entered into a wholesale power contract with the U.S. Air Force which was maintaining a forward air base in King Salmon from which it flew fighter interceptors in support of containment of Russian flights probing U.S. interests. (The Air Force base in King Salmon converted to a "warm" status in 1995, but still purchases approximately 3,000,000 kwh of wholesale electricity annually from the Debtor.) In the 1990's the fish processors began converting from canning operations to fresh fish freezing operations, which requires a larger electrical load.

In the 1990's the Debtor began exploring alternatives to diesel power generation. It explored wind power, methane from shallow coal beds and geothermal power. The University of Alaska Fairbanks conducted geothermal testing in Katmai National Park in the mid-1990's.

In 2005 the Debtor paid approximately \$1.20 per gallon for diesel fuel. In 2008 the Debtor paid more than \$4.00 per gallon for diesel fuel. (In 2011 the Debtor paid more than \$3.50 per gallon for diesel fuel.)

In 2003, the Debtor first utilized a line of credit from National Rural Utilities Cooperative Finance Corporation to finance a portion of its diesel fuel purchase, the price of diesel began to climb above \$.70 per gallon. In 2006 it borrowed \$4.5 million to purchase fuel. In 2008 it borrowed \$6 million to purchase fuel.

2. Geothermal Well

From the late 1990's into 2008 the Debtor had explored geothermal sources in its service area. It had conducted seismic testing and in 2007 it drilled two 400 foot wells with available water well drilling tools. The high cost of diesel fuel in 2008 led the Debtor's board of directors to direct management to aggressively pursue a geothermal power solution to the high cost of diesel power generation. Although it was anticipated that the initial costs of development would be very high, once a geothermal power system is producing electricity, the ongoing cost of power generation would be lower than the cost of the Debtor's diesel power generation operation.

In 2008 the Debtor acquired a 120 acre native allotment and, in mid-2009, began building a road into that location. In 2009 the Debtor obtained from National Rural Utilities Cooperative Finance Corporation, ("CFC") a \$15 million line of credit to be used in the exploration and development of the geothermal energy source. In May of 2009 the Debtor acquired a drill rig for \$8.5 million. The Debtor made approximately \$3 million of improvements to the drill rig. CFC loaned the Debtor \$8.5 million, secured by the drill rig and reduced the Debtor's \$15 million line of credit to \$10 million. The drill rig arrived in King Salmon by barge in July, 2009.

In April 2009, the Debtor submitted an environmental report to the Department of Energy ("DOE") seeking an exclusion from the requirement to file an Environmental Assessment based on the fact that the Debtor was obtaining environmental permits from the State of Alaska. DOE's representative suggested that the Debtor's permitting activity with the State of Alaska would qualify it for a "categorical exclusion" from the requirement that it submit an Environmental Assessment. The Debtor commenced work on its road and began drilling, but in October, 2009 was told by DOE that it must complete an Environmental Assessment and that no work associated with the drilling of Well 1 would be eligible for any DOE grants.

On August 13, 2009, three days before drilling of the exploratory well was scheduled to begin, the Alaska Oil and Gas Commission informed the Debtor that its exploratory well would be regulated as an oil & gas well instead of as a water well. This meant, among other things, that the Debtor would need more robust blowout preventers, and would have to use heavier drilling fluids than it had intended.

The Debtor began drilling Well 1 on August 16, 2009. In December 2009, at 11,218 feet, a drilling bit broke. After one attempt to retrieve the broken bit, the Debtor, on January 8, 2010, began a sidetrack well which failed after

about one week. The second sidetrack was commenced on about January 21, 2010, and was successfully drilled to 11,387 feet.

On the advice of one of its vendors, the Debtor utilized Barite as a drilling mud, which has proven to be very difficult to remove from the well. On about April 16, 2010, the Debtor set a well liner and began flow testing the well. The well refused to flow under its own pressure. The Debtor utilized air compressors to assist with flow, without significant success. The Debtor's experts have concluded that the Barite drilling mud is clogging the well and preventing reliable testing of the well for geothermal power generation capability. (More than 32,000 barrels of Barite were inserted into the well. Less than 3,500 barrels of used Barite have been recovered from the well.)

C. Debtor's rate history over last 10 years.

The members of the Debtor are billed for their electric usage based upon whether they are residential users, commercial single phase user, commercial three phase user, large power user, or wholesale users. The U.S. Air Force is the only wholesale user. Since 2001 the Debtor's base rates have varied between \$.165 per kwh and \$.27 per kwh. In 2009, rates were increased by \$.09 per kwh to help offset the costs of the geothermal well. The residential base rate since 2009 has been \$.27 per kwh. For the same period, commercial rates varied depending on usage between \$.255 and \$.27 per kwh.

In addition to these base rates the Debtor charges a cost of power adjustment designed to pay for fluctuations in the cost of diesel fuel. Since 2001 the cost of power adjustment has varied from \$.0143 per kwh to \$.2098 per kwh, which is what it is now. The Debtor's 2011 overall rates for commercial and residential customers, (which does not including the Air Force which pays a wholesale rate) including cost of power adjustment, varied between \$.4648 per kwh and \$.4955 per kwh. The Debtor's 2012 overall rates for commercial and residential customers, including cost of power adjustment, has, so far, varied between \$.4955 and \$.5225 per kwh.

For the reasons explained in Debtor's discussion of the risk factors associated with this Plan at Article VIII of this Disclosure Statement, it is important that the Debtor minimize rate increases to retain large power customers. The Debtor, however, does project that some rate increases will be necessary to fund its Plan (see discussion in Article VII of this Disclosure Statement.)

D. Debtor's Statement of Factors Leading to Petition.

The costs associated with the Debtor's geothermal exploratory well were substantially greater than had been anticipated. By the September 29, 2010 petition date, the Debtor had incurred approximately \$40 million of debt that was in one way or another associated with the geothermal project. Approximately \$47 million of claims have been filed in this case. Approximately \$7 million of those claims are either disputed or associated solely with the Debtor's diesel power generation activity.

The Debtor anticipated receiving substantially more grant funding of its project than it received. In 2008 and 2009 the Debtor obtained commitments from federal agencies for approximately \$18 million of grants or awards, but has received less than \$3 million.

Beginning in early 2010 the Debtor's geothermal vendors began recording statutory liens for unpaid goods and services. By its September 29, 2010 petition date, nine statutory liens had been recorded to secure claims in excess of \$7 million. In addition, in the summer of 2010, the Debtor had fallen behind in payments to its banks and at least one of its bank loans had matured. By August, 2010, the Debtor had been named as the defendant in five separate collection lawsuits.

The Debtor had hoped that its 2010 geothermal drilling program would establish the productivity of its geothermal asset. But, in July and August of 2010, as it began testing its well for temperature and pressure, the Debtor learned that drilling fluids it had used were difficult to remove from the well structure and were inhibiting the well flow. With its well unproven, the Debtor could not obtain additional grants or other funding with which to bring current obligations associated with the drilling of the geothermal well. To stop the various actions which had been

filed against it and to preserve its ability to avoid certain non-consensual liens against its assets, the Debtor filed its Chapter 11 petition on September 29, 2010.

IV. POST-PETITION EVENTS

The Debtor has continued to operate its diesel power generation plant since its September 29, 2010 petition date and has continued to supply electricity to its members, without interruption, as it supplied such electricity pre-petition. While in this Chapter 11, the Debtor acquired tools which it believed would permit it to clean its geothermal well and confirm that the temperature and flow characteristics of this well would support its geothermal plan. The Debtor has not been able to confirm viability of the geothermal well. The Debtor is the beneficiary of a \$2.4 million Department of Energy grant to drill a confirmation well, if it can pay for 20% of the cost of that well. It has investigated and continues to investigate finding the financing to pay for this 20% match so it can utilize the \$2.4 million DOE grant, but this effort, has, so far, been unsuccessful. Consequently, the Debtor will propose a Plan which plugs and abandons the geothermal well, while it continues to generate electricity with its diesel generators.

The Debtor experienced lower than projected utility usage in the summer of 2011. In 2011 the Debtor sold about 1.5 million kWh of electricity less than in 2010. The Debtor burned about 840,000 fewer gallons of fuel than it burned in 2010. About 70% of this drop in fuel usage and sales was attributable to a loss of a processor customer in the summer of 2011. The rest was due to commercial and residential efforts to reduce utility expenses.

A. Initial Orders

1. Professionals.

Shortly following the petition date the Debtor sought, and subsequently obtained Court approval for Debtor's employment of (i) Erik LeRoy, P.C. as debtor's counsel (DE 58), (ii) Kempel Huffman & Ellis as general counsel, (DE 59) and (iii) Tom Lovas and Energy & Resource Economics, for economic analysis in support of applications for financial assistance (DE 60). Subsequently, the Debtor has also obtained Court approval to employ (i) Mikunda Cottrell to prepare the Debtor's annual financial statements (DE 172), and (ii) Alan Meyers, a Texas attorney, to assist with a Texas contract claim (DE 221). Two committees have been constituted by the U.S. Trustee's Office. An unsecured creditor's committee was appointed. A committee to representing the members of the Debtor was appointed. The member committee hired David Bundy as counsel who obtained court authorization for his appointment. (DE 122) The unsecured creditors committee is comprised, to a significant degree, of attorneys for creditors, and it has not hired counsel.

2. Cash Collateral.

On the Petition Date the Debtor's accounts receivable and diesel assets were encumbered by security interests in favor of Rural Utilities Service. A preliminary Order was entered permitting use of cash collateral (DE 30) and subsequent orders extending that permitted use of cash collateral through December 31, 2012 have been entered. (DE's 84, 139, 216, 234, 303, 339)

3. Post-Petition Financing

a. Debtor in Possession loan.

On December 7, 2010 (DE 133) the Debtor obtained an order authorizing it to borrow \$1.5 million with which to purchase and operate a large air compressor to attempt to clean the geothermal well of the drilling fluids that the Debtor's experts believe are preventing it from obtaining accurate readings of the well's temperature and pressure. The Debtor did purchase and operate this machinery but the well continues to stubbornly resist cleaning. This loan amortizes over 36 months beginning June, 2011 and will be paid off in June, 2013. To secure this loan, CFC was granted a lien against the Debtor's diesel assets senior to all liens or claims, other than the liens and mortgage of

RUS. Prior to its Petition Date, the Debtor gave its members notice of a proposed amendment to its Articles of Incorporation which raised the Debtor's ability to incur debt over the \$25 million limit then applicable. The Debtor had inadvertently exceeded that limit when the Geothermal Project encountered difficulties. Approval of that proposed amendment was a necessary pre-condition to the Bankruptcy Court's approval of this Debtor in Possession loan. The amendment was approved by a vote of 214 in favor to 75 opposed (DE 124).

b. Fuel Loans.

On May 2, 2011 (DE 233) the Debtor obtained an order authorizing it to borrow from CFC up to \$ 6 million with which to purchase its June 2011 through June 2012 diesel fuel. Subsequently the Debtor purchased and received 1.6 million gallons of diesel fuel at a cost of more than \$5.5 million. As of June 1, 2012 the Debtor's remaining obligation on this loan had been reduced to approximately \$2 million. On May 17, 2012 (DE 348) the Debtor obtained an order authorizing it to borrow from CFC up to \$ 6 million with which to purchase its June 2012 through June 2013 diesel fuel. Subsequently the Debtor purchased and has received 904,000 gallons of diesel fuel at a cost of more than \$3.3 million. The Debtor held about 500,000 gallons of fuel from the 2011 delivery in its tanks at the time of the 2012 delivery. As of June 21, 2012, with the remainder of the 2011 fuel loan rolled into the 2012 fuel loan, the Debtor owed CFC approximately \$5 million on the 2012 fuel loan. Depending upon June and July, 2012 usage, the Debtor will acquire additional fuel in August, 2012. The Debtor will repay this loan sometime in the summer of 2013 and, if a Plan has not been confirmed earlier, obtain authority from the Bankruptcy Court to borrow funds to purchase its 2013-2014 fuel requirements sometime in the Spring of 2013. This will be a recurring annual borrowing event that will be repaid each year when the Debtor collects its rates from its members as it burns the fuel purchased. This loan is secured by a lien against the Debtor's diesel assets, senior to the lien and mortgage of RUS.

4. Bankruptcy litigation

a. NEA v. CoBank & Baker Hughes 10-90027

The Debtor filed an adversary action in the Bankruptcy Court seeking to avoid the judicial liens that had been recorded against its diesel assets by Baker Hughes and CoBank. On January 1, 2011 a Consent Judgment was entered in this adversary action avoiding those liens.

b. Baker Hughes v. NEA et. al. 11-90007

Baker Hughes filed a complaint in the Bankruptcy Court seeking to determine the priority of statutory liens against the Debtor's drill rig, geothermal equipment and geothermal site. Liens of more than \$10 million were filed against these assets. CFC and several other lien claimants filed counterclaims. On March 21, 2012 the Bankruptcy Court entered an Order and Memorandum on Cross Motions for Summary Judgment determining that the mining and mineral liens took priority over CFC's Uniform Commercial Code liens against the drill rig and that the mechanic liens did not encumber the drill rig. This decision facilitated settlement discussions between the lien claimants which has resulted in an Agreed Order Approving Motion to Compromise Controversy (DE) which the Debtor anticipated will be filed in early July, 2012. The Debtor believes this order will resolve all issues remaining in this adversary action other than whether the mineral and mechanics liens extend to the Debtor's non-certificated rolling stock equipment which was not used exclusively at the geothermal site. The Debtor values this equipment at approximately \$200,000 and this issue is resolved by the Plan which reverts this equipment in the Reorganized Debtor free and clear of all liens or other claims.

5. State and Federal Court litigation

a. NEA v. Bristol Bay Borough

NEA filed a complaint in Superior Court in Anchorage seeking judgment against Bristol Bay Borough for damages of more than \$500,000 which the Debtor alleges were caused by the Borough's agent when a portion of the drill rig known as the top drive was unloaded from the barge in 2009. The Bankruptcy Court approved a

\$175,000 settlement of this claim. The proceeds of this settlement were used to pay ongoing expenses of operation.

b. Premier v. NEA and GBR

Premier Equipment filed a complaint in federal district court in Lafayette, Louisiana, alleging that GBR, a vendor of the Debtor, and the Debtor, owed it more than \$2 million for the use of drilling equipment by the Debtor. Premier and GBR settled their claims in this action and GBR filed an amended proof of claim in this bankruptcy asserting a claim for \$909,000 which it maintains is a lien against the drill rig. The Debtor objected to this claim and Baker Hughes joined in the Debtor's objection. Subsequently, GBR, Baker Hughes and the Debtor have agreed to allow GBR a claim of \$450,000, which treatment is described in the Agreed Order Approving Motion for Compromise (DE).

6. Administrative Expenses

a. Professionals

Four orders have been entered approving fee applications through September 30, 2011 (DE's 164, 241, 261, 293) totaling \$194,789. Additional fees and costs, which as of June 28, 2012 are estimated to be approximately \$175,000 have been incurred since October 1, 2011, but no additional fee applications have been filed because the Debtor has not had the funds necessary to pay the last approved administrative expenses (DE's 293 for \$46,786.95 and DE 315 for \$17,438.12).

b. Arctic Drilling

Arctic Drilling filed a Motion seeking payment of approximately \$67,000 of post-petition charges for repairs relating to alleged usage of its equipment. The Debtor has opposed this Motion; Arctic Drilling does have a valid pre-petition claim in this approximate amount.

7. Other Orders

a. Official Service List

An order was entered at DE 172 approving a shortened Official Service List for noticing of matters other than Disclosure Statement and Plan issues.

b. Acquisition of Baker Hughes' nine silos

Baker Hughes owned nine metal silos located on the geothermal site, seven of which are filled with dry powder cement which the Debtor needed to redrill the geothermal well or to plug and abandon the geothermal well. The Debtor obtained Court approval to purchase these silos from Baker Hughes for \$112,500 and this payment was made in February, 2012.

V. ASSETS AND LIABILITIES

A. Assets.

1. Diesel Plant & non-geothermal assets.

The Debtor owns three and one half acres of land in Naknek, Alaska, on which is located an approximately 15,000 square foot building containing 10 diesel generators and the Debtor's offices. There is a separate metal building located on this property containing the Debtor's distribution assets, including transformers, switches and line. There are also six diesel fuel tanks located on the property with total capacity of 2,160,000 gallons. The Debtor owns 91 miles of above and below ground power lines, poles and appurtenant equipment.

As of May 31, 2012, the fuel tanks contained more than 1.3 million gallons of diesel fuel valued at roughly \$5 million, but encumbered by the fuel loan with a current balance equal to the approximate value of the fuel.

The Debtor owns a small parcel (less than one acre) with a small building in South Naknek located across the Naknek River (there is no bridge). The Debtor owns a small house in Naknek which has been vacant since before the petition date.

All but one piece of the rolling stock the Debtor owns are stored at the diesel facilities and used for both diesel and geothermal purposes. A small Volvo loader is stored at the geothermal site and is dedicated to that project. This piece is subject to some or all of the statutory liens.

Although it is located at the geothermal site, and is dedicated to that project, the air booster that the Debtor acquired with the Debtor in Possession loan, is considered a non-geothermal asset, because none of the pre-petition statutory liens attach to it.

The Debtor's May 31, 2012 financial statement values the Debtor's diesel power generation property at \$5,736,152 net of depreciation. A copy of this financial statement and the Debtor's analysis of its equity in the assets described in the financial statement is attached as Appendix 1. These assets are encumbered by the RUS loan, the CFC Debtor in Possession loan, and the cost of plug and abandonment. Before the cost of plug and abandonment, the Debtor's net equity is about \$2,829,504. A plug and abandonment budget is found in Appendix 1. After the cost of plug and abandonment he Debtor's net equity in its assets is about \$2,029,504.

2. Drill Rig.

The rig is a National 1320 oil and gas drill rig the Debtor bought in Eastern Washington in 2009 for \$8.5 million. The Debtor subsequently made approximately \$3 million of winterization and other improvements to the drill rig. The Debtor's financial statement values the drill rig at approximately \$11 million. Baker Hughes has obtained an appraisal of the drill rig valuing it at less than \$4 million. The Debtor is trying to sell or lease the drill rig. Sale of the rig has proven difficult. But there is significant interest in lease of the rig. The Debtor would like to use the Drill Rig to plug and abandon the geothermal well, but does not have the financing available to pay the estimated cost of plug and abandonment. The Debtor has received a preliminary estimate of approximately \$804,000 to plug and abandon the well.

3. Geothermal Property.

The Debtor purchased a 120 acre native allotment approximately 17 miles from King Salmon, in January, 2008 for \$120,000. Utilizing a conditional easement, the Debtor constructed a 1.4 mile road on land owned by the native village corporation, Paug-Vik, Inc. The easement, by its terms, reverts to Paug-Vik if the geothermal project is not developed. From the Paug-Vik conditional easement the Debtor constructed a .4 mile road to the geothermal pad. Alternative access to the geothermal pad is provided by the Pike Ridge Trail, an unimproved four wheeler track which passes within 60 feet of the geothermal property line. There is a 60 foot easement from this trail to the geothermal pad which is available access even if the geothermal pad is not developed.

The pad is about 430 feet by 300 feet. There is a 250,000 gallon fresh water storage pond with an impermeable liner on the east side of the pad. On the west side of the pad is a 250,000 gallon storage pond with impermeable liner containing about 200,000 gallons of used drilling fluid. Off of the pad on the west side is a 1 million gallon storage pond with an impermeable liner containing water removed from the well. On the northwest corner of the property, off the pad, is an inert waste certificated storage area approximately 200 feet by 200 feet containing bags of material, including cutting and other dried waste, recovered from the well. This area is similar to a small landfill. There are three environmental monitoring wells of 80 to 100 feet deep located just off the pad.

The Debtor spent \$887,866.79 on improvements to the geothermal real property including development of roads, pad, staging area inert waste monofil and settling ponds.

This property is included in Construction Work in Progress ("CWIP") on the Debtor's financial statement. CWIP is discussed below. The real property is also encumbered by statutory liens. The Debtor does not believe this property has any value, and may be a liability because it is burdened with state environmental monitoring expenses.

The Plan provides that the Geothermal Real Property will revert in the Reorganized Debtor, free and clear of all liens or other claims on the Effective Date. The Reorganized Debtor will record a mortgage in favor of the Classes 2 through 9 Allowed Secured Claims which mortgage expires Six (6) after the Effective Date. Any of Classes 2 through 9 may reconvey their interests in this mortgage and participate, to the extent of an remaining Allowed Secured Claim in Class 11, Unsecured. Class 11 Unsecured will receive a mortgage against the Geothermal Property which also expires in six (6) years. The purpose of these security interests is to give Debtor's creditors an interest in the geothermal project should it be revived within six years.

4. Additional Personal Property.

a. Geothermal

There is one trailer with two sleep quarters located on the geothermal pad. There is a second trailer with office space and break room. There are 6 to 7 20 to 40 foot containers, two of which contain a mechanic shop and a welding shop. There is also a small 2009 Volvo 1412 loader dedicated to the geothermal site. Although the original Schedule B filed in this case listed a number of rolling stock assets associated with the geothermal project, only the 2009 Volvo 1412 loader is stored at the geothermal pad and dedicated to this project. That loader is valued at approximately \$100,000 and may be subject to the statutory liens. The Debtor's inventory of casing and material, located on the geothermal pad, was purchased for about \$2.5 million.

5. Construction Work in Progress.

The Debtor's financial statements contains a line item in the amount of \$31.4 million described as Construction Work in Progress covering the Debtor's expenditures associated with the geothermal project. Some assets are included in this amount. Because the Debtor believes that its geothermal assets are over-encumbered by the totality of liens filed against those assets it does not believe there is any net value to the Debtor in Construction Work in Progress.

B. Administrative Expenses.

Administrative expenses associated with the bankruptcy case, to be paid under the Plan, cannot be estimated with precision. At present, the Debtor estimates that unpaid Administrative Expense Claims could be in the range of \$175,000 by the Confirmation Date.

C. Discussion of Significant Claims and Interests

1. Rural Utilities Service Mortgage & Lien.

The Debtor has ten outstanding loans owned by RUS, secured by the Debtor's diesel assets, totaling \$2,694,516 as of May 31, 2012. These loans were used to purchase or upgrade equipment. The most recent loan was issued in 2002 for a new fuel tank and tank farm upgrades. These loans amortize at various dates between 2013 and 2040. RUS's liens were subordinated to the post-petition super priority lien granted CFC for the fuel loan.

3. CFC Fuel Liens

CFC loaned the Debtor approximately \$5.5 million to purchase and ship to King Salmon its 2011-2012 diesel fuel. This loan was secured by first position lien against the fuel. The lien granted CFC also includes the Debtor's diesel assets and was senior to lien and mortgage of RUS. This loan was rolled into the approximately \$5 million loan to purchase 2012-2013 fuel which will be repaid in full in the summer of 2013. The Debtor will continue, in the foreseeable future, financing its annual fuel purchases and anticipates having to grant similar security interests to whoever loans it the funds to purchase that future fuel requirement. At this time, the CFC fuel loan has been paid down to about \$5 million, secured by about \$5 million of fuel, as well as the Debtor's diesel assets.

4. DIP Lien (air booster).

The Court approved a \$1.5 million debtor in possession loan from CFC to fund the purchase and operation of an air booster to attempt to clean the geothermal well of Barite drilling mud. CFC was granted a security interest in the Debtor's diesel assets, junior only to the mortgage and lien of RUS. The current balance of this loan is approximately \$1 million. This loan will be paid off in June 2013.

5. Drill Rig Liens

According to an appraisal obtained by Baker Hughes, the Debtor's drill rig and accessories may be worth less than \$4 million. It is valued in the Debtor's financial statement as worth about \$12 million. Inventory of casing and other material located on the site is valued by the Debtor in its financial statement as worth approximately \$2 million, but is probably worth substantially less than that if it is going to be shipped into Cook Inlet or other location other than Naknek. CFC holds two security interests in the drill rig, perfected under the Uniform Commercial Code securing loans of \$8.3 million and \$2.7 million. Between May 7, 2010 and August 25, 2010 six statutory liens against some or all of these assets totaling approximately \$7 million were recorded. On March 21, 2012 the Bankruptcy Court entered an Order and memorandum opinion in *Baker Hughes v. NEA et. al.* 11-90007, which prioritized the mining liens over CFC's Uniform Commercial Code liens. At this time the Debtor believes it is unlikely that there will be enough value in the drill rig to pay the statutory lien claimants in full, and, consequently, the CFC lien is completely unsecured.

6. Liens on geothermal real property

Between January 15, 2010 and August 17, 2010 three statutory liens were recorded in the Kvichak Recording District totaling about \$750,000 encumbering only the Debtor's Geothermal Real Property. In addition, some of the six statutory liens described above as Drill Rig Liens may also encumber the Geothermal Real Property. The Debtor believes the geothermal property is a liability, not an asset, but its Plan proposes that each statutory lien claimant will have the option of retaining its lien but not participating in any dividend paid to unsecured creditors, or reconveying its lien and joining the unsecured class in the amount of its remaining Allowed Secured Claim.

D. Claim Summary

A summary of the Debtor's pre-petition claims is found in Appendix 2. \$46,150,000 of claims have been filed in the case. Approximately \$2.7 million of these claims are the RUS loans secured by the diesel assets. RUS' lien is fully secured. Approximately \$15 million of these claims are secured by liens against the Debtor's drill rig and associated accessories and inventory. These liens are undersecured. The net value of the drill rig and associated accessories and inventory is substantially less than \$15 million and may be worth as little as \$3 million. CFC has filed a claim for \$26.7 million which is likely fully unsecured. Approximately \$37 million of total claims filed will be allowed as general unsecured claims.

VI. POTENTIAL LITIGATION AND DISPUTED CLAIMS

A. Avoidance Actions. The Debtor has investigated and determined that approximately \$500,000 of

payments it made to creditors within 90 days before its September 19, 2010 petition date were preferential payments under section 547 of the Bankruptcy Code. Under Section 546 of the Bankruptcy Code the Debtor has until September 18, 2012 to file complaints in the Bankruptcy Court seeking to avoid these transfers. Attached as Appendix 3 is a schedule of payments to creditors within the 90 days before the petition date which appear to not be payments in the ordinary course of Debtor's business and for which there do not appear to be subsequent value given by the creditor. The Debtor will report to the Unsecured Creditors Committee no later than July 31, 2012 what avoidance actions are meritorious and will be filed and its reasons for not pursuing other claims. Net proceeds of settlements or recovered judgments will be paid to Class 11.

C. Objection to Claims The Debtor has not completed review of claims filed.

GBR claim 10, \$908,000 The Debtor objected to this claim but has agreed that this claim should be allowed in the amount of \$450,000.

Arctic Drilling claim 29, \$67,000, The Debtor will object to the characterization of this claim as administrative.

VII. DESCRIPTION OF PLAN

A. Summary.

The following is only a general description of the Plan. Creditors and parties in interest should read the Plan carefully to determine its impact upon them and their Claims or interests. In the event of any inconsistency between this Disclosure Statement and the Plan, the provisions of the Plan shall control.

1. General The Debtor will terminate its geothermal project, close, plug and abandon the geothermal well. If it can raise the preliminary estimate of \$804,000 to plug and abandon its well before the drill rig is shipped out of Naknek, it will utilize the drill rig in this effort. Otherwise, it will lease a wireline vehicle, or other similar equipment to satisfy regulatory requirements that the well be plugged and abandoned. The Debtor's plug and abandonment budget of \$804,000, copy attached in Appendix 1, is preliminary and the Debtor has been told that it appears overstated. Even a plug and abandonment with a more limited cost of \$500,000 could not be performed in 2012. The Debtor's need to raise the funds necessary for plug and abandonment out of its rates will push out the first distribution to unsecured creditor, Class 11, into 2013 or 2014. The Geothermal Assets will be sold or otherwise disposed of in a manner fair and equitable to each lien claimant holding a lien in the Geothermal Assets. The proceeds of such sales or dispositions shall be paid to Allowed Secured Claims having liens against the Geothermal Assets, according to each claim as allowed, and in the priority established in the Agreed Order Approving Motion to Compromise Controversy (DE) or other proceedings in the Bankruptcy Court. Allowed Secured Claims in the Geothermal Real Property will be the beneficiaries of a mortgage recorded by the Debtor after the Effective Date, which mortgage will expire six (6) years after the Effective Date. Allowed Secured Claims who are beneficiaries of this mortgage may reconvey their interests before the first payments to Class 11, Unsecured Class and participate in the payment to that Class 11. Class 11 will be paid \$3 million over six years beginning in August, 2014. Class 11 will receive the net proceeds recovered in avoidance actions. No return of patronage capital to members will occur until after final payments under the Plan have been made. Class 11 will received a subordinated mortgage recorded against the geothermal property which expires six years after Confirmation.

2. Classification and Treatment of Claims. The Claims of creditors and interests of equity security holders are placed into Classes in Article 3 of the Plan. Article 4 specifies the treatment of Claims and interests.

The Debtor proposes the following classes of claims:

a. Administrative & Priority claims.

This class of claims does not vote.

- i. Priority claims. \$10,000. These are the claims of prior-members for return of their utility deposits. These claims will be paid in full to ex-members who can be found, at Confirmation.
- ii. CFC debtor in possession loan. \$1,037,000. This will be paid according to its terms over 36 months beginning in June 2011.
- iii. CFC fuel loan. \$5,000,000. This will be paid according to its terms or as amended beginning in July, 2012.
- iv. National Rural Electric Cooperative Association Any unpaid post-petition benefit contribution will be paid before Confirmation.
- v. Professional fees. All allowed professional fees will be paid on or before the Effective Date.
- vi. United States Trustee fees. All U.S. Trustee fees will be paid at or before confirmation and, later, when due.

b. Secured Claims

Class 1. Rural Utilities Services. \$2,694,516. This class of claims is impaired because it has been subordinated to the fuel loan lien of CFC. These loans are current and will remain current, and paid according to their terms.

Classes 2 through 9. Geothermal Asset liens and Geothermal Real Property liens. With the exception of a limited inventory of non-certificated rolling stock which the Debtor uses in both its diesel and geothermal operations, the Priority of Classes 2 through 9 in the Geothermal Assets is determined in the Agreed Order Approving Motion to Compromise Controversy (DE). The Allowed Secured Claims as allowed in that Order will receive pro rata distribution of the sale proceeds of the Geothermal Assets. Any remaining Allowed Secured Claim in the Geothermal Real Property will be the beneficiaries of a mortgage recorded by the Debtor after the Effective Date, which mortgage will expire six (6) years after the Effective Date. Allowed Secured Claims who are beneficiaries of this mortgage may reconvey their interests before the first payments to Class 11, Unsecured Class and participate in the payment to that Class 11.

Class 2. BJ Services, lien 1. \$914,484.39 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11.

Class 3 TIW \$128,043.88 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class

11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11.

Class 4 Centrifuge Services \$67,323.21 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11. This claimant will also receive a Class 11, unsecured claim in the amount of \$67,323.21

Class 5 GBR \$450,000 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11.

Class 6 Baker Hughes \$3,547,058.80 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11.

Class 7 BC Contractors. \$61,801. This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11. This claimant will also receive a Class 11, unsecured claim in the amount of \$61,801.

Class 8. Tecton Geologic. \$136,041.81 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11. This claimant will also receive an unsecured claim in the amount of \$136,041.81.

Class 9. Workstring. \$155,364.65 This class of claims is impaired. Its Allowed Secured Claim will be paid Proceeds from the sale or other disposition of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Following the Effective Date, this class of claims will be the beneficiary of a recorded

mortgage encumbering the Geothermal Real Property to secure any remaining interest this class has in the Geothermal Real Property. The mortgage will expire six (6) years following the Effective Date. This class of claims may reconvey its interest under this mortgage at any time before thirty (30) days before the first distribution to Class 11 under this Plan and participate in the Class 11 distribution to the extent of its remaining Allowed Claim. This class will receive forty five (45) written or electronic notice of the first distribution to Class 11. This claimant will also receive an unsecured claim in the amount of \$155,364.65.

Class 10 CFC \$26,760,209.07. This class of claims is impaired. This Class has an Allowed Secured Claim in the Geothermal Assets of approximately \$10,984,296, which is subordinate to the Allowed Secured Claims of Classes 2 through 9. It's Allowed Secured Claim will be paid Proceeds from the sale of the Geothermal Assets, according to its Priority, until such sale proceeds are exhausted. Then any remaining Claim 10 will be converted to Class 11, unsecured claims.

4.3 Unsecured Claims

Class 11. Unsecured claims. \$37,089,937. This class of claims is impaired. It will be paid \$3 million over six years, \$500,000 per year beginning in August, 2014, unless the Reorganized Debtor's obligation to plug and abandon the geothermal well is completed earlier than now scheduled, allowing for a first payment to this class before August 2014. This payment schedule will be accelerated with additional annual payments equal to the debtor's annual net income over \$100,000, as described in the Debtor's cash flow projections attached as Appendix 4 to the Amended Disclosure Statement. This class will also receive any Proceeds from the sale of Geothermal Assets not paid to any of Classes 2 through 10. This class will also receive the net proceeds from any avoidance actions the Debtor files. This class of claims will receive a mortgage subordinate to that mortgage given Classes 2 through 9, against Geothermal Real Property, which mortgage will expire six (6) years following the Effective Date.

4.4. Members

Class 12. Equity Interest Holders

The members of the Debtor have no interest cognizable in bankruptcy and are not entitled to vote on the Debtor's Plan of Reorganization.

3. Executory Contracts.

The Debtor is party to a labor contract which expired on October 31, 2011. It anticipates that the contract will be continued on a month to month basis until a new contract is negotiated, and, if necessary, approved by the Bankruptcy Court.

B. Financial Projections.

The Reorganized Debtor will pay Class 11 \$3 million over six years, \$500,000 per year beginning in August, 2014, unless the Reorganized Debtor's obligation to plug and abandon the geothermal well is completed earlier than now scheduled, allowing for a first payment to this class before August 2014. This payment schedule will be accelerated with additional annual payments equal to the debtor's annual net income over \$100,000. The Debtor will also pay Class 11 the Proceeds from any avoidance actions it files. A Schedule of these projected payments is found in Appendix 4. The Debtor's annual non-wholesale utilities sales has decreased from 17.2 million kWh in 2008 to 15.7 million kWh in 2011. The Debtor believes that sales will plateau at approximately non-wholesale 15.7 million kWh per year. The Debtor sells the largest percentage of its electricity in May through September of each year. This trend is apparent in both 2012 Monthly Cash Flow and Monthly Revenues in Appendix 4. This is why the annual payments to Class 11 are scheduled to be made in August of each year.

Appendix 4 contains two line charts which summarize the Debtor's fuel usage by gallons and energy sales by millions of kilowatt hours for the years 2008 through 2012 to date. These charts show both that the Debtor's sales in 2011 are lower than in earlier years, and that about one-half of its sales occur in April through July of each year.

In 2013 the Debtor will submit a construction work plan to purchase two engines to replace Units 9 and 10 which each have approximately 140,000 hours of use. That will be a \$2 million expense but might be financed through RUS over the life of the assets. The DIP loan will be paid off in 2013. The annual fuel loans do not appear on the Annual Pro Forma because they are paid off and refinanced on an annual basis. The Debtor's Annual Pro Forma predicts that it will develop sufficient net income to make the proposed plan payments.

Appendix 4 contains a summary of utility rates charged in other Western Alaska villages and cities. Total cost of power in those locations varies between \$.18/kWh in Kodiak to \$.81/kWh in Unalaska. The Debtor does not believe these comparisons are particularly useful because it is likely that its processors will decide to either purchase power from the Debtor or self-generate their power with their own generators. It is the Debtor's belief that it cannot significantly increase its rates above its current approximately \$.50/kWh without one of its processors electing to generate its own electricity.

The Debtor's May 31, 2012, RUS Form 7 financial statement, Appendix 1, contains a line item under Liabilities and other Credits for Patronage Capital. This entry does not represent a cash item. It is a bookkeeping entry which tracks the excess in Operating Revenue and Patronage Capital over the Total Cost of Electric Service. Through 2005, some portion of Patronage Capital was disbursed to members. In 2005 \$150,000 was disbursed to members. Prior to 2006 the Debtor was able to purchase its annual fuel needs with cash. Beginning in 2006, due to the higher cost of fuel, the Debtor began borrowing to purchase its fuel needs and suspended payment of Patronage Capital to its members. The Debtor's actual cash position in any month is accurately reported in its monthly reports. The Debtor will make no return of capital contributions during the term of its Plan. Because the Debtor must minimize rate increases to retain large power customers, it will reduce rates before it returns Patronage Capital.

VIII. CONFIRMATION

A. Bests Interests of Creditors / Liquidation Analysis.

To be confirmed by the Court, the Plan must pay creditors amounts at least equal to what they would obtain if it were liquidated under Chapter 7 of the Bankruptcy Code, unless a holder of a claim has agreed to different treatment. Because the Debtor is a non-profit cooperative corporation, under 11 U.S.C. §1112(c) no one, other than the Debtor can force it into a chapter 7. For purposes of analyzing whether the Debtors are treated fairly under the Plan, however, the Debtor has valued its assets at what a purchaser of the Debtor's business could recover in rates. Such a hypothetical purchaser is unlikely to pay more than it could recover in rates.

When a utility that is regulated by the Regulatory Commission of Alaska ("RCA") sets its rates, it must abide by the ratemaking rules set forth by the RCA and the Alaska Statutes. In general, rates are set to recover the utility's revenue requirements that, in turn, are equal to the sum of operating costs net of other income, depreciation, taxes, and return on rate base. Return on rate base includes both interest on debt and return on equity and is calculated by applying the weighted cost of capital (debt and equity) to the un-depreciated rate base. Thus when a utility or its assets are purchased, the purchaser will recover the cost of acquisition through depreciation and return on rate base.

When considering the value of a utility in Alaska, the purchaser must consider Sec. 42.05.441(b) of the Alaska Statutes. That section states:

"In determining the value for rate-making purposes of public utility property used and useful in

rendering service to the public, the commission shall be guided by the acquisition cost or, if lower, the original cost of the property to the person first devoting it to public service, less accrued depreciation, plus materials and supplies and a reasonable allowance for cash working capital when required."

In other words, the Regulatory Commission of Alaska ("RCA") places emphasis on the original cost less depreciation (or, net book value) when determining what is allowed in rate base and the amount that can be depreciated. Anything above the net book value is considered an "acquisition premium," and would, in most cases, not be allowed to be included in calculating rates. If an acquisition premium were allowed, the owners of the selling utility would be compensated above what they would normally achieve through regulated rates. This excess compensation would be borne by the ratepayers of the new utility. The owners of the purchasing utility also stand to gain since they will earn a return on the higher equity amounts used to fund the acquisition premium.

Even if the purchasing utility is not directly regulated by the RCA, the additional expenses associated with the acquisition premium may not be allowed when the RCA calculates the State subsidy payments through the Power Cost Equalization ("PCE") program.

There has been at least one instance in Alaska where an acquisition premium was allowed. However, both the seller and purchaser were non-profit utilities, and it could clearly be demonstrated that the ratepayers of both utilities would have lower rates in a combined utility even with the premium. The RCA has consistently held that it will not allow the inclusion of acquisition adjustments in rate base unless the adjustment is offset by clear economic benefit to utility customers, such as lower future rates.

Inclusion of the net book value of the well in the purchase price is also problematic in that it is not "used and useful." The RCA has a very strong history of not allowing assets into the rate base until they are operating and providing benefits to the ratepayers. If the purchaser continued development and eventually brought a resource on line, all assets prudently encumbered by the project could then be allowed. But to simply include part of the drilling costs in the purchase price and then abandon the well would, in all likelihood, not be allowed as a recoverable cost by the RCA.

In summary, the purchase price of the NEA system is prudently bound by the net book value of the system without any costs associated with the geothermal well.

It is likely that the piecemeal sale value of the Debtor's assets is not substantially different than the net book value of its assets. Its fuel tanks would be difficult to move. Most of the Debtor's generators are more than twenty years old. When the Debtor last retired generators it could not find buyers for them and ended up giving them away.

The Debtor's plan assumes that the electric utility will continue to be operated. The Debtor believes the liquidation value of its assets is the amount that the Regulatory Commission of Alaska would allow a buyer of the Debtor's utility assets to recover in its rates. The Debtor does not believe the Regulatory Commission of Alaska would allow the termination of the utility services the Debtor provides followed by piecemeal sale of its assets.

The Debtor's Liquidation Analysis (Appendix 1), is based upon its May 31, 2012 Form 7 and Trial Balance. A summary of the Debtor's Form 990 Tax Return of Organization Exempt from Income Tax (Appendix 1) shows that the Debtor reported net assets of \$8,926,311 on its 2011 Form 990. On its Liquidation Analysis, (page 1), the Debtor reported Net Plant in Service without Geothermal of \$5,736,152. The difference between the two is that the net assets on the Debtor's 990's include about \$3.2 million of fuel inventory, which are not included in the Liquidation Analysis. Finally, the Liquidation Analysis contains a line item for approximately \$800,000 of plug and abandonment expense. The expense of plug and abandonment in a liquidation would have to be paid before any distribution to unsecured creditors.

B. Fair and Equitable / Cramdown.

If a class rejects the Plan, but the Court finds that the Plan does not discriminate unfairly and is fair and equitable with respect to each impaired class which does not accept the Plan, the Plan Proponents may “cram down” the Plan by requesting the Court to confirm it over the objections of the rejecting class. The Plan Proponents request cramdown in Article X of the Plan.

C. Risk Factors.

Success of the Plan is conditioned on several factors

1. Maintaining the current rates does not result in loss of customers.

The Debtor cannot indiscriminately increase rates to pay its creditors. There will be a tipping point as rates are increased at which NEA's commercial customers will find other means of meeting their utility needs. They could do so in a variety of ways. They could produce all or more of their own electricity with generators in their possession or which they install at their facilities in the Debtor's service area. Fish processors could choose to process their fish in other locations. The Debtor believes that the rates it is currently charging members are very close to this tipping point. Ninety percent of non-wholesale power is purchased in the summer months by approximately five fish processors in the Debtor's service area. Three of those processors each purchase approximately 1,300,000 kwh per year of power, or a little less than 10% of the Debtor's annual non-wholesale power sales each. One of those processors has in place generators sufficient to allow it to generate the majority of its annual power requirements. If that processor were to chose to generate its own power, the Debtor would produce about 13,700,000 non-wholesale kwh of power on an annual basis. It would save, in today's dollars, approximately \$300,000 in fuel costs. But most of its remaining expenses would not decrease. It would have to recover those expenses from its remaining rate payers in the form of increased rates. The Debtor's Plan does not raise rates, but it also does not decrease rates. A loss of any load could easily trigger a cascade effect where increased rates lead other commercial customers to switch to their own electric generation or shift operations to other communities.

2. Increasing fuel surcharges will not result in loss of customers.

The Debtor projects that during the term of this Plan, the cost of diesel fuel may increase by 33%. That cost will be passed on to its members through cost of power surcharges. Any member of the Debtor which wishes to generate its own power will encounter similar fuel cost increases. But as the Debtor's rates increase to adjust for fuel price inflation, members will evaluate whether they can meet most or all of their power needs, with acceptable levels of attention to the mechanics of power generation, for price less than the Debtor will have to charge them.

3. Approval by Creditors. The success of the Plan is dependent upon prompt confirmation of the Plan and the contemplated pressure maintenance program. Confirmation of the Plan, in turn, is partially dependent upon the acceptance of the Plan by creditors and the determinations of the Court with respect to the requirements for confirmation under § 1129 of the Bankruptcy Code, which cannot be guaranteed.

D. Voting.

A ballot for voting to accept or reject the Plan is being mailed with this Disclosure Statement and the Plan. A creditor or holder of an equity security interest is entitled to vote if that person's claim or interest is “impaired” under the Plan. Articles 3 and 4 of the Plan identify the classes of Claims and interests, and whether they are impaired or unimpaired. Unimpaired classes are deemed to have accepted the Plan and need not vote.

Creditors and holders of equity security interests should read the ballot instructions carefully and complete all information requested on the ballot. The signed and dated ballot must be returned to Erik LeRoy, P.C., 500 L St., Ste 302, Anchorage, Alaska 99501, to be received by the date and time indicated on the ballot, in order to be

counted.

IX. AFTER CONFIRMATION

A. Tax Consequences.

The tax consequences of the Plan will vary significantly based upon each creditor's or affected party's individual circumstances. NEA is a non-taxable cooperative, so there should be no tax implications of the Plan. All creditors and parties in interest are urged to consult their own accountants or legal counsel regarding the tax effect of the Plan to them.

B. Discharge.

On the effective date of the Plan, the Debtor shall be discharged from any debt that arose before confirmation of the Plan, except that the Debtor shall not be discharged of any debt (i) imposed by the Plan, (ii) of a kind specified in 11 U.S.C. § 1141. After the effective date of the Plan all claims against the Debtor will be limited to these obligations.

C. Modification of Plan

The Debtor may modify the Plan at any time before confirmation of the Plan. However, the Court may require a new disclosure statement and/or re-voting on the Plan. The Debtor may also seek to modify the Plan at any time after confirmation only if (1) the Plan has not been substantially consummated *and* (2) the Court authorizes the proposed modifications after notice and a hearing.

D. Final Decree

Once the estate has been fully administered, either the Debtor shall file a motion with the Court to obtain a final decree to close the case, or the Court may enter such a final decree on its own motion.

1.X. CONCLUSION

After reading this Disclosure Statement and the Plan carefully, please complete the ballot and submit it in time to be counted. The Debtor requests your acceptance of the Plan.

NAKNEK ELECTRIC ASSOCIATION, INC.

Legal Counsel: ERIK LeROY, P.C.

Donna Vukich, General Manager

/s/ Erik LeRoy
500 L St., Ste 302
Anchorage, AK 99501
(907)277-2006