IN THE UNITED STATES DISTRICT COURT
FOR THE SOUTHERN DISTRICT OF TEXAS
CORPUS CHRISTI DIVISION

In Re:	§	
	§	
Scotia Development LLC, *et al.*,	§	**Civil Action: 08-259**
	§	
Debtor-In-Possession.	§	**Bankruptcy Case: 07-20027**
	§	

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CORPORATE DISCLOSURE STATEMENT

The Bank of New York Mellon Trust Company, National Association ("BNYM" or the "Indenture Trustee"), formerly known as The Bank of New York Trust Company, N.A., by and through its undersigned counsel, and pursuant to Federal Rules of Appellate Procedure 26.1 and Federal Rule of Civil Procedure 7.1, files this corporate disclosure statement identifying all of its parent corporations and all publicly held companies that directly or indirectly own, control, or hold, with power to vote, 10 percent or more of BNYM's outstanding voting securities. Regarding the foregoing, BNYM represents as follows:

1. BNYM's parent corporation is The Bank of New York Mellon Corp., a Delaware corporation.
2. No other publicly held company directly or indirectly owns, controls, or holds, with power to vote, 10 percent or more of BNYM's outstanding voting securities.

Angelo, Gordon & Co., L.P., Aurelius Capital Management, LP, and Davidson Kempner Capital Management LLC, by and through their undersigned counsel and pursuant to Federal Rule of Appellate Procedure 26.1 and Federal Rule of Civil Procedure 7.1, files this corporate disclosure statement identifying all of their parent corporations and all publicly held companies that directly or indirectly own, control, or hold, with power to vote, 10 percent or more of their respective outstanding voting securities. Regarding the foregoing, Angelo, Gordon & Co., L.P., Aurelius Capital Management, LP, and Davidson Kempner Capital Management LLC represent that no other publicly held company directly or indirectly owns, controls, or holds, with power to vote, 10 percent or more of their respective outstanding voting securities.

Scotia Redwood Foundation, Inc., by and through its undersigned counsel, and pursuant to Federal Rule of Appellate Procedure 26.1 and Federal Rule of Civil Procedure 7.1, files this

corporate disclosure statement identifying any parent corporation and all publicly held companies that directly or indirectly own, control or hold, with power to vote, 10 percent or more of its outstanding voting securities. Scotia Redwood Foundation, Inc. is wholly owned by Beal Financial Corporation, a privately-held company. No publicly held company directly or indirectly owns, controls, or holds, with power to vote, 10 percent or more of their respective outstanding voting securities.

CSG Investments, Inc., by and through its undersigned counsel, and pursuant to Federal rule of Appellate Procedure 26.1 and Federal Rule of Civil Procedure 7.1, files this corporate disclosure statement identifying any parent corporation and all publicly held companies that directly or indirectly own, control or hold, with power to vote, 10 percent or more of its outstanding voting securities. Scotia CSG Investments, Inc. is wholly owned by Beal Nevada Service Corporation, which is owned by Beal Bank Nevada, a subsidiary of Beal Banc Holding Company, which is owned by Beal Financial Corporation. These are all privately-held companies. No publicly held company directly or indirectly owns, controls, or holds, with power to vote, 10 percent or more of their respective outstanding voting securities.

STATEMENT REGARDING ORAL ARGUMENT

On September 21, 2008, this Court set oral argument for February 18, 2009, at 9:00 a.m.

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STATEMENT OF JURISDICTION

This is an appeal from the denial of a claim for a superpriority administrative expense under 11 U.S.C. § 507(b) over which the Bankruptcy Court had jurisdiction pursuant to 28 U.S.C. §§ 157(b)(2) and 1334. This Court has jurisdiction over this appeal pursuant to 28 U.S.C. § 158(a)(1).

On July 9, 2008, The Bank of New York Mellon Trust Company, N.A. (the "Indenture Trustee") filed its Notice of Appeal of the "Order Denying The Indenture Trustee's Motion For A Superpriority Administrative Expense Claim Pursuant To Section 507(b)," signed and entered by the Honorable Richard S. Schmidt of the United States Bankruptcy Court for the Southern District of Texas (Corpus Christi Division) (the "Bankruptcy Court") on July 8, 2008 (the "507(b) Order"). *See* Appellant 136;[1] *see also* Appellant 135. Noteholders Angelo, Gordon & Co. L.P., Aurelius Capital Management, LP, Davidson Kempner Capital Management LLC, CSG Investments, Inc. and Scotia Redwood Foundation, Inc. (collectively, the "Noteholders") also filed Notices of Appeal on July 9, 2008. Appellant 137-139.

The 507(b) Order is a final order for purposes of appeal. *See In re Datavon, Inc.*, 303 B.R. 119, 122 (Bankr. N.D. Tex. 2003); *In re SGS Studio, Inc.*, 256 B.R. 580, 581 (Bankr. N.D. Tex. 2000); *In re Mr. Gatti's, Inc.*, 164 B.R. 929, 930 (Bankr. W.D. Tex. 1994).

ISSUES PRESENTED

1. Whether the Bankruptcy Court erred in determining that there was no diminution in value of Scotia Pacific Company LLC's ("Scopac" or "Debtor") timberlands ("Timberlands") from January 18, 2008 (the "Petition Date") through June 6, 2008 (the "Confirmation Date")?

[1] References to the record are denoted herein as: "Appellant #" for items designated by the Appellants, and "Appellee #" for items designated by the Appellees.

2. Whether the Bankruptcy Court erred by considering the liquidation and/or foreclosure value in determining the diminution in value of Scopac's Timberlands from the Petition Date through the Confirmation Date?

3. Whether the Bankruptcy Court erred by relying on data and information that was not available on the Petition Date in determining the value of Scopac's Timberlands as of that date?

4. Whether the Bankruptcy Court erred by failing to find that Mendocino Redwood Company LLC ("MRC") and Marathon Structured Finance Fund L.P. ("Marathon") were judicially estopped from arguing that the value of the Timberlands did not decline between the Petition Date and the Confirmation Date?

5. Whether the Bankruptcy Court erred in determining that there was no diminution in value of Scopac's other assets, including Scopac's cash and cash equivalents, from the Petition Date through the Confirmation Date?

6. Whether the Bankruptcy Court erred in denying the Indenture Trustee's Motion to Grant Indenture Trustee a Superpriority Administrative Expense Claim Pursuant to Section 507(b) (the "507(b) Motion")?

STANDARD OF REVIEW

This Court reviews a bankruptcy court's findings of fact for clear error and its conclusions of law de novo. *Aguiluz v. Bayhi (In re Bayhi),* 528 F.3d 393, 402 (5th Cir. 2008); *Bossart v. Havis,* 389 B.R. 511 (S.D. Tex. 2008); *see also* FED. R. BANKR. P. 8013. Mixed questions of fact and law are reviewed de novo. *Bradley v. Ingalls (In re Bradley),* 501 F.3d 421, 428 (5th Cir. 2007); *Neely v. Smith (In re Neely),* 334 B.R. 863, 867 (S.D. Tex. 2005).

PRELIMINARY STATEMENT

The filing of a petition for bankruptcy protection under Chapter 11 triggers the entry of an automatic stay that prohibits disposition of the debtor's assets, including assets that serve as collateral for secured creditors' liens. A debtor-in-possession, however, may use that collateral during the course of the bankruptcy proceedings – including by spending cash collateral – if the debtor satisfies certain legal thresholds ensuring that the secured creditors' interests are adequately protected. This appeal concerns whether those legal requirements were properly observed during the 18 months that elapsed between the filing of the Debtor's bankruptcy petition and confirmation of the plan.

A debtor-in-possession may use cash or non-cash collateral securing creditors' liens only if the debtor can provide "adequate protection" to compensate the secured creditor for any decline in the collateral's value during the course of the bankruptcy. *See* 11 U.S.C. §§ 361, 362, 363(e). Adequate protection can take a number of forms, including (1) periodic cash payments to the secured creditor; (2) an additional or replacement lien on other property; or (3) other relief that provides the indubitable equivalent of an entity's interest in the property. 11 U.S.C. § 361. Such protection must be provided in a manner that takes into account the foreseeable likelihood that the collateral will decline in value. *See, e.g., In re Braniff Airways, Inc*., 783 F.2d 1283, 1286 (5th Cir. 1986) (noting that, in determining adequate protection "the potential harm to the creditor as the result of the property's decline in value" is to be considered). In the event that the collateral's loss in value is greater than anticipated – such that the offered protection ultimately proves "inadequate" to cover the actual loss in value – a secured creditor is provided additional protection in the form of a "superpriority administrative expense claim" under 11 U.S.C. § 507(b) (also known as a "507(b) claim" or "superpriority claim"). Such claims must be paid *in*

addition to amounts the secured creditor is entitled to receive under the confirmed bankruptcy plan.

In this case, the Appellant Indenture Trustee and the Appellant Noteholders were secured creditors of Scopac. They held notes issued by Scopac – on which had outstanding principal and interest of approximately $740 million was on the day the bankruptcy petition was filed – that were secured by virtually every asset of Scopac, including, most significantly, approximately 209,000-acres of redwood forest in Humboldt County, California ("the Timberlands") and approximately $48,700,000 in cash and equivalents ("the Cash Collateral"). By virtue of the automatic stay, the Appellants were prohibited from exercising their right to foreclose on the Timberlands, the Cash Collateral, or any other of Scopac's assets.

In a series of orders commencing immediately after the January 18, 2007 bankruptcy filing (the "Petition Date"), the Bankruptcy Court authorized Scopac to use the Indenture Trustee's Cash Collateral to fund various operations and obligations of the company. In doing so, the Bankruptcy Court ordered that Scopac provide "adequate protection" to the Indenture Trustee, both for the Cash Collateral and for the Timberlands. The Bankruptcy Court specifically promised that the Indenture Trustee would be entitled to a superpriority administrative expense claim to the extent of any "post-petition diminution of its interest in the Prepetition Collateral [which includes the Timberlands] and the Cash Collateral." *See* Appellant 20 at ¶¶ 28-29. That is, in exchange for allowing Scopac to use the property and spend the cash that secured their liens, the Indenture Trustee and the Noteholders were promised that they would be protected against any intervening loss in the value of their collateral by a superpriority claim. The premise of the Bankruptcy Court's assurance was that there ultimately would be

sufficient funds in the estate – indeed, in the Timberlands alone – to cover the Noteholders' $740 million-plus secured interest.

When confirming the reorganization plan 18 months later, however, the Bankruptcy Court determined that the Timberlands should be valued at only $510 million, nearly $250 million less than the debt. The Bankruptcy Court made that finding in the course of confirming a plan of reorganization – over the Indenture Trustee's objection – that, in effect, sold the Timberlands and Scopac's other assets to Appellees Marathon Structured Finance Fund ("Marathon") and the Mendocino Redwood Company ("MRC" and, together with Marathon, "MRC/Marathon"), stripped the Indenture Trustee's liens on those assets, and left the Noteholders with approximately $226 million in unpaid claims.[2] The Bankruptcy Court's going concern valuation of the Timberlands at the Confirmation Hearing was based expressly on the assertion that log prices had decreased precipitously in the six months before the hearing. Also, it was undisputed that the Cash Collateral was depleted by approximately $28 million through Scopac's payment of professional fees. Notwithstanding that evidence, the Bankruptcy Court denied the Indenture Trustee's superpriority claim, concluding that the value of the Timberlands had *not*, in fact, decreased during the 18 months between the Petition Date and the Confirmation Hearing.

The Bankruptcy Court's math simply does not add up. When Scopac wanted to spend the Indenture Trustee's Cash Collateral, the Indenture Trustee was told it had nothing to fear because the Timberlands were worth upwards of $750 million. However, when MRC/Marathon wanted to buy the Timberlands and other Scopac assets free and clear of the Indenture Trustee's liens, the Indenture Trustee was told that a recent drop in log prices had reduced the value of the

[2] The Noteholders have separately appealed confirmation of the plan directly to the Fifth Circuit pursuant to 28 U.S.C. § 158(d), arguing that the plan violates a number of legal requirements. After expedited briefing, the case was argued before Chief Judge Jones and Judges Owen and Southwick on October 6, 2008.

Timberlands to just $510 million. But, when presented with the Indenture Trustee's superpriority administrative expense claim to compensate for Scopac's use of the Cash Collateral and reduction in the value of the Pre-Petition Collateral during the bankruptcy case, the Indenture Trustee was told that the assets had actually *not* declined in value.

Unable to reconcile those obvious contradictions, the Bankruptcy Court made a series of errors that are the subject of this appeal. As explained in detail below, the Bankruptcy Court:

- erred in applying a "liquidation" or "foreclosure" value for the Timberlands instead of the fair market value that had been applied during confirmation proceedings;
- committed clear error in concluding that the Timberlands had not declined in value, by improperly relying on data and information unavailable as of the petition date;
- incorrectly refused to hold that, because MRC and Marathon had successfully advanced a lowball offer for the Timberlands during confirmation based on assertions that log prices had plummeted since the petition date, they were judicially estopped from claiming otherwise in opposition to the Indenture Trustee's 507(b) superpriority claim;
- erred in valuing the Cash Collateral by ignoring the effect of change in business losses, payment of professional fees, and the consumption of cash generated and then consumed during the course of the bankruptcy proceedings.

Accordingly, this Court should reverse the Bankruptcy Court's denial of the Indenture Trustee's 507(b) claim.

STATEMENT OF FACTS

I. General Case Background.

In 1998, Scopac was established as a separate and distinct company to take ownership of some 209,000 acres of timberlands in Humboldt County, California, previously held by its parent The Pacific Lumber Company ("Palco"), to facilitate the sale of certain collateralized notes on the public market. Appellant 3 at ¶ 5.

Pursuant to an Indenture dated July 20, 1998 (the "Indenture"), Scopac issued $867.2 million in notes (the "Notes"). Appellant 269. The Notes were secured by essentially all of

Scopac's assets under a Deed of Trust dated July 20, 1998 (the "Deed of Trust").[3] Included among these assets were: (1) the Timberlands themselves (Scopac's principal holding); (2) exclusive rights to harvest timber on an additional 12,000 acres of land owned by Palco; (3) computer software and other personal property used in Scopac's business; and (4) cash, including funds Scopac had placed in a Scheduled Amortization Reserve Account (the "SAR Account") (collectively "the Pre-Petition Collateral.").[4]

On the Petition Date, Scopac, Palco, Scotia Development Company LLC, Britt Lumber Co., Inc., Salmon Creek LLC and Scotia Inn Inc. (collectively the "Debtors") each filed separate voluntary petitions for relief under chapter 11 of title 11 of the United States Code (the "Bankruptcy Code"). Appellant 2. Approximately $714 million in principal and $26 million in interest (a total of $740 million) was outstanding on the Notes as of the Petition Date. Appellant 3 at ¶ 7. In addition, on the Petition Date, Scopac had $48.7 million in cash and cash equivalents, including approximately $42.5 million in the SAR account. Appellant 4 at pg. 8.

II. The Cash Collateral Orders

On the day after the petitions were filed, January 19, 2007, Scopac filed an Emergency Motion for Interim and Final Orders Authorizing the Debtor's Use of Cash Collateral. Appellant 4. In this motion, Scopac requested to use certain funds, including those in the SAR Account (i.e. Cash Collateral) to pay ordinary and necessary expenses of Scopac's ongoing business. In return, Scopac offered to provide adequate protection for all of the Indenture Trustee's Pre-Petition Collateral, which included the Timberlands. Appellant 4 at pg. 11.

[3] Pursuant to the Indenture and Deed of Trust, the holders of the Notes and Bank of America, N.A. ("BofA") were the beneficiaries of a joint, first priority lien on substantially all of Scopac's assets. Appellant 269 – 271.

[4] The SAR Account was established in 1999 to provide a revenue stream from which to make principal payments on the Notes. Funds held in the SAR account include interests in partnerships that carry a diverse portfolio of investments. Appellant 4 at 7-8.

That same day, the Bankruptcy Court entered an order authorizing Scopac to use the Cash Collateral to pay its post-petition operating and administrative expenses and found that the Indenture Trustee (and "BofA") was adequately protected because it would receive:

1. A replacement lien on all of the Pre-Petition Collateral, "equal to any diminution of the secured creditors' interest in the Pre-Petition Collateral [including the Timberlands] and Cash Collateral [including the SAR Account];"

2. "Grant" of a superpriority claim, as provided by section 507(b) of the Bankruptcy Code "to the extent of any diminution of their respective interests in the Prepetition Collateral and the Cash Collateral"; and

3. By operation of law, because the cash collateral "will be used to pay for ordinary and necessary expenses of maintaining and operating Scopac's business . . . ."[5]

Subsequent cash collateral order almost all of which were entered over the Indenture Trustee's objections, provided for the same adequate protection and further provided that, to the extent that funds were available, they were to be used to make interest payments and otherwise cover "all fees and expenses that become due subsequent to the Petition Date . . . under the Indenture when such amounts become due." Appellant 20 at ¶ 29. Identical language was included in every subsequent cash collateral order entered in the case. *See* Appellant 6, 13, 32, 92.

III. The Confirmation Hearing.

From April 8, 2008 through June 6, 2008, hearings were held to consider confirmation of five proposed plans of reorganization (the "Confirmation Hearing").[6] *See* Appellant 188-93, 197-202, 206-07. On June 6, 2008, the Bankruptcy Court entered its Findings of Fact and Conclusions of Law Regarding (A) Confirmation of MRC/Marathon Plan; (B) Denial of

[5] Appellant 4 at pgs. 12-13 ¶¶ 28, 30, 31.

[6] By the conclusion of the Confirmation Hearing, the only plans before the Bankruptcy Court were: (a) the Joint Plan of Reorganization for the Debtors proposed by MRC and Marathon, as later amended (the "MRC/Marathon Plan") [Appellant 86, Exhibit A-1] and (b) the Chapter 11 Plan for Scopac proposed by the Indenture Trustee, as later amended (the "Indenture Trustee Plan") [Appellant 86, Exhibit B-1]. The three plans of reorganization proposed by the Debtors were withdrawn during the course of the Confirmation Hearing. Appellee 48.

Confirmation of the Indenture Trustee Plan and (C) Denial of the Motion to Appoint a Chapter 11 Trustee (the "Findings and Conclusions"). Appellant 113. In its Findings and Conclusions, the Bankruptcy Court found that the value of the Timberlands was "no more than $510 million." Appellant 113 at pg. 61. In making that determination, the Bankruptcy Court found, among other things, that from October 1, 2007 through June 6, 2008 there had been a "significant" decline in log prices of 10% to 15%. Appellant 113 at pg. 36 ¶111 and pg. 45 ¶156. As demonstrated below, the Bankruptcy Court's Findings and Conclusions regarding the significant post-petition decline in log prices were adopted virtually verbatim from findings proposed by MRC/Marathon.

The Bankruptcy Court's Findings and Conclusions with respect to its intended confirmation of MRC/Marathon's Plan required that the Indenture Trustee receive a minimum of $510 million as payment of the "indubitable equivalent" of its collateral. Appellant 113 at pg. 6. However, a large 507(b) claim in favor of the Indenture Trustee (which would have to be paid in addition to the $510 million) would have required MRC/Marathon to pay more than they had anticipated under their plan and they indicated that they would not be willing to go forward on their plan. Appellant 207 at pgs. 13:14 – 15:24. The Bankruptcy Court, therefore, delayed the entry of its Confirmation Order and expedited the trial of the Indenture Trustee's 507(b) Motion. Appellant 208 at 29:11-17 and 48:25-49:2.

IV. The Hearing on the Indenture Trustee's 507(b) Motion.

On May 1, 2008, the Indenture Trustee filed its 507(b) Motion. Appellant 97.[7] From June 30, 2008 through July 2, 2008, a hearing was held to consider the Indenture Trustee's 507(b) Motion (the "507(b) Hearing"). Appellant 210-212.

[7]The Indenture Trustee filed an amended 507(b) Motion on July 2, 2008 (the "Amended 507(b) Motion"). Appellant 123. The 507(b) Motion and the Amended 507(b) Motion are referred to collectively herein as the "507(b) Motion."

At the 507(b) Hearing, a variety of evidence was presented of the value of the Timberlands at the Petition Date. The Indenture Trustee's expert, Mr. James Fleming, a registered professional forester with 30-years of experience appraising California redwood timberlands, determined the Petition Date value of the Timberlands to be $646 million. *See* Appellant 219; Appellant 211 at pg. 105:17. Mr. Fleming based his appraisal on a harvesting rate of 82 million board-feet per year and a discount rate of nine percent. Appellant 211 at pgs. 127:8-10, 145:14-16. To determine log prices, Mr. Fleming used actual local sales data from May 2006 until May 2007, as comparable sales were not available from the months immediately prior to the Petition Date. Appellant 211 at pgs. 170:13-171:13. To determine the discount rate, Mr. Fleming analyzed both general market risk (represented by Baa-rated bonds) as well as company specific risk. Appellant 211 at pgs. 145:22-146:9. In his June 2008 proffer, Mr. Fleming provided an in-depth, 9-page analysis of his determination of the discount rate, clearly setting forth both the general trends in the financial markets as well as issues specific to the Timberlands, such as the size of the property and the local regulatory environment. Mr. Fleming then confirmed the reasonableness of his discount rate analysis utilizing published discount rates associated with other real estate investments. Appellant 384 at pgs. 75-81, 83-86.

Mr. Joseph Radecki, a capital markets expert retained by the Indenture Trustee, offered reasons for a potential decline in value. He testified that during the bankruptcy period (i.e., from January 18, 2007 through June 6, 2008), economic conditions in the United States, and specifically in California, had significantly deteriorated as a result of certain market factors, including the subprime mortgage crisis, which affected new construction[8] as well as a variety of associated market mechanisms. Appellant 389 at pgs. 2-3. Mr. Radecki also testified that, as a

[8] The housing industry is the primary market for the timber harvested from the Timberlands.

result of these factors, the value of assets, particularly those which generate relatively low present earnings, such as timberlands, dropped precipitously beginning in the middle of 2007 and continue to drop, as financing for such assets (which has supported higher valuations in the past) continued to be either unavailable or much more expensive than in prior time periods. Appellant 390 at pg. 2. No party opposing the 507(b) Motion offered any testimony to rebut Mr. Radecki's expert opinions. Based on the testimony of Mr. Fleming and Mr. Radecki, the value of the Timberlands declined at least $136 million between the Petition Date and the Confirmation Hearing.

Mr. Richard La Mont, a consultant retained by MRC/Marathon as a timberland appraiser, testified that the Timberlands were worth approximately $370 million as of the Petition Date (approximately $60 million less than his $430 million valuation as of the Confirmation Hearing). *See* Appellant 276. Mr. La Mont used a discount rate of eight percent (one percent higher than he used in his Confirmation Hearing valuation) and a harvest rate of 60-65 million board-feet per year in reaching his valuation. Appellant 211 at pgs. 360:2-5; 376:19. However, while working as a consultant for MRC/Marathon, Mr. La Mont had participated in drafting a business plan in November of 2007, prior to his Timberlands appraisal, that estimated the 2007 harvest rate for the Timberlands at 78 million board-feet, but he testified that he decreased this rate sharply for his Timberlands valuation after "talking to Dr. Barrett," Scopac's CEO. Appellant 211 at pg. 377:8.

In addition, at the 507(b) Hearing, Mr. La Mont used redwood prices found in the little-known Pacific Rim Wood Reporter (Appellant 191 at pg. 131:1-12) as the basis for his estimate of log prices on the Petition Date, but reduced these prices by ten percent before including them in his Petition Date appraisal, even though he was aware that the publication's listed prices were

already lower than those of other reputable sources. Appellant 211 at pg. 403:15-404:10. Mr. La Mont later testified that he had not used this ten-percent-reduction approach in any of the seven property appraisals that he completed in the months prior to his Timberlands appraisal, nor had he ever before used the Pacific Rim Wood Reporter in making any appraisal. Appellant 211 at pgs. 391:24-392:10, 405:7-18.

Finally, limiting Mr. La Mont to the information that was available as of the Petition Date, Mr. La Mont's discount rate analysis consisted entirely of reviewing six sales in Oregon and Washington that occurred between April 2004 and January 2006 – between one and almost three years prior to the Petition Date. *See* Appellee 344; Appellee 276 at ¶ 16. Reviewing all of the comparable sales utilized by Mr. La Mont reveals that his analysis entirely fails to give any weight to the most contemporaneous transaction that he reviewed – an April 2007 transaction (three months after the Petition Date) that used a discount rate that was a full percentage point lower than the discount rate that Mr. La Mont selected. Appellee 344. The remainder of Mr. La Mont's analysis is comprised solely of reviewing materials prepared in mid-2008 that tended to indicate that discount rates for timberlands had been falling over the past several years. *See* Appellee 276 at ¶¶ 16-17; Appellee 280-282. Mr. La Mont's own contemporaneous data strongly suggests that this decline in discount rate had already begun as of the Petition Date, yet Mr. La Mont chose to rely on sales that occurred a year or more before the Petition Date in determining his discount rate for the Timberlands without providing any rationale for this methodology and without relating this discount rate to this specific property. After increasing his discount rate 1% above the rate used in his Confirmation Hearing appraisal, Mr. La Mont determined that the Timberlands had actually *increased* in the value by approximately $60 million during the bankruptcy case. Appellee 276 at ¶ 20.

The Bankruptcy Court also heard testimony that the fair market value of the Indenture Trustee's Cash Collateral diminished significantly during the pendency of the case. A significant portion of the Cash Collateral was lost when Scopac altered its business arrangement with Palco. Prior to August 2007, Palco was contractually obligated to advance certain costs associated with its timber purchases from Scopac. Appellant 3 at ¶ 24. Subsequently, however, over the Indenture Trustee's objections, the Bankruptcy Court permitted Palco to alter the contractual arrangement to require Scopac to pay for the costs up front. This alteration also contributed to the decrease in the overall value of the Indenture Trustee's cash collateral. Appellant 167 pgs. 116:13-20 and 118:18-20. Finally, during the case, Scopac's estate paid interest and professional fees which resulted in the depletion of the value of the Indenture Trustee's Cash Collateral. MRC/Marathon contended that the use of cash collateral to pay these expenses should not "count" toward any diminution. Appellant 210 pg. 81:9-12. Nonetheless, the Indenture Trustee lost a significant portion of its collateral as a result of these post-petition expenses. Appellant 211 at pgs. 237:13 – 238:5.

V. The Bankruptcy Court's Denial of the Section 507(b) Motion

On July 7, 2008, the Bankruptcy Court announced its findings on the record on the Indenture Trustee's 507(b) Motion. Appellant 213. The Court denied the Indenture Trustee's claim on the sole basis that it found no decrease in value in the Timberlands between the Petition Date and the Confirmation Hearing. Appellant 213 at pg. 26:6-7. The Bankruptcy Court made this determination even though it had previously found that there had been a substantial decline in the value of the Timberlands between October 2007 and the Confirmation Hearing. Thus, in order for the Bankruptcy Court's determination to make any sense, there had to be evidence that between the Petition Date and October 2007 the value of the Timberlands went up enough to

offset the substantial decline the Bankruptcy Court found had occurred between October 2007 and the Confirmation hearing. As demonstrated herein, there was no such credible evidence.

On July 8, 2008, the Bankruptcy Court issued its Order Denying the Indenture Trustee's 507(b) Motion. Appellant 135. This appeal followed. Appellant 136. The Bankruptcy Court ignored well-settled legal principles and the evidentiary record to justify its determination that, between the Petition Date and the Confirmation Hearing, there was no decline in the value of the Timberlands. The Bankruptcy Court concluded it was appropriate to value the Timberlands as of the Petition Date at their foreclosure/liquidation value. It then compared that *foreclosure/liquidation value* at the Petition Date to its own finding at Confirmation that the Timberlands had a *fair market value* of $510 million and held that the Timberlands had not decreased in value between the Petition Date and the Confirmation Date. Appellant 213 at pgs. 23:16-24:11; 18:14. Almost as an afterthought, the Bankruptcy Court also stated that the fair market value of the Timberlands at the Petition Date was also equal to their fair market value at Confirmation. *See* Appellant 213 at pgs. 24:23-25:3.

The Bankruptcy Court's entire basis for these remarkable determinations – remarkable in that the Bankruptcy Court had already found that there had been a substantial decline in value between October 2007 and the Confirmation Hearing – was its adoption of the discount rate used by MRC/Marathon's expert. Specifically, the Bankruptcy Court stated that:

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

Appellant 211 at pg. 25:13-23. Given this last statement, it is apparent that the Bankruptcy Court either failed to read or simply ignored Mr. Fleming's 9-page analysis of discount rates. Rather, the Bankruptcy Court's finding was based exclusively on Mr. La Mont's chart of discount rates from six sales in Oregon and Washington that occurred over a year before the Petition Date – a finding that enabled the Bankruptcy Court to determine, despite all of the evidence to the contrary, that the value of the Timberlands had not changed.

As to the Cash Collateral, the Bankruptcy Court found that those assets had a value of $48.7 million as of the Petition Date. After subtracting the $36.2 million payment due to BofA, the Bankruptcy Court determined that the remaining assets had a value of $12.5 million. Appellant 213 at pg. 27:3-16. The Bankruptcy Court then reduced the Indenture Trustee's distribution to account for the Indenture Trustee's professional fees that had been paid by Scopac's estate. Appellant 213 at pg. 28:3-15.[9] Accordingly, the Bankruptcy Court changed its Confirmation Order to require that the Indenture Trustee receive a minimum of $513.6 million (rather than the original $510 million) "in order to avoid any administrative claim" and to permit the MRC/Marathon Plan to go forward. Appellant 213 at pgs. 26:20-28:18.

SUMMARY OF THE ARGUMENT

The Bankruptcy Court's denial of the Indenture Trustee's 507(b) Motion should be reversed for the following reasons:

A. **The Bankruptcy Court erred in finding that the Indenture Trustee was not entitled to a superpriority administrative expense claim pursuant to section 507(b) of the Bankruptcy Code.** The Indenture Trustee proved the three elements necessary for a section 507(b) claim. First, the Indenture Trustee was afforded adequate protection by the Bankruptcy Court and that protection proved

[9] In particular, the Bankruptcy Court found that the Indenture Trustee had security of $522.5 million as of the Petition Date (i.e., timberlands ($510 million) + other assets ($48.7 million) – BofA's claim ($36.2 million) = $522.5 million). Appellant 213 at pgs. 26:20 – 28:5. Of that $522.5 million in alleged collateral value, the Bankruptcy Court then reduced the Indenture Trustee's distribution by $8.9 million to account for the Indenture Trustee's professional fees that were paid by Scopac's estate. *Id.* at pg. 28:6-10.

to be insufficient, leading to a diminution in the value of the Indenture Trustee's collateral. Second, the Indenture Trustee has a valid administrative expense claim pursuant to section 503(b) because the use of the Indenture Trustee's collateral was necessary to Scopac's bankruptcy estate. Finally, the diminution in the value of the Indenture Trustee's collateral was caused by (i) the Indenture Trustee being prohibited from foreclosing due to the automatic stay; and/or (ii) Scopac's use of the Indenture Trustee's collateral. Accordingly, the Bankruptcy Court erred in denying the Indenture Trustee's 507(b) claim.

B. **The Bankruptcy Court erred in finding that the Timberlands had not diminished in value from the Petition Date through the Confirmation Date.** In connection with the Confirmation Hearing, the Bankruptcy Court found that the Timberlands were valued at $510 million as of June 6, 2008. In reaching that conclusion, the Bankruptcy Court found that log prices dropped "significantly" during the bankruptcy case "by as much as 10% to 15%." Notwithstanding this finding and contrary to Marathon's and MRC's own documents and admissions with respect to the value of the Timberlands as of the Petition Date, the Bankruptcy Court erroneously found, for purposes of the 507(b) Motion, that the Timberlands had not diminished in value during the bankruptcy case.

C. **The Bankruptcy Court erred by considering the liquidation and/or foreclosure value in determining the diminution in value of Scopac's Timberlands from the Petition Date through the Confirmation Date.** The Supreme Court has held that value should be determined by considering the proposed use or disposition of the subject property. In this case, there was no question that Scopac was to be sold as a going concern; as no plan before the Bankruptcy Court proposed a liquidation. Accordingly, the fair market value of Scopac's assets was the correct measure of value to use in determining the diminution in value of such assets from the Petition Date through the Confirmation Date.

D. **The Bankruptcy Court erred by considering information that was not available on the Petition Date in determining the value of the Timberlands as of that date.** The Bankruptcy Court should have established the value of the Timberlands at the Petition Date by taking a "snap-shot" based on what was known at that point in time; the use of hindsight was not appropriate. By accepting the positions advanced by MRC's and Marathon's witnesses – who relied on information that was not available as of the Petition Date – the Bankruptcy Court erred in reaching its valuation conclusion with respect to the Indenture Trustee's 507(b) Motion.

E. **The Bankruptcy Court erred by failing to find that MRC and Marathon were judicially estopped from arguing that the value of the Timberlands had increased after the Petition Date.** In connection with the Confirmation Hearing, MRC/Marathon argued that the value of the Timberlands had decreased during the months preceding the Confirmation Hearing. The Bankruptcy Court

ultimately accepted this assertion and even adopted, in large part, MRC's/Marathon's proposed findings of fact to the effect that the value had decreased during the case. During the 507(b) Hearing, however, MRC/Marathon changed their position and argued that the value of the Timberlands actually *increased* during the bankruptcy case. Because the Bankruptcy Court had already accepted their position at the Confirmation Hearing, MRC/Marathon should have been judicially estopped from arguing otherwise at the 507(b) Hearing.

F. **The Bankruptcy Court erred in finding that Scopac's other assets, including Scopac's cash and cash equivalents, had not diminished in value from the Petition Date through the Confirmation Date.** Had the Indenture Trustee been allowed to foreclose on its collateral at the outset of the case, millions of dollars worth of its collateral would not have been consumed to pay (i) professional fees incurred by Scopac's estate; (ii) millions more in professional fees incurred by the Indenture Trustee; and (iii) millions of dollars more in professional fees and interest to BofA. By failing to account for this substantial expenditure of fees and expenses, the Bankruptcy Court erred in denying the 507(b) Motion.

ARGUMENT AND AUTHORITIES

The Bankruptcy Court erred by denying the Indenture Trustee's motion for a superpriority administrative expense claim pursuant to 11 U.S.C. § 507(b). The requirements for establishing a superpriority administrative expense claim pursuant to section 507(b) of the Bankruptcy Code have been summarized as follows:[10]

> First, adequate protection must have been provided previously, and the protection ultimately must prove to be inadequate. Second, the creditor must have a claim allowable under § 507(a)(1) (which in turn requires that the creditor have an administrative expense claim under § 503(b)). And third, the claim must have arisen from either the automatic stay under § 362; or the use, sale or lease of the collateral under § 363; or the granting of a lien under § 364(d).

[10] Section 507(b) of the Bankruptcy Code provides:

> If the trustee, under section 362, 363, or 364 of this title [11 U.S.C. § 362, 363, or 364], provides adequate protection of the interest of a holder of a claim secured by a lien on property of the debtor and if, notwithstanding such protection, such creditor has a claim allowable under subsection (a)(2) of this section arising from the stay of action against such property under section 362 of this title [11 U.S.C. § 362], from the use, sale, or lease of such property under section 363 of this title [11 U.S.C. § 363], or from the granting of a lien under section 364(d) of this title [11 U.S.C. § 364(d)], then such creditor's claim under such subsection shall have priority over every other claim allowable under such subsection.

11 U.S.C. § 507(b).

In re DeSardi, 340 B.R. 790, 801 (Bankr. S.D. Tex. 2006) (internal citations omitted); *In re McLeod*, 205 B.R. 76, 78 (Bankr. E.D. Tex. 1996) (citing *Ford Motor Credit Co. v. Dobbins*, 35 F.3d 860, 865 (4th Cir. 1994)).

I. Adequate Protection was Ordered by the Bankruptcy Court and that Protection was Proven Inadequate.

In order to have a valid section 507(b) claim, a creditor must first be granted a form of adequate protection. *See In re Welch*, No. 00-31731-T, 2001 Bankr. LEXIS 841 (Bankr. E.D. Va. Apr. 11, 2001); *Vincent Props., Inc. v. Five Star Partners, L.P. (In re Five Star Partners, L.P.)*, 193 B.R. 603 (Bankr. N.D. Ga. 1996); *In re James B. Downing & Co.*, 94 B.R. 515 (Bankr. N.D. Ill. 1988).

As noted above, early in the case, the Bankruptcy Court entered orders providing the Indenture Trustee with the following forms of adequate protection: replacement liens in the post-petition collateral, a superpriority claim as provided by section 507(b) of the Bankruptcy Code "to the extent of any diminution of their respective interests in the Cash Collateral resulting from Scopac's actual use thereof[,]" and a superpriority cost of administration priority claim under 11 U.S.C. § 507(b) to the extent of the post-petition diminution of its interest in the Prepetition Collateral [including the Timberlands] and the Cash Collateral [including the SAR Account].[11] *See* Appellant 20 at ¶¶ 28, 29 (emphasis added). Subsequent cash collateral orders provided for the same adequate protection and further provided that, to the extent that funds were available, they were to be used to pay a portion of the Indenture Trustee's professional fees and

[11] Determinations of appropriate adequate protection are within the bankruptcy court's discretion. *See* 11 U.S.C. § 361; *Resolution Trust Corp. v Swedeland Dev. Group (In re Swedeland Dev. Group)*, 16 F.3d 552, 564 (3d Cir. 1994) (citing *In re O'Connor*, 808 F.2d 1393, 1397 (10th Cir. 1987)). Marathon and MRC had numerous opportunities to object both to Scopac's motions for use of cash collateral as well as the language of each of the cash collateral orders entered thereon – but they failed to do so.

to make interest payments to the Indenture Trustee as additional adequate protection.[12] *See* Appellant 6 and 13.[13] Virtually identical language was included in every subsequent cash collateral order entered in the case. *See* Appellant 32, 42, 67, and 73.[14] However, the adequate protection purportedly granted to the Indenture Trustee completely failed, as demonstrated below.

II. The Appellants Were Entitled to an Administrative Claim Because Their Interest in the Timberlands Decreased Significantly Between the Petition Date and the Confirmation Date.

The determination of any diminution of value of the Timberlands requires an analysis of the value as of the Petition Date versus the value ascribed to it as of the Confirmation Hearing.

In its Findings and Conclusions, the Bankruptcy Court found that the Timberlands had a value of no more than $510 million as of the Confirmation Hearing (i.e., June 6, 2008). Appellant 113 at pgs. 9, 31, 61. The Bankruptcy Court reached that value determination based largely on the evidence that there had been a significant decline in applicable timber prices from at least October, 2007 through June 6, 2008. *Id.* at pg. 45, ¶¶ 156 - 157. In particular, the Bankruptcy Court found as follows:

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[12] No interest payments were ever made to the Indenture Trustee, as funds were never available.

[13] Section 506(b) of the Bankruptcy Code provides:

> To the extent that an allowed secured claim is secured by property the value of which, after any recovery under subsection (c) of this section, is greater than the amount of such claim, there shall be allowed to the holder of such claim, interest on such claim, and any reasonable fees, costs, or charges provided for under the agreement or State statute under which such claim arose.

11 U.S.C. § 506(b) (emphasis added). Because Section 506 has the effect of preventing a secured creditor from receiving interest on its claims where no equity cushion exists upon which such payments could be based, the Bankruptcy Court clearly accepted the premise that, as of the Petition Date, the Indenture Trustee was oversecured.

[14] Throughout the course of the bankruptcy case, the Indenture Trustee endeavored to insure that its collateral interests were adequately protected. *See* Appellant 7 & 9 (Motion for Determination that Scopac was a Single Asset Real Estate Debtor); Appellant 17, 30, 40, 45, 66, 71, 100 (Cash Collateral Objections/Responses); Appellant 28, 44, 46, 63 (Exclusivity Objections/Responses); Appellee 51 (Motion to Appoint a Chapter 11 Trustee); *see also* Appellant 210 at pg. 72:16-18 (The Bankruptcy Court: "Now, here we have the SAR[E] motion, which is similar to a motion to lift stay; it basically shortens the stay; it shortens everything.").

- In the last six months, log prices have dropped significantly by as much as 10% to 15%, particularly in young growth redwood. Likewise, Douglas fir prices are at an all-time low. This decrease in log prices is attributable to the economic slowdown, particularly in the housing market, which has resulted in a decline in building and remodeling activity. Appellant 113 at ¶ 111 (emphasis added) (internal citations omitted).

- Despite the considerable drop in log prices during the 6-month period from October 1, 2007, through the present time, Mr. Fleming made no efforts to update his findings to reflect the value of the Timberlands during this time. Appellant 113 at ¶ 157 (internal citations omitted).

- Changing only this one price of this one type of log to $800–$850/MBF and keeping all other aspects of Fleming's report the same reduces Fleming's valuation by $100-$153 million, dropping his fair market value of the timberlands from $605 million to $452 million. Appellant 113 at ¶ 158 (emphasis added).

See also Appellant 113 at ¶¶ 103, 104, 147, 163, 206. Having reached its Confirmation Hearing value, all that remained for purposes of determining the amount of the Indenture Trustee's 507(b) claim was for the Bankruptcy Court to determine the corresponding value for the Timberlands as of the Petition Date.

A. The Bankruptcy Court Erred by Using the Liquidation and/or Foreclosure Value in Determining the Diminution in Value of the Timberlands as of the Petition Date.

The Bankruptcy Court's first and most fundamental error was that, although it valued the Timberlands at the Confirmation Hearing using a fair market value analysis, it used an entirely different method of valuing the Timberlands as of the Petition Date.

The Bankruptcy Court chose to measure the value of the Timberlands at the Petition Date according to the "foreclosure" or "liquidation" value of the Timberlands, rather than their "fair market" or "going concern" value. *See* Appellant 213 at pg. 23:20-23 and pgs. 24:24 – 25:1

(stating that "there's been no evidence as to a decline in the foreclosure value of the case").[15] It justified this decision by claiming that the interest preserved through "adequate protection" is the "secured creditors' interest in the property." Appellant 213 at pg. 23:16-18. The Bankruptcy Court continued its justification for its choice of valuation standard by stating that, because the "interest a secured creditor has a right to is the right to foreclose," foreclosure value should be used. Appellant 213 at pg. 23:18-20. The Bankruptcy Court then denied the Indenture Trustee's administrative superpriority claim because it determined the Indenture Trustee had not offered evidence of foreclosure or liquidation value, and had therefore failed to meet its burden under 507(a). Appellant 213 at pgs. 22:17-19, 24:15-19.

B. The Bankruptcy Court Should Have Used a Valuation Method that Reflected the Intended "Use" of the Collateral.

The Bankruptcy Court erred by using a foreclosure valuation contrary to the standards of valuation clearly mandated by the Bankruptcy Code and case law precedent. Section 507(b) of the Bankruptcy Code does not specifically provide which valuation model should be employed when determining whether a diminution of collateral value has occurred. Instead, it is well established that valuation decisions must be made on a case-by-case basis. *Fin. Sec. Assurance Inc. v. T-H New Orleans Ltd. P'ship (In re T-H New Orleans Ltd. P'ship)*, 116 F.3d 790, 799 (5th Cir. 1997).

However, Section 506(a) of the Bankruptcy Code, which states the mechanism for determining the extent of the claim of an *undersecured* creditor (one whose claim is greater than the current value of the collateral), provides, in relevant part, that an undersecured creditor's claim is a "secured claim to the extent of the *value* of such creditor's interest" in the collateral.

[15] In its oral ruling, the Bankruptcy Court did acknowledge that "even looking at the fair market value, the evidence showed that from filing to confirmation, the forests grew so that there are more trees." Appellant 213 at pgs. 24:23-25:1-3.

11 U.S.C. § 509(b); *see also United Savs. Ass'n of Tex. v. Timbers of Inwood Forest Assocs., Ltd.*, 484 U.S. 365, 372 (1988) (citing H.R. REP. NO. 95-595, pp. 181, 356 (1977)) ("[t]he phrase 'value of such creditor's interest' in § 506(a) means 'the value of the collateral.'"). Thus, Section 506(a) requires a finding of the value of a secured creditor's collateral and states further that "[s]uch value shall be determined in light of the purpose of the valuation and of *the proposed disposition or use of such property*, and in conjunction with any hearing on such disposition or use or on a plan affecting such creditor's interest." 11 U.S.C. § 506(a)(1) (emphasis added). The Supreme Court has noted, "As we comprehend § 506(a), the 'proposed disposition or use' is of paramount importance to the valuation question." *Assocs. Commercial Corp. v. Rash*, 520 U.S. 953, 962 (1997) (holding that "replacement value"[16] rather than "foreclosure value" provided the appropriate standard to value a truck that secured a creditor's claim because the debtor proposed to retain and use the truck under a chapter 13 plan).[17]

Thus, under Section 506(a)(1), the applicable standard for determining value of collateral turns ought to turn on the proposed disposition or use of the property. Here, the Bankruptcy Court was calculating a super priority administrative claim in connection with a plan of reorganization that contemplated that the collateral would continue to be used as part of a going concern. Therefore, it was not proper for the Bankruptcy Court to focus on the value of the collateral from the hypothetical point of view of a lender who might foreclose and accept liquidation value. Indeed, in *Rash*, the Supreme Court explicitly rejected the notion - applied

[16] The Supreme Court explained that "replacement value" was consistent with "fair market value"—"the price a willing buyer in the debtor's trade, business, or situation would pay a willing seller to obtain property of like age and condition." *Rash*, 520 U.S. at 959 n.2.

[17] Importantly, however, the valuation difference in *Rash* is not present in this case. In *Rash*, because of market conditions for the collateral in question (a used truck), the debtor would have had to pay more to replace the collateral than the secured creditor would have received upon selling it. In contrast, there is no reason to believe that, in the case of an asset as unique as the Timberlands, there would be any meaningful difference between what Scopac would have to pay to buy it and what the Indenture Trustee could receive upon selling it.

here by the Bankruptcy Court - that secured property should be valued from the secured creditor's perspective. *See Rash*, 520 U.S. at 960. Liquidation value should not be used unless a foreclosure is imminent, or is, at the very least, the foreseeable outcome.[18] Rather, the valuation should be based on the proposed use of the collateral as of the Petition Date.

C. Throughout the Bankruptcy Case the Debtors Were in Continuous Operation of their Businesses, Thus, Fair Market Value Was the Appropriate Valuation Standard.

At no time during the course of this bankruptcy has a foreclosure or liquidation been imminent, or even foreseeable. Not at the Petition Date, not at confirmation, and at no point in between. To the contrary, beginning with the entry of the first cash collateral order through the entry of the Findings and Conclusions, the focus of all determinations relating to value was on the Timberlands' fair market value as a going concern. Scopac's business was operating throughout the time period during which the Cash Collateral Orders were entered.

Moreover, during the Confirmation Hearing, all of the experts valued the Timberlands based on their fair market value. *See, e.g.*, Appellant 113 at pg. 31 (Mr. La Mont's analysis); Appellant 113 at pg. 41 (Mr. Fleming's analysis.); Appellant 113 at pg. 53 (Dr. Reimer's analysis).[19] Likewise, the Bankruptcy Court, in its Findings and Conclusions, used the fair market value standard to determine the value of the Timberlands as of the Confirmation Hearing.

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[18] Courts utilizing liquidation value in 507(b) cases only do so in cases where liquidation of the collateral has either already occurred or is imminent. *See United Missouri Bank of Kansas City, N.A. v. Federman (In re Modern Warehouse, Inc.)*, 74 B.R. 173, 177 (Bankr. W.D. Mo. 1987) (stating that, when "liquidation is the ultimate event which must be contemplated," liquidation value is appropriately considered). Sensibly, when the back-end value of property has already been fixed by liquidation, a court should determine diminution from a front-end liquidation value. *See id.*; *In re Ralar Distribs.*, 166 B.R. 3, 5 (Bankr. D. Mass. 1994), *aff'd sub nom, Baybank-Middlesex v. Ralar Distribs. (In re Ralar Distribs.)*, 182 B.R. 81 (D. Mass. 1995), *aff'd*, 69 F.3d 1200 (1st Cir. 1995). Accordingly, where, as here, a back-end fair market valuation has been determined as of the Confirmation Hearing, fair market value of the collateral as of the Petition Date must be used.

[19] Mr. Richard La Mont was Marathon's timberland appraiser; Mr. James Fleming was the Indenture Trustee's timberland appraiser; and Mr. James Yerges was the Debtors' timberland appraiser. Although Mr. La Mont also offered opinions as to the liquidation value of Scopac, those opinions were offered to support MRC/Marathon's efforts to satisfy 11 U.S.C. § 1129(a)(7), which concerns a hypothetical liquidation under chapter 7 of the Bankruptcy Code. *See* Appellant 113 at pgs. 40-41, 105–06.

See, e.g., Appellant 113 at pg. 114. This standard was appropriate because Scopac was in continuous operation and each of the proposed plans of reorganization before the Bankruptcy Court at the Confirmation Hearing contemplated and provided for such continued operation.

At the 507(b) Hearing, the Bankruptcy Court refused to reconsider its "confirmation value," and limited the Indenture Trustee to proving the correlative fair market value of the Timberlands as of the Petition Date. *See* Appellant 210 at pgs. 32:21 – 33:7; *see also* Appellant 213 at pg. 19:23-25 (The Bankruptcy Court: ". . . I'm not changing any of those findings with respect to the analysis that I did in the opinion on confirmation."). With the Bankruptcy Court's fair market valuation of the Timberlands at Confirmation as the back end starting point, in order to compare "apples to apples," the Indenture Trustee and all of the other parties who presented evidence, including MRC/Marathon, presented evidence of the fair market value of the Indenture Trustee's collateral as of the Petition Date.[20]

Thus, any suggestion that the conduct of the parties contemplated a diminution or value calculation based on a future, potential liquidation of Scopac is not supported by the record. Fair market value, based on the continued use of the Timberlands as a going concern, was the only valuation measure ever contemplated, from Petition Date to Confirmation. Accordingly, the fair market value of the Timberlands at the Petition Date was the only fair basis of comparison to the value determined at the Confirmation Hearing.

The Bankruptcy Court found no decline in the value of the Timberlands during the bankruptcy proceedings, in no small part because it chose a false basis of comparison, explicitly comparing the fair market value of the Timberlands at Confirmation ($510 million) with the

[20] While the valuation process "is not an exact science and the Court must consider approximations founded upon opinions and assumptions" (*La Jolla Mortgage Fund v. Rancho El Cajon Assocs.*, 18 B.R. 283, 288 (Bankr. S.D. Cal. 1982)), the Supreme Court has made clear that the court must select one general method for determining value and cannot combine multiple approaches. *See Assocs. Commercial Corp. v. Rash*, 520 U.S. 953, 964–65 (1997).

foreclosure value on the Petition Date. *See* Appellant 213 at pg. 24: 5-19 ("No evidence was presented to suggest that the *liquidation* or *foreclosure* value at filing was higher than the *fair market value* at confirmation.") (emphasis added).

The Bankruptcy Court provided no basis for juxtaposing these two separate valuation methods, and none exists. Comparing foreclosure value at one point to fair market value at another will never accurately measure a decrease in value, because the difference in value due simply to the change in valuation methodology will usually overwhelm any actual change in the value at issue. Foreclosure value is, by its nature, always less than fair market value (because a financially secure seller can hold out for a better offer—an option that is unavailable in a foreclosure). The Bankruptcy Court erred by applying inconsistent valuation standards to support its finding that there was no diminution in value of the Timberlands from the Petition Date through Confirmation.

D. The Bankruptcy Court Ignored the Substantial Evidence Showing a Decline in the Value of the Timberlands.

The Bankruptcy Court ignored the overwhelming evidence of value, *including its own previous findings*, the assumptions of all the parties to the case, and the *only* competent testimony offered of the Timberlands' value as of the Petition Date, all of which compelled the conclusion that the Timberlands declined in value between the Petition Date and the Confirmation Hearing.

Throughout the bankruptcy case, Scopac maintained that the value of the Timberlands exceeded the amount of the Indenture Trustee's secured claim (i.e., in excess of $740 million). In fact, in September 2007, when Scopac filed its initial plan of reorganization, Scopac proclaimed that: "The Debtors' appraisals of their assets, determined in consultation with their experts, indicate the appraised value to be in excess of $1.4 billion. . . ." Appellant 57 at pg. 1;

see also Appellant 304 at pgs. 4-5 (Yerges expert report) and Appellant 307 at pg. ii (Mundy expert report). Indeed, as the Bankruptcy Court noted a few months before the Confirmation Hearing:

> There is . . . we'll find out if it protects you [Indenture Trustee] like I did before based on the evidence that we have before us and the forest that's out there. No question that the issue is getting closer and closer. We don't know specifically, although there is some indications the value of the force [sic] is **way more than $758 million.** Whether that is true or not, I mean nobody's offered to come in and buy it yet for anything more than $758 million . . . . But, I'm going to keep the operations . . . .

Appellant 172 at pg. 86:7-16 (emphasis added).

As for MRC, in 2005, an MRC affiliate indicated that it was seeking to acquire Scopac's Timberlands for in the range of $600-$760 million. Appellant 263 at pg. 3. In addition, in 2006, MRC negotiated a lengthy term sheet to acquire all of the equity in Palco (which would include Palco's interest in Scopac), implying a valuation of $781 million for Scopac's assets. Appellant 192 at pgs. 353:24-355:20.

The only reliable evidence of the Timberlands' value as of the Petition Date,[21] came from the Indenture Trustee's expert Mr. James Fleming, who opined that the Timberlands were valued at $646 million at that point.[22] Mr. Fleming was the only expert offered at the 507(b) Hearing with 30 years experience or who was a Registered Professional Forester in the state of California. *See* Appellant 387 (CV of Fleming). Mr. Fleming was also the only expert who had ever appraised redwood timberlands. *See* Appellant 211 at pgs. 200:4 – 8.

To further establish that the value of the Timberlands as of the Petition Date was far in excess of $510 million even using MRC's own methodologies, Mr. Fleming performed an

[21] Notwithstanding the fact that MRC/Marathon's expert, Mr. La Mont, acknowledged that a full appraisal was the preferred approach because it was a more reliable indicator of value, Mr. La Mont did not complete such an appraisal. *See* Appellant 212 at pg. 43:1. In fact, before this case, Mr. La Mont had never been qualified in court to give an appraisal opinion. Appellant 211 at pg 373:17-19.

[22] Appellant 384 (Proffer of Fleming).

alternative analysis that (i) utilized the harvest rate and discount rate estimates presented by MRC's CEO around the Petition Date, and (ii) employed all other assumptions utilized by Marathon's expert.[23] Under this approach, Mr. Fleming found the Petition Date value of the Timberlands was $668 million.[24] Accordingly, the value of the Timberlands declined by $136-$158 million from the Petition Date through the Confirmation Hearing.[25]

The Bankruptcy Court's own Findings and Conclusions further support Mr. Fleming's Petition Date valuation and the reason for a decline in value, as explained by Mr. Radecki. The Findings and Conclusions established that log prices had dropped significantly, by as much as 10% to 15% in the six months prior to the Confirmation Hearing, particularly for young growth redwood, and that this decrease was incorporated into the Bankruptcy Court's Confirmation Hearing valuation, and was relied upon by MRC/Marathon's expert. Appellant 113 at ¶¶ 111, 156. According to the Bankruptcy Court, the 10%-15% decrease in log prices had the effect of reducing Mr. Fleming's valuation of the Timberlands by between $100 million and $153 million. Appellant 113 at ¶ 158.

The Bankruptcy Court's Findings and Conclusions tied this 10%-15% decline in timber prices to the economic slowdown, which resulted in a decline in building and remodeling activity. Appellant 113 at ¶ 111. Thus, the Bankruptcy Court's Findings and Conclusions are consistent with Mr. Radecki's testimony. The Bankruptcy Court's own findings therefore

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[23] *See* Appellant 417 at pg. 672 (Email from MRC CEO Sandy Dean suggesting a harvest rate of 90-100 million board feet ("MBF")); *see also* Appellant 437 at pg. 2 (admitting that discount rates were lower than 7% around March 2007).

[24] Mr. Fleming's Petition Date appraisal was based upon market information that was available as of that date. *See* Appellant 211 at pg. 114:9-17.

[25] This decline in value was supported by the testimony of Mr. Joseph Radecki, the Indenture Trustee's capital markets expert. Mr. Radecki testified to a decline in timber prices due to several market factors, including the slowdown in construction caused by the subprime mortgage crisis, and noted that this price decline would have a precipitous effect on the value of the Timberlands. *See* Appellant 389 at 2-3. No party opposing the 507(b) Motion offered any evidence to rebut Mr. Radecki's testimony.

suggest that a change in fair market value occurred, based on macroeconomic factors outside the Timberlands themselves, resulted in a valuation loss of the approximate magnitude as claimed by the Indenture Trustee.

However, the Bankruptcy Court ignored its previous findings in denying the Section 507(b) Motion. The Bankruptcy Court stated that it was unconvinced by Mr. Radecki's testimony on market forces, because Mr. Radecki could not tie the decline in timber prices "with any specificity to this case, to this county, to the redwood forests, or this industry specifically." *See* Appellant 213 at pg. 23:10 – 15. This attack on Mr. Radecki's testimony not only makes no sense - Mr. Radecki was testifying as to decline in the building and home remodeling markets, which affected the entire country, so there was no need to have the testimony be directed with more specificity - the Bankruptcy Court ignored the fact that it had relied on a similar market decline in its own Findings and Conclusions. In fact, Mr. La Mont, MRC/Marathon's expert, admitted that general market risk had increased significantly since the Petition Date and that there has been a general market decline, and used this information in his Confirmation Hearing valuation. *See* Appellant 212 at pgs. 58:12 – 59:19.

Most importantly, the Bankruptcy Court also found that any change in the price of timber was outweighed by the fact that the discount rate had gone down since the Petition Date. Appellant 213 at pg. 25: 13-23. Beyond the fact that the Bankruptcy Court makes no attempt to quantify the actual changes in value caused by changing these two valuation variables, this finding is also clearly erroneous because it is based on the testimony of Mr. La Mont, who obtained his data on the discount rate on the Petition Date through, among other things, inappropriate hindsight evidence, as described *infra*. The Bankruptcy Court disregarded the careful analysis of discount rates by Mr. Fleming and adopted the fundamentally flawed opinions

of Mr. LaMont which provided a basis for making a ruling that would permit the MRC/Marathon Plan to go forward.

E. The Bankruptcy Court Credited Evidence by MRC/Marathon's Appraisers, Who Lacked Qualifications and Relied on Improper Evidence of Value.

Having discounted, without reason, the evidence presented by the Indenture Trustee showing a decline in value, the Bankruptcy Court then accepted MRC/Marathon's evidence, which was materially flawed in a number of respects, each of which is discussed below.

1. MRC/Marathon's Witnesses' Testimony Lacked Any Credibility Because they Conveniently and Improperly Changed Their Methodologies to Suit Their Clients' Interests.

The Bankruptcy Court found at the Confirmation Hearing that Mr. La Mont's testimony was the most credible. *See* Appellant 113 at ¶ 134. Yet, testimony elicited at the 507(b) Hearing revealed that Mr. La Mont had never appraised redwood timberlands; had never appraised timberlands in Humboldt County; and had never used Pacific Rim Wood Market pricing data (the source he used in both his Confirmation Hearing and Petition Date valuations) in any appraisal prior to Scopac's chapter 11 case.[26] *See* Appellant 211 at pgs. 371:6 – 372:13, 404:14 – 405:19.

Moreover, Mr. La Mont testified that he obtained the Pacific Rim Wood Market pricing data from MRC (primarily because Mr. La Mont did not even subscribe to the newsletter publication) and Mr. La Mont did nothing to validate this data prior to his Confirmation Hearing valuation.[27] Appellant 211 at pgs. 405:21 – 406:24, 410:18-23; Appellant 432. At the 507(b)

[26] Pacific Rim Wood Market was a monthly newsletter which published log pricing data based upon voluntary surveys of log buyers. This newsletter, which stopped publication in or around April 2007, contained limited redwood pricing information; involved primarily species common to the Pacific Northwest (not California); and was not widely distributed in California. *See* Appellant 427; Appellant 119 at pg. 131:1-12. In contrast to Mr. La Mont, every other expert in the case utilized either California State Board of Equalization ("SBE") pricing data or actual market data.

[27] The evidence established that a portion of the Pacific Rim pricing that Mr. La Mont relied upon was in fact never published. *See* Appellant 211 at pgs. 409:23-25 – 410:1-9; Appellant 212 at pgs. 28:22-25 – 30:1-23. Once Mr. La

hearing, Mr. La Mont again used redwood prices found in the Pacific Rim Wood Reporter as the basis for his estimate of log prices on the Petition Date, but reduced these prices by ten percent before including them in his Petition Date appraisal, even though he was aware that the publication's prices were widely considered to be very conservative. Appellant 211 at pg. 403. When pressed on cross-examination, Mr. La Mont later testified that he had not used this ten-percent-reduction approach in any of the seven property appraisals that he completed in the months prior to his Timberlands appraisal, nor had he ever before used the Pacific Rim Wood Reporter in making any appraisal. Appellant 211 at pgs. 388-92, 405.

In addition, the Indenture Trustee uncovered a September 2007 email from Mr. Dean,[28] MRC's CEO, that described a meeting with representatives of Marathon. Appellant 437. The e-mail disclosed a cynical view of the manner in which the appraisal/valuation process could be manipulated:

- A Marathon representative "conceded that if the note holders could prove impairment that they would not have to share with Marathon, but he thinks the valuation arguments will (be) so muddied (three sets of appraisals, hearings etc. . . .) that the note holders will never prove impairment."

- "We knew this before Marathon meeting, but Marathon show that debtor and Marathon think they can proceed with a bogus appraisal and cram down to leave note holders in a very bad place."

Appellant 437 at 3.

Consistent with "muddying" the "valuation arguments," Mr. La Mont found that, despite the worst housing market conditions in recent memory, the significant decline in log values, and

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Mont realized that the data he had been relying on did not exist, he switched to a different methodology whereby he used averages of historic data to fill in the price points for which Pacific Rim data did not exist. *See* Appellant 212 at pg. 74:7-18. This change in methodology was not disclosed to the Indenture Trustee and puts into question Mr. La Mont's credibility as an expert. Appellant 212 at pgs. 74:22-25 – 76:1-3.

[28] This email was directly contrary to the testimony offered by Mr. Dean at the 507(b) Hearing. *See* Appellant 210 at pgs. 123:9 – 125:12.

the general market decline – *all of which occurred after the Petition Date*[29] – the value of the Timberlands actually *increased* over the course of the bankruptcy case. Mr. La Mont reached this flawed conclusion by simply increasing the discount rate for his Petition Date valuation by 1% (thus resulting in a decrease in value of the Timberlands as of the Petition Date in the amount of $60 million).[30] Appellee 276 at ¶¶ 14-16. As justification for assuming this higher discount rate, Mr. La Mont relied on two PowerPoint presentations that were prepared in mid-2008 and which were improperly admitted over the objections of the Indenture Trustee[31] (one of which was actually prepared by the expert retained by the Official Committee of Unsecured Creditors – a co-proponent of the MRC/Marathon Plan). Appellee 276 at ¶¶ 17-18.

Mr. Dean, not surprisingly, agreed with Mr. La Mont's use of a higher discount rate as of the Petition Date. *See* Appellee 275 at ¶ 7. Yet, the Indenture Trustee uncovered another email indicating Mr. Dean's true belief with respect to the discount rate applicable to the Timberlands during the bankruptcy case. That e-mail evidenced a belief that the discount rate had increased – not decreased – since the Petition Date. Specifically, Mr. Dean suggested that a 7% to 8% yield would be appropriate for the Timberlands, and went on to state that "it would have been *lower* 6 months ago [i.e., in early 2007]." Appellant 437 at pg. 2 (emphasis added).

With a similar lack of candor, during the 507(b) Hearing, MRC/Marathon argued that post-petition timber growth in the Timberlands resulted in an *increase* in the total value of the Timberlands post-petition, even though at the Confirmation Hearing Mr. La Mont testified that

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[29] *See* Appellant 38 at ¶ 6. MRC/Marathon's own expert, Mr. La Mont, admitted that general market risk has increased significantly since the Petition Date and that there has been a general market decline. *See* Appellant 212 at pgs. 58:12 – 59:19.

[30] *See* Appellee 276 at pg. 91:13-14 (acknowledging that a 1% change in discount rate amounts to a $60 million difference in value).

[31] The Indenture Trustee objected to the admission of the PowerPoint presentations on the basis that they constitute hearsay. *See generally* Appellant 211, 212.

all of the growth of the timberlands since the Petition Date had been harvested. *See* Appellant 212 at pg. 32:3-21.

In addition, communications between Mr. Dean, Mr. La Mont, Mr. Phillip Tedder (one of Marathon's valuation experts), and MRC/Marathon's lawyers showed that neither MRC nor Marathon believed that the value of the Timberlands had actually increased due to growth. Appellant 429 at pgs. 38-40. In particular, on March 6, 2008, Dr. Jeffery Barrett, then a Vice President of Scopac, filed an affidavit suggesting that the growth of the Timberlands exceeded Scopac's harvest rate. Appellant 455 at pgs 2-4. Because MRC/Marathon were proposing a lower valuation for the Timberlands than that advanced by Scopac at the Confirmation Hearing, they criticized and discredited Dr. Barrett's analysis. Appellant 429 at pgs. 38-40. Later, when responding to the Indenture Trustee's 507(b) Motion, MRC/Marathon tried to rely upon this very same Barrett affidavit, which they had previously attacked, to argue that the Timberlands had increased in value. *See* Appellant 212 at pg. 35:19-24.

However, a March 6, 2008 email from Mr. Dean to various individuals at MRC and Marathon showed that neither MRC nor Marathon truly believed Dr. Barrett's theory that post-petition timber growth produced an increase in value. This March 6, 2008 email stated that Scopac had "harvested almost all the redwood growth for the year" and that "[t]he amount of redwood [Scopac] did not harvest seems quite small to me (7mmbf on a forest with a standing inventory of harvestable [redwood] of something like 2 bb board feet?) So we are talking about 0.35%? Seems to me like that would be close to the margin of error for estimating what the forest is producing." Appellant 429 at pg. 39. The "bottom line" was that Scopac had "removed almost 100% of the growth of the redwood timber for the year."[32] In response to Mr. Dean's

[32] Mr. Dean did state that a "[s]ignificant" amount of Douglas fir had been added to the forest. However, this additional growth did not produce any additional value because the market value of Douglas fir, as found by the

email, Mr. Tedder reaffirmed Mr. Dean's assertion that all of the growth in the forest had been harvested.[33] Appellant 429 at pgs. 38-39. Likewise, Mr. La Mont never responded to this email to suggest that Mr. Tedder's analysis was somehow flawed or incorrect. This behavior was in line with what Mr. La Mont had told the Bankruptcy Court several months previously: that, according to his analysis, the 2007 harvest of the Timberlands consumed all of the 2007 growth of the Timberlands. *See* Appellant 212 at pgs. 31:22-:33:10; Appellee 279 at pg. 35. Yet, MRC/Marathon urged the Bankruptcy Court to include an increase in value from the growth in the forest when making its Section 507(b) value determination.

All of the above demonstrates the character of the "evidence" that the Bankruptcy Court relied upon to determine that the value of the Timberlands was $510 million on the Petition Date.

Based on the forgoing, the evidence presented at the 507(b) Hearing clearly established that: (i) the testimony of Mr. Dean and Mr. La Mont should have been disregarded for purposes of the 507(b) Motion due to their lack of credibility and candor with the Bankruptcy Court; (ii) according to Marathon's and MRC's own documents and admissions, the value of the Timberlands was well over $668 million as of the Petition Date; and (iii) Mr. Fleming's appraisal conservatively valued the Timberlands at $646 million as of the Petition Date. Thus, because the Bankruptcy Court valued the Timberlands at $510 million as of the Confirmation Date there was a post-petition diminution in value for the Timberlands of at least $136 million.

Bankruptcy Court in its Findings and Conclusions, was less than the costs of harvesting it. Appellant 429. Similarly, any growth of hardwoods in the forest had to be discounted because hardwoods had "no economic value." Appellant 429 at pgs. 39-40.

[33] Mr. Tedder also agreed that there had been Douglas fir and hardwood growth which "currently have no value when logging costs and the market are considered." Appellant 429 at pgs. 38-39.

2. The Bankruptcy Court Improperly Relied on Data and Information that was Unavailable on the Petition Date.

When valuing assets as of a particular date, it is a well-settled principle that hindsight should not cloud the mind of the appraiser. *See, e.g., In re Heritage Org., L.L.C.*, 375 B.R. 230, 284 (Bankr. N.D. Tex. 2007) (holding that valuations should be accomplished "without the benefit of hindsight"); *WRT Creditors Liquidation Trust v. WRT Bankruptcy Litig. Master File (In re WRT Energy Corp.)*, 282 B.R. 343, 383 (Bankr. W.D. La. 2001) (holding that the "use of hindsight is inappropriate in determining the value of assets at a particular point in time").

To resist the temptation of hindsight valuation, bankruptcy courts commonly apply the "snap shot" approach when making determinations of insolvency, an analogous instance when bankruptcy courts look backwards in time to draw conclusions about valuation:

> The better approach, when possible, is to base the determination of insolvency on some form of seasonal appraisal of the assets. *See, e.g., In re Roblin Indus.*, 78 F.3d at 38; *In re Lamar Haddox*, 40 F.3d at 121–22. Although appraisals are not the exclusive or dispositive means for determining fair value, they do afford a court a more accurate snapshot of the market value of those assets at the time and under the circumstances when a debtor files in bankruptcy. *See, e.g., In re Roblin Indus.*, 78 F.3d at 38 (opining that appraisal is the better approach to determine fair valuation).

In re Zeta Consumer Prods. Corp., 291 B.R. 336, 347 (Bankr. D.N.J. 2003).[34] Reliance on improper "hindsight" information necessarily results in clear error because any factual findings arise from application of the wrong legal standard.

[34] By analogy, courts undertake a "look-back" valuation \when determining whether "reasonably equivalent value" was received. *Peltz v. Hatten*, 279 B.R. 710 (D. Del. 2002), *aff'd*, 60 Fed. App'x 401 (3d Cir. 2003) (denying the trustee's offered DCF-based valuation opinions and stating "[w]hile the Liquidating Trustees' experts' views about the growth prospects for CT Tel may in hindsight be accurate, their views alone do not convince the court that at the time of the transaction, [the debtor's] contemporaneous DCF studies that supported the $68 million price were unreasonable"); *In re WRT Energy Corp.*, 282 B.R. at 383 (finding that the fact that the properties did not actually contain the expected amount of oil and gas at the point of valuation did not bear on the parties' valuation of those properties); *Krommenhoek v. Natural Res. Recovery, Inc. (In re Treasure Valley Opportunities, Inc.)*, 166 B.R. 701, 704 (Bankr. D. Idaho 1994) ("Subsequent appreciation or depreciation should not, and does not, transform a transfer for reasonably equivalent value into a fraudulent transfer.").

Here, however, the Bankruptcy Court accepted the testimony of Messrs. Dean and La Mont notwithstanding their reliance on discount rate data, harvest rate data, and pricing information, that was not available as of the Petition Date. Appellee 276 ¶¶ 13-30.[35] In particular, Mr. La Mont relied on two PowerPoint presentations to support his conclusion that discount rates had declined over the course of the bankruptcy case, and that, as a result, the value of the Timberlands may have increased. Appellee 276 at ¶¶ 17-18. These PowerPoint presentations, however, were not even created until mid-2008. Appellee 280 and 282. Further, in arriving at his discount rate for purposes of determining the value of the Timberlands on the Petition Date, Mr. La Mont also considered several allegedly comparable sales which did not occur until after the Petition Date. Appellee 344.

With respect to the timber harvest rates used for purposes of his Petition Date analysis (which generate the projected income to which the discount rates are applied), Mr. La Mont used an arbitrarily low starting harvest rate of 60 million board feet ("MBF"). *See* Appellant 211 at pgs. 374:16 – 376:23. As of the Petition Date, however, Scopac was expecting to harvest approximately 100 MBF for 2007. Appellant 15 at p. 2[36] Thus, there was no reason to believe, and no evidence to support, Mr. La Mont's use of dramatically lower harvest rates as of the Petition Date. Ironically, even as late as November 2007, Mr. La Mont, while he was preparing a business plan for Scopac on Marathon's behalf, projected an initial harvest rate for Scopac of 78 MBF. *See* Appellant 211 at pgs. 373:17 – 374:15. Thus, it was only after Marathon proposed a plan designed to "tap" into Scopac's equity and to "bolster their collateral position" that Mr. La Mont's harvest rate projections suddenly dropped. Appellant 437 at pg. 2.

[35] In fact, Mr. La Mont admitted that, in determining a valuation as of the Petition Date, he used information to which he did not have access on the Petition Date. *See* Appellant 212 at pg. 111:7-13.

[36] Historically, Scopac had harvested 145 MBF in 2005 and 99 MBF in 2006. Appellant 251 at pg. 4.

MRC/Marathon also offered a valuation model developed by Sandy Dean, MRC's CEO. Mr. Dean's testimony relied on a projected harvest rate of 55 MBF as of the Petition Date and was entirely inconsistent with the position he had taken only a few months before the Petition Date. In particular, in April 2006 – when MRC was considering acquiring the Debtor's assets– Mr. Dean made the following observations:

> As we discussed, we think a reasonable starting cost structure is 200 per MBF of non-log and haul expenses, and a 5 mm cap ex number per year, and **a 90 mm foot harvest rate. We would expect after 5 years the harvest rate could rise modestly, perhaps to 100 mm, and then be set as a function of percent of inventory**.

See Appellant 417 at pg. 672.[37] Thus, had Mr. Dean's included only information that was available to him as of the Petition Date, there is no reason to believe that Mr. Dean would have used anything other than 90-100 MBF – approximately the same as what Scopac was projecting over that same time period.

Finally, Mr. La Mont assumed a decline in log prices for purposes of his Petition Date valuation analysis. *See* Appellant 211 at pgs. 389:12-15, 390:17-20. Notwithstanding this assumed decline in log prices, the evidence adduced at the 507(b) Hearing proved that with respect to the multiple timberland appraisals that Mr. La Mont conducted for other clients in December of 2006, *he assumed flat log pricing*. *See* Appellant 211 at pgs. 391:3 – 392:4. Thus, by using an inconsistent assumption of log price declines in his Petition Date valuation analysis, Mr. La Mont artificially depressed the Timberlands' value as of the Petition Date and artificially skewed his estimate of the post-petition change in value of the Timberlands.[38]

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[37] At the Confirmation Hearing, Mr. La Mont testified that his harvest rates were based upon what a potential purchaser (i.e., MRC) would harvest with respect to the Timberlands and not on what was actually sustainable. As evidenced by Mr. Dean's April 2006 email (Appellant 417 at pg. 672), however, MRC's business philosophy was much different pre-petition than post-petition.

[38] Contrary to Messrs. Dean and La Mont, Mr. Fleming considered only information and data that was relevant and available at the Petition Date.

By accepting the positions advanced by Messrs. Dean and La Mont and by failing to consider only the market data and future projections available as of the Petition Date in connection with the 507(b) Claim, the Bankruptcy Court erred as a matter of law.

F. The Bankruptcy Court Erred In Failing to Judicially Estop MRC/Marathon From Arguing That There Was No Decline in the Value of the Timberlands Between the Petition Date and the Confirmation Hearing.

The doctrine of judicial estoppel is designed to protect the integrity of the judicial process by "prohibiting parties from deliberately changing positions according to the exigencies of the moment." *United States v. McCaskey*, 9 F.3d 368, 378 (5th Cir. 1993). In 2001, the Supreme Court addressed judicial estoppel in *New Hampshire v. Maine*, 532 U.S. 742 (2001), listing three factors that courts may consider in their discretion in applying the doctrine: (1) the party asserted "clearly inconsistent" positions; (2) the party successfully persuaded a court to accept its earlier position; or (3) the party seeking to assert an inconsistent position would derive an unfair advantage or impose an unfair detriment on the opposing party if not estopped. *See id.* at 750–751. The Supreme Court, however, did not "establish inflexible prerequisites or an exhaustive formula for determining the applicability of judicial estoppel." *Id.* at 751. Instead, only the first factor is mandatory, and "[a]dditional considerations may inform the doctrine's application in specific factual contexts." *Id.* at 751.

1. MRC/Marathon Took Clearly Inconsistent Positions.

As described above, MRC/Marathon took "clearly inconsistent" positions in the Confirmation Hearing and the 507(b) hearing. In support of their efforts to confirm the MRC/Marathon Plan, MRC/Marathon presented, and advocated that the Bankruptcy Court rely upon, the expert testimony of Mr. La Mont and his opinion regarding the negative impact on value of a substantial post-petition drop in log prices. During the Confirmation Hearing, when confronted with the much higher value testimony proffered by both Scopac and the Indenture

Trustee, MRC/Marathon argued that their expert properly considered a decline in log prices that followed on the heels of the sub-prime loan and liquidity crisis and a significant drop in housing construction. *See* Appellant 113 at 8–9. For example, MRC/Marathon argued that:

- One of the Indenture Trustee's expert witnesses had testified "since the September 2007 valuation, that the housing market has softened, the construction is down, and that . . . the housing markets generally have deteriorated and that the debtor's business has generally suffered due to a severe liquidity crisis." Appellant 202 at 105:24-106:4;
- ". . . numerous testimonies from many of the experts in this case that the price of redwood, especially young redwood, has gone down significantly, 10 to 15 percent during the last several months since the real estate recession . . . has taken hold in the United States." *Id.* at 106:5-9;
- There had been a significant decline in log prices since October 1, 2007. *See* Proposed Findings (as defined and discussed below);
- That one of the Indenture Trustee's expert witnesses' analysis was flawed because his valuation was conducted in October 2007, "prior to when the . . . pricing came down . . . in the marketplace." Appellant 202 at 114:22-24.

MRC/Marathon presented this testimony for two purposes: one, to justify paying less than $530 million to the Indenture Trustee under their plan; and two, to undercut the testimony of the Indenture Trustee's expert, whose opinion Mr. La Mont criticized for not taking into account a 10% to 15% decline in log prices after October 1, 2007. This decline in prices, as found by the Bankruptcy Court in connection with Mr. Fleming's valuation, resulted in a drop in value during the pendency of the case of $100-$150 million.

Yet, at the 507(b) Hearing MRC/Marathon completed contradicted their prior position when they argued that not only had there been no post-petition decline in the value of the Timberlands, there had actually been an *increase* in the value post-petition.

2. The Bankruptcy Court Accepted MRC/Marathon's Argument that the Value of the Timberlands Had Declined Between October 2007 and the Confirmation Hearings.

The Bankruptcy Court indisputably "accepted" MRC/Marathon's position when it made the findings proposed by MRC/Marathon quoted above, including that there had been a 10%–15% decline since October 1, 2007 in log prices, which Mr. La Mont's analysis accounted for but Mr. Fleming's analysis did not (Appellant 113 at ¶¶ 111, 156–58); and that "the same reduces Fleming's valuation by $100–$150 million" (Appellant 113 at ¶ 158). *See In re Ark-La-Timer Co., Inc.*, 482 F.3d 319, 332 (5th Cir. 2007).

Indeed, the Bankruptcy Court's Findings and Conclusions on these points virtually mirror those proposed by MRC/Marathon (the "MRC/Marathon Proposed Findings"). Appellant 103. The following chart highlights the manner in which the Bankruptcy Court's Findings and Conclusions regarding the substantial post-petition drop in log prices and value were taken almost verbatim from the MRC/Marathon Proposed Findings:

BANKRUPTCY COURT FINDING	MRC/MARATHON PROPOSED FINDING
¶ 111 In the last six months, log prices have dropped significantly by as much as 10%-15%, particularly in young growth redwood. (Tr. 4/8/08 258:13-258:258:22; [MMX 85, MMX 86]. Likewise, Douglas fir prices are at an all-time low. (Tr. 4/8/08 350:18-350:25). This decrease in log prices is attributable to the economic slowdown, particularly in the housing market, which has resulted in a decline in building and remodeling activity. (Tr. 4/8/08 258:23-259:5) [MMX 1 ¶ 78; MMX 4 ¶ 25]. Mr. La Mont's analysis accounts for this decline in pricing (Tr. 257:25-258:22); [MMX 4 (La Mont's Report at 38)]	¶ 111 In the last six months, log prices have dropped significantly by as much as 10%-15%, particularly in young growth redwood. (Tr. 4/8/08 258:13-258:258:22; [MMX 85, MMX 86]. Likewise, Douglas fir prices are at an all-time low. (Tr. 4/8/08 350:18-350:25). This decrease in log prices is attributable to the economic slowdown, particularly in the housing market, which has resulted in a decline in building and remodeling activity. (Tr. 4/8/08 258:23-259:5) [MMX 1 ¶ 78; MMX 4 ¶ 25]. Mr. La Mont's analysis accounts for this decline in pricing (Tr. 257:25-258:22); [MMX 4 (La Mont's Report at 38)]

¶ 134 Mr. La Mont is a credible witness whose testimony deserves significant weight, and whose conclusions are given great weight by the Court.	¶ 134 Mr. La Mont is a credible witness whose testimony deserves significant weight, and whose conclusions are accepted by the Court.
¶ 156 Log prices have dropped significantly from October 1, 2007, through the present by as much as 10%-15%, particularly in young growth redwood.	¶ 158 Log prices have dropped significantly from October 1, 2007 through the present by as much as 10%-15%, particularly in young growth redwood.
¶ 157 Despite the considerable drop in log prices during the 6-month period from October 1, 2007, through the present time, Mr. Fleming made no efforts to update his findings to reflect the value of the Timberlands during this time. (Tr. 4/10/08 37:15-37:18, 95:4-95:14). He did not know that redwood prices have declined since October 1, 2007, the date of his appraisal. (Tr. 4/10/08 38:9-38:12).	¶ 159 Despite the considerable drop in log prices during the 6-month period from October 1, 2007 through the present time, Mr. Fleming has made no efforts to update his findings to reflect the value of the Timberlands during this time. (Tr. 4/10/08 37:15-37:18, 95:4-95:14). He was not even aware that redwood prices have declined since October 1, 2007, the date of his appraisal. (Tr. 4/10/08 38:9-38:12).
¶ 158 Changing only this one price of this one type of log to $800-$850/MBF and keeping all other aspects of Fleming's report the same reduces Fleming's valuation by $100-$150 million, dropping his fair market value of the timberlands from $605 million to $452 million. (Tr. 4/8/08 264:6-264:19).	¶ 160 Changing only this one price of this one type of log to $800-$850/MBF and keeping all other aspects of Fleming's report the same reduces Fleming's valuation by $100-$150 million, dropping his fair market value of the timberlands from $605 million to $452 million. (Tr. 4/8/08 264:6-264:19).

¶ 163 Mr. Fleming's analysis has significant flaws including . . .the failure to account for the recent and significant decline in redwood and Douglas fir prices. . . .	¶ 165 Mr. Fleming's analysis has significant flaws including . . .the failure to account for the recent and significant decline in redwood and Douglas fir prices. . . .
¶ 206 [T]he price of redwood has experienced a recent decline due to the slowdown in the economy and the presence of competitor products on the market. (Tr. 4/30/08 309:17-309:20; Tr. 4/8/08 258:13-259:5); [MMX 4 ¶ 25]. This is significant because a likely buyer of the timberlands will look at a short-term business cycle in evaluating log prices. (Tr. 5/1/08 157:18-157:25). As Mr. Yerges concedes, his inflated price increase results in a $150-$200 million increase in his valuation price. (Tr. 4/30/08 306:13-307:8; Tr. 5/1/08 158:10-158:13).	¶ 208 [T]he price of redwood has experienced a recent decline due to the slowdown in the economy and the presence of competitor products on the market. (Tr. 4/30/08 309:17-309:20; Tr. 4/8/08 258:13-259:5); [MMX 4 ¶ 25]. This is significant because a likely buyer of the timberlands will look at a short-term business cycle in evaluating log prices. (Tr. 5/1/08 157:18-157:25). As Mr. Yerges concedes, his inflated price increase results in a $150-$200 million increase in his valuation price. (Tr. 4/30/08 306:13-307:8; Tr. 5/1/08 158:10-158:13).

3. MRC/Marathon Obtained An Unfair Advantage.

MRC/Marathon incontrovertibly derived an unfair advantage by arguing inconsistent positions at the Confirmation Hearing and 507(b) Hearing. In particular, at the Confirmation Hearing, MRC/Marathon advanced the argument that there had been a substantial decline in the value of the Timberlands in order to persuade the Bankruptcy Court to confirm their Plan which would pay the Noteholders substantially less than what was owed to them under the Notes. The findings highlighted above regarding the post-petition decline in value clearly played a crucial role in the Bankruptcy Court's conclusion that the fair market value of the Timberlands was no more than $510 million. Appellant 113 at pgs. 61, 113–14.

Once the Bankruptcy Court announced its intention to confirm the MRC/Marathon Plan and announced its Findings and Conclusions in support of such confirmation, it became apparent that the 507(b) Motion filed by the Indenture Trustee would be problematic - in large part

because of the Bankruptcy Court's value findings. MRC/Marathon found themselves in a bind, faced with the Indenture Trustee's superpriority administrative claim that found conclusive support in the very post-petition diminution arguments that MRC/Marathon had zealously and successfully advocated at the Confirmation Hearing. Thus, at the 507(b) Hearing, MRC/Marathon argued that the Timberlands had *increased* in value over the course of the bankruptcy case. Such a flagrant adoption of inconsistent positions for purposes of gaining an unfair advantage after having previously prevailed in the prior position is precisely what the doctrine of judicial estoppel prohibits. *See New Hampshire v. Maine,* 532 U.S. 742, 750-51 (2001) ("The purpose of the judicial estoppel is to protect the integrity of the judicial process"). Appellant 119 at pgs. 25-33.

Based on the forgoing, the Bankruptcy Court should have found that MRC/Marathon were judicially estopped from asserting that the value of the Timberlands had not declined post-petition and erred as a matter of law by considering the contradictory valuation evidence presented by MRC/Marathon.

G. The Noteholders' Interest in the Cash Collateral Decreased from the Petition Date to the Confirmation Date.

In addition to the diminution of the Timberlands' fair market value between the Petition Date and the Confirmation Date, the Indenture Trustee's cash collateral was depleted significantly during the pendency of the case.

1. "Change in Business" Losses

Palco was originally contractually obligated to advance the costs for the logging, felling and hauling of timber it purchased from Scopac. Appellant 446 at pgs. 2-7. Palco was also required to pay Scopac for the logs (less a reimbursement for harvest costs) shortly after their delivery to Palco's "log deck." Appellant 446 at pgs. 2-3. In August 2007, however, over the

Indenture Trustee's objection, the Bankruptcy Court, at the request of Scopac on less than a week's notice, permitted Palco to alter this contractual relationship to Scopac's detriment to help Palco (a separate debtor) deal with its financial difficulties.[39] Under this drastically different financial arrangement, Scopac paid upfront in cash for the costs of harvesting the timber rather than Palco financing all costs of harvesting. These payments were made using the cash collateral of the Indenture Trustee. However, instead of selling the logs immediately to Palco, Scopac began for the first time to warehouse the logs in a newly created "Scopac log deck" pending a decision by Palco about whether Palco would purchase them in the future. This deprived Scopac of incoming cash causing it to further exhaust the Indenture Trustee's cash collateral.

Prior to this new method of doing business, Scopac was operating on a cash flow positive basis (albeit without making payments on the Notes). After this change in business, however, Scopac's cash position deteriorated precipitously causing a severe drain on Scopac's cash reserves and creating a large post-petition administrative claim of Scopac against Palco for log deliveries that Palco was unable to pay for (a claim that was subject to the Indenture Trustee's lien).[40] Appellant 134 (Attachment #2) at § 4.10.2.

2. Payment of BofA Interest and Professional Fees and Payment to the Indenture Trustee's Professionals

As explained above, after determining that the value of the Cash Collateral as of the Petition Date was approximately $48.7 million and then subtracting the approximately $36 million owed on account of BofA's principal, there was approximately $12.5 million in Cash Collateral as of the Petition Date that should have been provided to the Indenture Trustee.

[39] No final order approving this change in business was ever entered by the Bankruptcy Court.

[40] Not surprisingly, MRC was very complimentary of this "sleight of hand" of getting Scopac to pay for logging and inventory costs. *See* Appellant 437.

At the 507(b) Hearing, MRC/Marathon contended that, to the extent that such Cash Collateral was used to pay postpetition attorneys' fees and interest to BofA and the Indenture Trustee's professionals, such amounts should not "count" as part of any diminution.[41] In the case of BofA, MRC/Marathon's argument ignores the fact that, had the Indenture Trustee been allowed to foreclose at the outset of the case, the substantial post-petition fees and interest paid to BofA would not have accrued or been paid because the cash and cash equivalents of $46 million that existed on the Petition Date could have been used to pay the $36 million in principal owed to BofA, leaving $12.5 million to fund operations pending the sale of the Timberlands to a new operator. This amount would have been more than adequate, since the evidence was clear that without the drain of the massive professional fees incurred in Scopac's chapter 11 case, Scopac was cash flow positive. *See* Appellant 18 at pg. 6.

Similarly, the Indenture Trustee itself would not have incurred the approximately $8.9 million in its own professional fees that accrued over the eighteen months of active participation and frequent, often intense, litigation in this case. The $8.9 million should not have been deducted from the $12.5 million, because the $8.9 million was paid from proceeds of the Indenture Trustee's collateral, to which the Indenture Trustee would have been entitled in any event, and not from unencumbered assets. Hence, the Bankruptcy Court's deduction of the $8.9 million from the $12.5 million essentially charged Noteholders twice for the same $8.9 million payment: once, when $8.9 million of collateral proceeds was used to pay this amount, and again when $8.9 million was deducted from $12.5 million. Had the $8.9 million not been paid: (x) there would have been $8.9 million more in encumbered current assets (i.e., $57.6 million, rather than $48.7 million); and (y) deducting the $36.2 million for Bank of America from the $57.6

[41] Approximately $8.9 million accounted for fees paid to the Indenture Trustee's professionals as of June 2008. Appellant 445 at pgs. 4-5.

million would have left a balance of $20.4 million for the Indenture Trustee. So, in that scenario, the Indenture Trustee would have been entitled to the entire $20.4 million. By holding that the single payment of $8.9 million to Noteholders reduced their entitlement from this amount to $3.6 million, the Court double counted the $8.9 million. This was clearly erroneous.

3. The Bankruptcy Court Failed to Account for the Use of the Indenture Trustee's Collateral to Fund Payment to Estate Professionals

In addition to the payment of professional fees incurred by the Indenture Trustee and BofA, Scopac's estate expended approximately $18 million of the Indenture Trustee's collateral to pay its own professional fees as well as those of the Unsecured Creditors Committee incurred during the period between the Petition Date and June 27, 2008. Appellant 449 at pgs. 3-4. This expenditure of cash collateral was not accounted for in any way by the Bankruptcy Court.

The Bankruptcy Court's analysis of the Indenture Trustee's claim for diminution in value of its non-Timberland collateral consisted entirely of comparing the amount of other current assets, net of the BofA claim as of the Petition Date, to the amount of the same current assets, net of the BofA claim as of the Confirmation Date. Appellant 213 at pgs. 26:20 – 28:18. The legal error in this analysis is that it ignores the $29.7 million in operating income that Scopac generated during the 16 months it was under bankruptcy protection. Appellant 118 at pg. 6. Scopac's operations generated cash that was subject to the Indenture Trustee's liens; however, nearly all of this cash was burned up paying non-Indenture Trustee professionals who received cash of approximately $18 million prior to the Confirmation Date. Appellant 211 at pgs. 237:13 – 238:5. Absent payment of these professional fees and expenses, the Indenture Trustee's collateral would have been approximately $18 million higher.

Because the expenditure of the Indenture Trustee's cash collateral to pay estate and other professionals during the course of the case was not accounted for in any way by the Bankruptcy

Court, the Indenture Trustee was forced to finance all of the professional fees paid during the bankruptcy case without receiving any compensation. As several courts have noted, "parties subjected to loss and expense as a result of the administration of a bankruptcy estate are entitled to be made whole as a matter of fundamental fairness and should be allowed an administrative claim to implement that result." *See Brandt v. Lazard Freres & Co., L.L.C. (In re Healthco Int'l, Inc.)*, 310 F.3d 9, 13 (1st Cir. 2002); *Tama Beef Packing, Inc.*, 283 B.R. 274, 276 (Bankr. N.D. Iowa 2002); *In re Hildebrand*, 205 B.R. 278, 286 (Bankr. D. Colo. 1997); *In re G.I.C. Gov't Secs., Inc*., 121 B.R. 647 (Bankr. M.D. Fla. 1990) (analyzing *Reading Co. v. Brown*, 391 U.S. 471, 483 (1968)).

The Indenture Trustee has been subject to loss as a result of the administration of the bankruptcy case and it would be fundamentally unfair to require the Indenture Trustee to finance the actual and necessary professional fees incurred in an effort to preserve the bankruptcy estate without being made whole.[42] *See In re Hildebrand*, 205 B.R. 278, 286 (Bankr. D. Colo. 1997). These costs clearly represent administrative expenses consistent with this overriding policy of bankruptcy law. Consequently, the Bankruptcy Court erred by failing to compensate the Indenture Trustee for these losses.

[42] To illustrate the inequity that results by not compensating the Indenture Trustee for the $18 million loss of its collateral, assume that this collateral had not been used to pay professional fees but rather was used to build up an uninsured $18 million log inventory that was lost due to fire during the pendency of the case. Under either scenario, the Indenture Trustee would be in the exact same position - $18 million of its collateral would have been burned up. That the Debtor might have still generated enough income during the pendency of the bankruptcy case to offset this loss and bring its cash balances to where they have been before the loss does not negate the fact that $18 million in collateral was destroyed and that the Indenture Trustee would be entitled to an administrative claim for these losses. *See In re Stembridge*, 287 B.R. 658, 669, n.34 (Bankr. N.D. Tex. 2002) (noting that if, postpetition, "collateral is uninsured and lost through fire or theft, an independent obligation to the secured creditor may arise"). It is irrefutable that the Indenture Trustee lost $18 million in collateral that was being used by the Debtor during the pendency of the case. It should not matter whether the loss was on account of fire, payment of professional fees, or otherwise.

III. The Indenture Trustee's Administrative Expense Claim Arose from the Imposition of the Automatic Stay, Scopac's Use of Its Collateral, and the Bankruptcy Court's Cash Collateral Orders.

To have a 507(b) claim, a claimant must first have been granted adequate protection. As demonstrated above, the Bankruptcy Court awarded adequate protection for the Indenture Trustee's interest in both the Cash Collateral and the Pre-Petition Collateral, which included the Timberlands.

Second, a 507(b) claimant must also possess an administrative expense claim under section 503(b). Section 503(b) provides that an administrative expense exists for "the actual, necessary costs and expenses of preserving the estate." 11 U.S.C. § 503(b)(1). The cash collateral orders determined that the use of the Indenture Trustee's cash collateral was a necessary expense of preserving the estate. Scopac used its cash collateral to fund operations, to pay employees and trade creditors, and to pay millions of dollars of professional fees during the case. The Second Final Cash Collateral Order states specifically that:

> The use of Cash Collateral to the extent authorized by this Order is in the best interest of, and will benefit, Scopac, its creditors and its estate. Scopac's ability to operate its business and have any realistic prospect to reorganize depends upon its access to financing. The relief requested in the Motion is necessary, essential and appropriate for the preservation of Scopac's estate and the operation of its business.

Appellant 32 at ¶ 22 (emphasis added).

Scopac retained control of the Timberlands as an essential part of its attempt to reorganize. Accordingly, Scopac's use of both the cash collateral and the Timberlands gave rise to expenses that were necessary for the preservation of Scopac's estate, and the Bankruptcy

Court's prior orders provided the measure of that claim.[43] As such, the Indenture Trustee satisfied the second element required to have a section 507(b) claim.

Finally, to qualify as a section 507(b) claim, an administrative expense claim must arise either from: the automatic stay under section 362; the use, sale or lease of the collateral under section 363; or from the granting of a lien under section 364(d). The Indenture Trustee's 507(b) claim arises from both the imposition of the stay and the use of its collateral.

The automatic stay precluded the Indenture Trustee from exercising its rights under the Indenture[44] and permitted Scopac, beginning in January of 2007, to maintain its ownership and use of the Timberlands and the Indenture Trustee's other collateral, including, as demonstrated above, cash collateral. During the course of the bankruptcy case, log prices declined significantly and, as a result, the value of the Indenture Trustee's collateral declined dramatically. Appellant 379-382. Because the Timberlands declined in value as the result of "market forces" during the course of the case, that diminution in value of the property attributable to and necessary for the operation of Scopac's business entitled the Indenture Trustee to a superpriority administrative expense claim for that loss. *See In re Callister*, 15 B.R. 521, 533 (Bankr. D. Utah 1981) (concluding that the diminution in value resulting from market forces should be borne by the estate because the restraint on liquidating the property was imposed on behalf of the estate). In addition, while the bankruptcy case was pending, Scopac depleted the Indenture Trustee's cash collateral through the payment of professional fees. Appellant 118.

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[43] Even Marathon's counsel agreed with this contention. *See* Appellant 210 at pg. 75:10-17 ("They certainly are entitled to a super-priority administrative claim for any use of the debtor's collateral. Absolutely. If the debtor uses the collateral, okay, under this order, they should be allowed a super-priority administrative claim. So, if there is any diminution as a result of the use of the collateral . . . they should be allowed a claim."); *see also id.* at pg. 81:22-23 (Marathon's Counsel admitting that "if the debtors do use the collateral, that should result in the diminution claim").

[44] *See* Appellant 269 at Article 7, entitled "Remedies."

In the case of *In re Carpet Center Leasing Co.*, the court found "no indication that [the secured creditor]'s loss was caused by anything other than the imposition of the stay, [the secured creditor's] forbearance from foreclosing, and the continued use of the trucks by Debtor." 991 F.2d at 689. Similarly, in *United Missouri Bank of Kansas City, N.A. v. Federman (In re Modern Warehouse, Inc.)*, 74 B.R. 173 (Bankr. W.D. Mo. 1987), the court stated:

> It is true that the debtor becomes responsible to pay under the plan any amount of pre-confirmation depreciation which is due to its misconduct. But diminution for almost any other imaginable cause must, in contemplation of the purpose of adequate protection to ensure against it, be attributed to the automatic stay within the meaning of § 507(b) . . . .

Id. at 176 (footnote omitted).

Here, the Indenture Trustee's administrative expense claim is attributable to both the automatic stay, pursuant to section 362, and the use of the Indenture Trustee's collateral pursuant to section 363, as well as the terms of the Bankruptcy Court's orders. If not for the automatic stay, the Indenture Trustee would have exercised its rights to obtain possession of its collateral and would not have suffered the consequences of the diminution of the value of its collateral. Similarly, if Scopac had not been permitted, since January 2007, to use the Indenture Trustee's cash collateral, that collateral would not have been expended for the preservation of the estate and to pay millions of dollars in professional fees – it would have gone to the benefit of the Appellants.

Accordingly, the Indenture Trustee satisfied the third and final element and was, thus, entitled to a section 507(b) claim for the diminution in value of its collateral. The Bankruptcy Court erred by entering an order denying the Indenture Trustee's 507(b) Motion.

CONCLUSION AND PRAYER

For the reasons, and based on the authorities presented above, this Court should reverse the Bankruptcy Court's 507(b) Order and award relief by rendering a judgment that the Indenture

Trustee is entitled to a superpriority administrative expense claim pursuant to 11 U.S.C. § 507(b) in an amount not less than $170 million based upon: (i) the decline in the value of the Timberlands from the Petition Date through the Confirmation Date; and (ii) the use and depletion of Scopac's cash collateral for which the Indenture Trustee received no benefit, and grant such other relief to which the Appellants may be justly entitled.

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