

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

IN RE:	§	
	§	JOINTLY ADMINISTERED
	§	
SCOTIA DEVELOPMENT LLC, ET. AL.,	§	Case No. 07-20027-C-11
Debtors.	§	Chapter 11

**AFFIDAVIT OF GARY L. CLARK IN SUPPORT OF FIRST DAY MOTIONS OF
SCOTIA DEVELOPMENT, LLC, THE PACIFIC LUMBER COMPANY, BRITT
LUMBER CO., INC., SALMON CREEK LLC, AND SCOTIA INN, INC.**

I, Gary L. Clark, declare and state as follows:

**I.
FOUNDATION**

1. I am the Vice President of Finance & Administration and Chief Financial Officer of Scotia Development, LLC (“Development”), The Pacific Lumber Company (“PALCO”), Britt Lumber Co., Inc. (“Britt”), Salmon Creek LLC (“Salmon Creek”), and Scotia Inn, Inc. (“Scotia Inn”), debtors and debtors in possession, (herein “Debtors”).

2. In my capacity as the Vice President of Finance & Administration and Chief Financial Officer of the Debtors, I am required to and have become generally familiar with the manner in which Debtors’ documents, books and records are prepared and maintained. Debtors maintain records of all their transactions in the regular course of business, and it is the regular course of business to create and maintain such records.

3. I submit this Supplemental Affidavit in support of Debtors’ petitions for relief under chapter 11 of title 11 of the United States Code, 11 U.S.C. §§ 101-1330 (the “Bankruptcy Code”), and Debtors’ First Day Pleadings (as defined below). I am authorized to submit this Affidavit on behalf of Debtors.

4. Except as otherwise indicated, all statements in this Affidavit are based on my personal knowledge, my review of relevant documents or my opinion based upon my experience and knowledge of Debtor's business operations and financial condition. If I were called upon to testify, I could and would testify to each of the facts set forth herein based on such personal knowledge, review of the documents or opinion

**II.
THE DEBTORS' BANKRUPTCY FILING**

5. On January 18, 2007 (the "Petition Date"), each of the Debtors filed a separate voluntary petition under Chapter 11 of the Bankruptcy Code in the above-captioned Court¹ The Debtors continue to manage and operate their respective businesses and properties as debtors in possession pursuant to Sections 1107 and 1108 of the Bankruptcy Code. No trustee has been appointed in the case of any Debtor.

**III.
DESCRIPTION OF THE DEBTORS**

6. Development, Britt, Salmon Creek and Scotia Inn are wholly owned subsidiaries of PALCO. PALCO, in turn, is wholly owned by MAXXAM Group, Inc. ("MGI"), which is wholly owned by MAXXAM Group Holdings Inc. ("MGHI"), which is wholly owned by MAXXAM, Inc. ("MAXXAM"), a publicly traded company involved in several different industries.

7. The Debtors, who currently have approximately 586 employees in the aggregate, operate in several principal areas of the forest products industry, including the growing and

¹ Another wholly owned subsidiary of PALCO, Scotia Pacific Company LLC ("Scopac"), also filed a Chapter 11 petition on January 18, 2007.

harvesting of redwood and Douglas-fir timber, the milling of logs into lumber and the manufacture of lumber into a variety of finished products²

8. PALCO, which has been in continuous operation for more than 130 years, owns and manages, directly or through its subsidiaries, approximately 210,000 of virtually contiguous commercial timberlands (the “Timberlands”) located in Humboldt County, along the northern California coast, an area which has very favorable soil and climate conditions for growing timber. These Timberlands are located in close proximity to PALCO’s and Britt’s sawmills, and contain an extensive network of roads.

9. Scotia Pacific Company LLC (“Scopac”), PALCO’s largest operating subsidiary, was established in 1993, in conjunction with a securitization transactions pursuant to which the vast majority of the Timberlands were transferred to Scopac, and Scopac issued certain Timber Collateralized Notes (the “Timber Notes”) secured by substantially all of Scopac’s assets, including such Timberlands. Pursuant to a 1998 refinancing transaction, Scopac issued Timber Notes in the aggregate principal amount of approximately \$867 million. The outstanding principal amount of the Timber Notes is approximately \$714 million.

10. Scopac currently owns approximately 200,000 acres of the Timberlands (the “Scopac Timberlands”). Scopac also has the exclusive right to harvest (the “Scopac Timber Rights”) approximately 12,000 acres of Timberlands owned directly by PALCO and Salmon Creek. (The Scopac Timberlands, together with the Scopac Timber Rights, are hereinafter collectively referred to as the “Scopac Timber.”) PALCO harvests and purchases from Scopac virtually all of the logs harvested from the Scopac Timber. Scopac relies on the revenue from

² PALCO also sells energy generated from its cogeneration plant, utilizing wood byproducts from its milling operations. Such sales typically constitute less than 10% of PALCO’s revenue.

such sales to service the Timber Notes, as well as to pay its operating expenses. Such sales from Scopac to PALCO, as well as various related services that PALCO and Scopac provide to each other, are the subject of several agreements between the parties entered into in conjunction with the issuance and sale of the Timber Notes. PALCO arranges for the cutting and hauling (through independent contractors) of the logs it purchases from Scopac, mills the logs into lumber, and sells such lumber for a variety of construction uses.

11. Britt is engaged in manufacturing redwood fencing and decking products from small diameter logs (a substantial portion of which it acquires from PALCO), for sale to retail and wholesale customers. Britt does not own any of the Debtors' timberlands.

12. Salmon Creek was activated as a Delaware limited liability company in 1999 in anticipation of the Headwaters Agreements and, along with PALCO and Scopac, is a party to those Agreements. Most of Salmon Creek's acreage was transferred under the Headwaters Agreements. Because the approximately 1,300 acres it continues to own constitute part of the Scopac Timber, Salmon Creek has very limited operations.

13. Scotia Development was created in 2006 for the purpose of exploring and facilitating development opportunities with respect to commercial, industrial and residential properties, including raw land, in California and Texas. It is party to development contracts with both Scopac and PALCO, and owns option rights to real property on the Texas Gulf Coast.

14. Scotia Inn operates a historic inn in Scotia, California in close proximity to PALCO's headquarters building. It has been closed in recent years and has very limited operations.

15. For more background and a more comprehensive description of the Debtors' business, including the Debtors' independent affiliate Scotia Pacific Company, please see my previously filed affidavit.

**IV.
NEED FOR FIRST DAY PLEADINGS**

16. In order to minimize the adverse effects of this chapter 11 case on Debtors' businesses, Debtors have requested various types of relief in certain "first day" motions and applications (collectively, the "First Day Pleadings"). The First Day Pleadings seek relief to, among other things, maintain employee morale and vendor confidence, ensure the continuation of Debtors' cash management systems and other business operations without interruption, obtain access to cash collateral, and establish certain other administrative procedures to promote a smooth transition to chapter 11.

17. Maintaining the support of Debtors' customers, employees, vendors, service providers and other key constituencies, as well as maintaining the day-to-day operations of Debtors' business with minimal disruption, is crucial to Debtors' successful emergence from chapter 11. I have reviewed each of the First Day Pleadings, including the exhibits thereto, and believe that the facts stated therein are true and correct to the best of my information and belief and that the relief sought in each of the First Day Pleadings is tailored to meet the goals described above and, ultimately, is critical to Debtors' ability to successfully reorganize. The facts underlying each First Day Pleading, together with a brief description of the relief sought, are set forth below. Capitalized terms used but not defined in these descriptions shall have the meaning set forth in the Motions or Applications.

**V.
MOTION TO PAY PREPETITION COMPENSATION AND BENEFITS OF
EMPLOYEES.**

18. In order to continue their operations while in Chapter 11, it is crucial that the Debtors retain their current trained, qualified and experienced work force. Absent authorization from this Court to pay and honor regular pre-petition employee compensation and benefits, the Debtors may lose personnel necessary for a seamless transition and their continuing operations.. Further, over 586 employees will face the uncertainty of a potential interruption of their wages and important benefits necessary to their livelihood.

A. PRE-PETITION COMPENSATION AND BENEFITS

19. The following charts summarize the compensation and benefits for which approval is sought herein.³

Compensation

	PALCO	Britt
Estimated Pre-Petition Salaries and Wages	\$940,948	\$165,301
Number of Employees:	394	106
Average per Employee:	\$2,388	\$1,559
Total Estimated Pre-Petition Salaries and Wages for PALCO and Britt	\$1,106,249	

Benefits

TYPE OF BENEFIT	PALCO ESTIMATED PRE-PETITION AMOUNT UNPAID	BRITT ESTIMATED PRE-PETITION AMOUNT UNPAID
Employer Tax Deductions	\$100,500	\$14,701
Accrued Vacation Payout	\$520,255	\$49,700
Medical Benefits	\$404,414	\$65,000

³ All amounts are approximate.

Flexible Savings Accounts	\$264	\$150
Basic Life/AD&D Insurance	\$8,987	\$915
Long Term Disability Insurance	\$4,828	\$1,575
Short Term Disability Benefits	\$0	\$0
Workers' Compensation	\$9,600,700 (as it is due in ordinary course)	\$739,905
401(k) Plan	\$26,500	\$4,900
Pension Plan	\$20,598,612 (as it is due in ordinary course)	Not offered to Britt employees
Business Expense Reimbursements	\$17,500	\$4,500
Scholarship Program	\$33,000	\$0
Scotia Recreational Center	\$0	\$0

B. THE DEBTORS' WORK FORCE

20. Scotia Development, PALCO, Scopac, Britt and Salmon Creek⁴ currently have approximately 586 employees in the aggregate.⁵ The Debtors' workforce consists of two broad categories: (1) salaried employees ("Salaried Employees") and (2) hourly employees ("Hourly Employees"). Salaried Employees are generally corporate management, administrative and technical staff and mill supervisors and foremen. Hourly Employees are primarily workers engaged in lumber production activities at the Debtors' sawmills or workers engaged in hands-on maintenance of the Debtors' timberlands. These categories are described in more detail below on a company by company basis.

1. PALCO

⁴ Scotia Development, Salmon Creek and Scotia Inn each has officers but has no salaried employees.

⁵71 of those employees (including 8 salaried and 63 hourly employees) are on PALCO's or Britt's payroll only through the end of January pursuant to the federal Worker Adjustment and Retraining Notification ("WARN") Act, and are no longer actually working for any of the Debtors.

21. PALCO has a total of approximately 394 employees working at two primary locations: the headquarters office located in Scotia, California and the sawmill located in Scotia, California (the “Scotia Sawmill”).

a. Salaried Employees

22. PALCO has approximately 75 Salaried Employees. PALCO’s Salaried Employees include senior executives, division superintendents and on-site supervisors and foremen. Approximately 41 Salaried Employees provide the supervision and management required to operate PALCO’s business or fulfill non-supervisory roles that are legally mandated or critical to business operations. Approximately 34 Salaried Employees perform primarily administrative and non-supervisory professional duties. Examples of Salaried Employee classifications at PALCO include Logging Superintendent, Human Resources Director, Supervisor, Purchasing Agent and Plant Services Manager.

b. Hourly Employees

23. Over 80% (approximately 319 employees) of PALCO’s work force is comprised of Hourly Employees engaged in production activities. The majority of PALCO’s production employees work at the Scotia Sawmill. Many of these employees are skilled craftspeople who provide a variety of core services for PALCO, including the operation of specialized equipment such as planers and scales; maintenance of PALCO’s power plant; carpentry; and lumber grading. This group also includes a small number of clerical staff who provide support to the administrative departments of PALCO. Typical job classifications in the production area include Grader, Electrician, Carpenter, Lumber Handler and Clerk.

Some of the skilled craft personnel must meet certain industry certification requirements. These positions typically require approximately one to two years of on-the-job training and experience before employees become fully qualified in all aspects of their jobs.

2. Britt

24. Britt has approximately 106 employees. The majority of Britt's employees work at its sawmill located in Arcata, California (the "Britt Sawmill").

a. Salaried Employees

25. Britt has approximately 7 Salaried Employees who generally provide the management and supervision necessary to operate the company's business.⁶ Salaried Employees also include a small number of non-supervisory employees who perform administrative work necessary for business operations. Typical Salaried Employee classifications include Sawmill Supervisor, Accounting Manager and Foreman. Salaried Employees must have either several years of operational or industry experience, or advanced degrees.

b. Hourly Employees

26. The remaining 99 Britt employees are Hourly Employees who are engaged in production activities. Typical Hourly Employee classifications include Lumber Handler, Grader, Edger Operator and Millwright. These positions typically require approximately one to two years of on-the-job training and experience before employees become fully qualified in all aspects of their jobs.

C. PRE-PETITION EMPLOYEE COMPENSATION AND PAYROLL DEDUCTIONS

27. This section describes the payment of employee compensation and payroll deductions with respect to the employees of each of the applicable Debtors, including amounts accrued pre-petition that the Debtors seek authority to pay pursuant to the Motion.

1. Employee Wages, Salaries and Commissions

a. PALCO

⁶ Although a small number of PALCO's executive management employees also serve as executives for Britt, such individuals are considered PALCO employees for the purposes of the Motion and this MPA. In other words, the definition of a Britt employee in this MPA is an individual solely employed by Britt.

28. PALCO issues payroll checks and direct deposits to its employees on the 10th and 26th days of each month. Payroll checks consist entirely of amounts due for services previously rendered, *i.e.*, wages are paid in arrears. The payroll checks issued on the 10th day of each month cover services rendered from the 16th day to the last working day of the previous month; the payroll checks issued on the 26th day of each month cover services rendered from the first to the 15th day of that month. Thus, certain payroll checks to be issued to PALCO employees after the Petition Date will include amounts due for pre-petition services. It is also likely that at any given time there are some uncashed payroll checks for prior pay periods.

29. PALCO seeks authority to pay outstanding amounts related to compensation of its employees for services provided prior to the Petition Date. PALCO estimates that the pre-petition portion of the payroll checks that are scheduled to be issued on January 26, 2007 and February 10, 2007 aggregate approximately \$940,948, which represents an average amount of \$2,388 per employee.

30. In addition to the foregoing, PALCO maintains an incentive bonus program (the "IBP") for its middle-management and senior-management employees, pursuant to which, on an annual basis, bonuses may be afforded to such qualifying employees based on both quantitative and qualitative performance measures. Under the IBP, such performance benchmarks are established, and the compensation committee of PALCO's board of directors in December of each year authorizes a bonus pool of up to an aggregate dollar amount based on the extent to which the benchmarks have been fulfilled. The senior officers of PALCO then are afforded the discretion to allocate and divide such bonus pool among the qualifying employees based on their individual performance achievements during the calendar year. In light of the Debtors' financial difficulties this past year and the attendant failure to meet the quantitative IBP benchmarks established for 2006, in December 2006 the compensation committee of PALCO's Board of Directors authorized a limited bonus pool (half of the maximum bonus pool amount) based on various qualitative performance criteria having been fulfilled. The senior executives of PALCO then allocated such

authorized bonus pool among the qualifying employees, and, consistent with the IBP program, distributed such bonuses by checks issued in January 2007.

31. These payments in January 2007 under the IBP aggregated approximately \$123,500 divided among 77 qualifying employees, for an average of approximately \$1,604 each. To the extent there are any checks representing these bonus payments for calendar year 2006 made in January 2007 that have not yet fully cleared the check-clearing process as of the Petition Date, PALCO by this motion seeks authority to permit these checks to clear, which effectively means that to the extent any such checks clear after the Petition Date, they will constitute a post-petition payment on account of pre-petition services. PALCO seeks this relief as part of this Motion because although these bonus payments are relatively small in amount, they are an important incentive and reward to the middle- and senior-level management employees who receive them, and are generally viewed by such employees as a meaningful component of their wages.

b. Britt

32. Britt issues payroll checks and direct deposits to its employees on every other Friday. Each payroll check covers services rendered for the two-week period ending on the Sunday preceding each pay date. The first payroll checks to be issued to Britt employees after the Petition Date will include amounts due for pre-petition services. Specifically, the payroll checks to be issued on January 19, 2007 will be in compensation for services rendered pre-petition for the pay period of January 1-14, 2007, and the payroll checks to be issued on February 2, 2007 will include compensation for services rendered pre-petition during the period of January 15-18, 2007. It is also likely that at any given time there are some uncashed payroll checks for prior pay periods.

33. Britt seeks authority to pay outstanding amounts related to compensation of its employees for services provided prior to the Petition Date. Britt estimates that the pre-petition portion of the payroll checks that are scheduled to be issued on January 19, 2007 and February

2, 2007 aggregate approximately \$165,301, which represents an average amount of \$1,559 per employee.

2. Payroll Deductions

34. In the ordinary course of business, in each pay period, each of the Debtors makes deductions from employees' paychecks for obligations such as state income taxes, state disability insurance contributions, federal income taxes and Social Security and Medicare contributions (collectively, "the Payroll Deductions"). The amounts deducted are generally held in trust by the Debtors until they are remitted to the relevant governmental authority. In addition, the Debtors make deductions from employee paychecks for employee contributions with respect to: (i) flexible spending accounts, (ii) 401(k) plans, and (iii) employee directed contributions to other recipients, and (iv) plans for benefits (in excess of those already provided to the employee by the Debtors) for medical, dental, prescription drug and vision coverage, the Employee Assistance Program, life and accidental death and dismemberment insurance coverage, supplemental group term life insurance, and other similar programs, as described in Section IV, *infra*. Typically such contributions to employee benefit plans, once deducted from the employees' paychecks, are remitted by the Debtors to third parties (collectively, the "Benefits Deductions"). As of the Petition Date, the Debtors had collected, but not remitted, certain Payroll Deductions and Benefits Deductions.

35. To the extent that the Debtors are holding funds belonging to employees that are collected from employees and remitted to others, the Debtors maintain that such funds are not property of the estate. However, in an abundance of caution, to the extent that such funds relate to pre-petition periods, the Debtors seek authority to remit to the appropriate governmental authorities and other third parties the applicable Payroll Deductions and Benefits Deductions collected pre-petition, in accordance with the Debtors' regular policies and procedures.

36. The Debtors further seek authority to continue to collect and remit Payroll Deductions and Benefits Deductions, as described herein, in the ordinary course of business and pursuant to existing policies and procedures.⁷

D. PRE-PETITION EMPLOYEE BENEFITS

37. As of the Petition Date, the Debtors are obligated to make certain contributions and provide certain benefits under various employee benefit programs, as described below.⁸

1. Health Benefits

38. The Debtors provide medical, dental, prescription drug, mental health and substance abuse and vision coverage to their employees (the “Health Benefits”), as described below.

a. Medical, Dental and Prescription Drug Coverage

39. The Debtors provide comprehensive medical, dental and prescription drug coverage to all full-time employees beginning on the first of the month following 90 days of service, pursuant to a self-insured plan. Employees pay a flat fee for their own coverage under these plans, and pay additional fees for any desired dependent coverage, as well as certain deductibles and co-payments.

40. Claims for medical and dental benefits are administered through a third party administrator, the Humboldt Del Norte Medical Foundation (the “Foundation”). All employees and dependents covered by the Debtors’ medical plan are automatically covered by the Debtors’ prescription drug plan. Claims for prescription drug benefits are administered by HealthTrans.

⁷ The amounts collected by the Debtors as Benefits Deductions are not included in the calculation of the amounts entitled to priority under Section 507(a)(5) of the Bankruptcy Code, as they constitute the employees’ own funds, as opposed to “claims for contributions to employee benefit plans” within the meaning of that provision.

⁸ PALCO also provides certain “retiree benefits” (within the meaning of Bankruptcy Code Section 1114(a)) to retired employees and their spouses and dependents. PALCO does not seek authority pursuant to this Motion to continue to pay such retiree benefits, as continued timely payment of such benefit is generally required (and thus authorized) pursuant to the terms of the statute. See 11 U.S.C. §1114(e)(1).

41. The Debtors pay the amounts owing for the medical and dental claims not covered by deductibles and co-payments on a weekly basis for the claims that accrued during the previous week. The Debtors pay the amounts owing for prescription drug claims not covered by deductibles and co-payments on a monthly basis for the claims that accrued during the previous month. The Debtors pay the Foundation and HealthTrans on a monthly basis, in arrears, for administrative services provided during the previous month.

b. Employee Assistance Program

42. The Debtors also offer an Employee Assistance Program that provides mental health and substance abuse services to all full-time and regular part-time employees beginning on their first day of employment at no cost to the employee. Community Health Alliance (“CHA”) administers the employee assistance program. CHA is paid on a monthly basis, in arrears, for claims paid the previous month.

c. Vision Benefits

43. The Debtors also offer a vision insurance plan to all full-time employees beginning on the first of the month following 90 days of service at no cost to the employee. Dependent coverage is available for an additional fee. The vision insurance plan is provided by Superior Vision Services, Inc. (“Superior”). Amounts owed to Superior for premiums and administrative fees are paid on a monthly basis, in arrears.⁹

44. The Debtors, by this Motion, seek authority to pay any premiums, claims, fees and other amounts relating to the foregoing Health Benefits that accrued prior to the Petition Date and remain unpaid as of the Petition Date. While it is difficult to state with specificity the amounts remaining outstanding with respect to the foregoing Health Benefits as of the Petition Date, based on previous experience, PALCO estimates its total pre-petition Health Benefits

⁹ Amounts owing for the Employee Assistance Program and vision insurance are paid to CHA and Superior, respectively, by PALCO on behalf of both PALCO and Scopac employees. Scopac then reimburses PALCO on a pro rata basis, based on the number of covered Scopac employees.

liability is approximately \$5,000, and Britt estimates its total pre-petition Health Benefits liability is approximately \$1,000.

2. Flexible Spending Accounts

45. All of the Debtors' employees are eligible to contribute to a health care and/or dependent care flexible spending account ("FSA") through payroll deductions. On an annual basis, employees are permitted to allocate up to \$2,400 of their salaries or wages to the health care FSA and up to \$5,000 to the dependent care FSA, which allocations are deducted from their paychecks by the Debtors. The Debtors then transfer such payroll deductions on a monthly basis to Alt Benefit Consultant, Inc. ("Alt"), which administers these programs.

46. The FSA benefit program is centrally maintained by MAXXAM. MAXXAM pays administrative fees, in arrears, on a monthly basis to Alt. MAXXAM then bills its various subsidiaries, including the Debtors, for their proportionate share of those fees.

47. The Debtors seek authority to continue the FSA benefits program in the ordinary course of business, and to pay amounts billed by MAXXAM for their respective shares of administrative fees for the pre-petition period. PALCO estimates its total pre-petition liability for such administrative fees is approximately \$264, and Britt estimates its total pre-petition liability for such administrative fees is approximately \$150.

3. Life and AD&D Insurance

48. PALCO provides two times an employee's annual salary (rounded up to the nearest \$1,000) of basic group life insurance coverage through Metropolitan Life Insurance Company ("MetLife") to all full-time employees beginning on the first of the month following 90 days of service at no cost to the employee. Accidental death and dismemberment ("AD&D") optional coverage is available for up to five times an employee's annual salary. Britt provides life insurance coverage equal to an employee's annual salary to all full-time employees. Britt provides AD&D insurance coverage provides coverage equal to an employee's annual pay, up to a maximum of \$150,000. AD&D optional coverage is available for up to five times an employee's annual salary. MetLife provides the Debtors' life and AD&D insurance coverage.

49. The Debtors seek authority to continue to provide the life and AD&D insurance coverage described above, and to pay any outstanding premiums related thereto for the period prior to the Petition Date. PALCO estimates the pre-petition liability for such premiums is approximately \$8,987; and Britt estimates the pre-petition liability for such premiums is approximately \$915.

4. Supplemental Group Term Life Insurance

50. The Debtors offer all full-time employees beginning on the first of the month following 90 days of service the option to purchase supplemental group term life and/or AD&D insurance coverage for an additional cost. MetLife provides the Debtors' supplemental group term life and AD&D insurance coverage. The Debtors transfer employees' payroll deductions for premium amounts related to supplemental group term life and/or AD&D insurance to MetLife on a monthly basis. The Debtors seek authority to continue to offer this coverage option to employees in the ordinary course of business.

5. Long-Term Disability Insurance

51. PALCO and Britt each offers its employees long-term disability ("LTD") insurance coverage through Aetna after 12 months of employment, at no cost to the employee. PALCO's LTD plan and Britt's LTD plan each provides benefits to employees who have remained disabled due to illness or injury for at least 180 days. Benefit eligibility continues as long as the employee cannot perform the duties of his or her occupation and the employer is unable to place the employee in a job suited to the employee's reduced work capabilities. PALCO and Britt each pays Aetna on a monthly basis, in arrears, for LTD insurance premiums on behalf of itself for its qualifying employees. PALCO also pays Aetna on a monthly basis, in arrears, for LTD insurance premiums on behalf of Scopac for its qualifying employees participating in a similar LTD plan, and then obtains reimbursement from Scopac for its pro rata share.

52. PALCO and Britt each seeks authority to continue to provide for such LTD insurance coverage to its respective employees in the ordinary course of business and to pay

outstanding premiums related to the foregoing LTD insurance coverage for its respective employees. PALCO also seeks authority to continue to pay outstanding premiums pertaining to Scopac employees, assuming Scopac seeks and obtains Court authority to reimburse PALCO on a prompt ongoing basis for any and all premium payments made for the benefit of Scopac employees) for periods prior to the Petition Date. PALCO estimates its aggregate pre-petition liability for such LTD premiums (including premiums for the benefit of PALCO employees and premiums for the benefit of Scopac employees) is approximately \$4,828, and Britt estimates its aggregate pre-petition liability for such LTD premiums is \$1,575.

6. Short-Term Disability Plan

53. The Debtors offer self-insured, self-administered, short-term disability coverage to all Salaried Employees, at no cost to the employee, after three full months of employment. No such coverage is offered to the Debtors' Hourly Employees. The amount of short-term disability benefits is calculated based on the employee's length of employment and base salary and is coordinated with any payments received through workers' compensation and state disability insurance. Eligible employees may receive benefits for up to six months.

54. The Debtors seek authority to continue their short-term disability coverage for Salaried Employees and to pay any unpaid benefits which accrued prior to the Petition Date. At this time, no PALCO employees are currently receiving benefits under its short-term disability plan.

7. Workers' Compensation Benefits

a. PALCO

55. PALCO is self-insured for workers' compensation liability under state law pursuant to a Certificate of Consent to Self-Insure Workers' Compensation Liabilities in the State of California. Accordingly, PALCO pays the full costs of these benefits. As a condition to its authority to self-insure, the State of California required PALCO to post a letter of credit supporting Its liability.

56. PALCO seeks authority to honor its workers' compensation obligations in the ordinary course of business, and to pay any outstanding claims related to its workers' compensation benefits program for injuries suffered prior to the Petition Date. It is difficult to accurately estimate the total obligations that will remain outstanding under PALCO's self-insured workers' compensation plan. Based on its most recent actuarial calculations, however, PALCO estimates that the total maximum unpaid pre-petition liability for workers' compensation claims is approximately \$9,600,700¹⁰ as of December 31, 2006.¹¹ This amount reflects PALCO's estimated total liability with respect to known injuries suffered prior to the Petition Date, and in the ordinary course of business would be paid out to claimants on a monthly basis over an extended period of time.

b. Britt

57. Britt is insured for workers' compensation claims of up to \$1,000,000 per incident by AIG. Thus, as to any claim that exceeds \$1,000,000, Britt is self insured as to the portion in excess of \$1,000,000.

58. With respect to Britt's workers' compensation insurance, AIG calculates the amounts owing to workers' compensation claimants on a monthly basis. Because MAXXAM as the ultimate parent of a number of operating companies can more efficiently arrange for insurance for a number of its subsidiaries, MAXXAM procures the applicable workers' compensation

¹⁰ While this figure may initially seem high relative to the number of current employees, it must be noted that PALCO has been providing workers' compensation benefits to its employees for decades, and that its current workforce is substantially smaller than it has been historically. Further, in the past, PALCO's operations depended heavily on manual labor and lacked much of the automated machinery available today. In addition, the injuries sustained in this industry tend to be more serious and costly than those sustained in the typical workplace.

¹¹ Upon submittal, claim amounts are estimated in accordance with industry actuarial standards to reflect the anticipated total cost of the injury suffered. The actual amounts paid for any particular claim may be above or below this initial estimate depending on the particular nature of the injury suffered and the applicable recovery time. Amounts outstanding for workers' compensation claims are recalculated and updated at the end of each month to account for such variances.

policy from AIG and AIG is paid premiums and services-based administrative fees by MAXXAM. MAXXAM then bills Britt for its pro rata shares of premiums and administrative fees (just as it bills any other participating subsidiaries for their pro rata share of premiums and administrative fees).

59. Britt seeks authority to continue to provide the workers' compensation coverage described above and to pay in the ordinary course of business any outstanding claims, premiums and administrative fees related to its workers' compensation benefits program that accrued prior to the Petition Date. Britt estimates that its liability for premiums and administrative fees relating to workers' compensation coverage for the pre-petition period is approximately \$610,312. Based on its most recent actuarial calculations, Britt estimates that the total unpaid pre-petition liability for workers' compensation claims was approximately \$739,905 as of December 31, 2006, all or a material portion of will be covered by insurance. This amount reflects the estimated total maximum remaining liability with respect to known injuries suffered prior to the Petition Date.

8. Retirement Plans

a. Defined Contribution (401(k)) Plan

60. The Debtors offer a defined contribution ("401(k)") plan for all full-time employees beginning on the first quarter following 90 days of service. Eligible employees may contribute a percentage of their regular pay on a pre-tax basis. PALCO and Britt provide an employer matching contribution of the designated percentage of the employee's base and overtime earnings to employee's 401(k) accounts. The Debtors also provide a contribution for employees (the "Transition Benefit") who were previously eligible under the pension plan described in part H.2. below. The Transition Benefit is a percentage contribution of the employee's regular and overtime pay based on the employee's age. The Debtors deduct contributions from the paychecks of participating employees and remit the employee contributions and employer matching amounts to the plan administrator, Fidelity Institutional Retirement Services Company ("Fidelity"), on a semi-monthly basis.

61. MAXXAM manages the 401(k) plan on behalf of all of its subsidiaries, including the Debtors. MAXXAM pays the amount owing to Fidelity for administrative and maintenance fees on a monthly basis for services provided during the previous month. MAXXAM then bills, on a monthly basis, the portion of fees attributable to each of its subsidiaries, including the Debtors, on a pro rata basis.

62. The Debtors seek authority to continue to honor their 401(k) plans, and to pay any outstanding employer contributions and administrative fees related to the 401(k) plan which accrued prior to the Petition Date. PALCO estimates its total pre-petition liability for employer contributions and administrative fees with respect to its 401(k) plan is approximately \$26,500. Britt estimates its total pre-petition liability for employer contributions and administrative fees with respect to its 401(k) plan is approximately \$4,900.

b. Defined Benefit Pension Plan

63. In addition to the 401(k) plan, PALCO offers its employees a tax-qualified defined benefit plan (“pension plan”) that provides a certain amount of monthly income upon the employee’s retirement, at no cost to the employee. Britt does not offer a pension plan to its employees.

64. Employees become eligible after three months of continuous service or 1,000 hours of service during any consecutive 12-month period, whichever occurs first. Benefits payable under the pension plan are determined based on an employee’s years of service, salary and age at retirement. Funds become vested after five years. The pension plan funds are held in a trust administered by Fidelity Investments, Inc. (“Fidelity Investments”). PALCO pays amounts owing to Fidelity Investments on a monthly basis, in arrears, on behalf of both itself and on behalf of Scopac in connection with its participation in the same pension plan, for contributions for their respective participating employees and for record-keeping and administrative services. Scopac then reimburses PALCO for Scopac's pro rata share. The pension plan was frozen as of December 31, 2005, meaning that while vested benefits are not

affected, there is no accrual of any additional or new benefits. Although no new benefits are accrued, the Debtors continue to have funding requirements.

65. PALCO seeks authority to continue to honor its pension plan obligations and to pay any outstanding contributions and administrative fees related to its participating employees in the pension plan (and, assuming Scopac seeks and obtains authority to reimburse PALCO on a prompt and ongoing basis for all advances made by PALCO on behalf of Scopac related to Scopac's participating employees In the pension plan), in each case which accrued prior to the Petition Date. PALCO's total estimated amount of pre-petition liability for contributions and fees with respect its employees participating in the pension plan is approximately \$20,598,612, and with respect to Scopac's employees participating in the pension plan is zero. Palco is current on this obligation which is paid as it comes due. No payments are budgeted form the first thirty (30) days as no payments are currently due and payable.

9. Employee Business Expense Reimbursements

66. In the ordinary course of business, the Debtors reimburse certain business expenses incurred by employees, including but not limited to business-related travel, meals, telephone, relocation and gas. The Debtors typically reimburse employees for business expenses on an as-needed basis.

67. The Debtors seek authority to pay outstanding amounts related to appropriate business expense reimbursements which accrued prior to the Petition Date. The Debtors are unable, at this time, to provide a detailed listing of unpaid reimbursable pre-petition business expenses because it is likely that employees will submit requests for reimbursement of expenses incurred pre-petition after the Petition Date. Based on past experience, PALCO estimates the requests for reimbursement of pre-petition employee business expenses will total approximately \$17,500, and Britt estimates the requests for reimbursement of pre-petition employee business expenses will total approximately \$1,000.

10. Work and Family Programs

68. The Debtors offer a non-competitive “Scholarship Program” to all children of full-time employees who have been employed for at least one year as of August 1st of that year. The Scholarship Program provides a maximum yearly benefit for those attending junior colleges or trade schools and a greater yearly benefit for those attending four year colleges or universities. Scholarship recipients must maintain certain requirements to qualify. Although the Debtors believe that all scholarship monies related to the pre-petition period have already been paid, some students may file late paperwork or enroll in studies after the beginning of the semester or quarter. Therefore, in an abundance of caution, the Debtors seek authority to continue to honor their Scholarship Program and pay any outstanding amounts relating to the pre-petition period that may arise, which Debtors believe would be relatively nominal.

69. The Debtors also subsidize employee use of the Scotia Recreational Center, located in Scotia, California. Participating employees pay a nominal fee through payroll deductions. The Debtors seek authority to continue to provide this employee benefit in the ordinary course of business.

11. Accrued Vacation

70. In the ordinary course of business, the Debtors’ employees begin accruing vacation time from the date of hire. Employees become eligible to take paid vacation time after 90 days of employment, and employees may accrue a portion of any unused vacation time from year to year, up to one and a half times their annual accrual. The maximum earned annual vacation leave is based on the employee’s length of service with the Debtors. The Debtors pay a lump sum to employees upon employment termination equal to their accrued, unused vacation time up to maximum amount of 160 hours.

71. The Debtors seek authority to honor all vacation time accrued by employees as of the Petition Date by allowing employees to use such accrued vacation after the Petition Date, in accordance with the Debtors’ existing vacation policy. In addition, the Debtors seek authority to pay the liquidated amounts for vacation hours accrued prior to the Petition Date to any

employees terminated on or after the Petition Date. Based on prior experience, PALCO estimates these lump-sum payments to terminated employees will total approximately \$520,255 over time, and Britt estimates these lump-sum payments to terminated employees will total approximately \$49,700 over time.

12. Paid Personal Time Off

72. In the ordinary course of business, the Debtors allow full-time Hourly and Salaried Non-Exempt Employees to take a specified amount of personal time off (“PPTO”) for any purpose determined by the employee (including, without limitation, vacation, sick leave or bereavement leave) as part of an employee’s regular salary package. The amount of PPTO available is accrued monthly at four hours per month (48 hours per year). Employees may also roll over a maximum of 96 hours each year. The Debtors pay a lump sum to employees upon employment termination equal to their accrued, unused PPTO hours.

**VI.
DEBTORS’ EMERGENCY MOTION FOR INTERIM AND FINAL ORDERS
AUTHORIZING THE DEBTOR’S USE OF CASH COLLATERAL**

A. THE DEBTORS’ PREPETITION DEBTS AND LIENS

73. PALCO and Britt are co-borrowers, and Scotia Development, Salmon Creek and Scotia Inn are guarantors under (i) a Revolving Credit Agreement dated as of July 18, 2006 with LaSalle Bank National Association, LaSalle Business Credit, LLC (collectively, “LaSalle”) and Marathon Structured Finance Fund, L.P. (“Marathon”) as lenders (collectively, the “Lenders”), which provides for borrowings up to \$60 million,¹² and (ii) a Term Loan Agreement, dated as of July 18, 2006 with Marathon as lender, which provides for borrowings up to \$85 million (collectively, the “Credit Agreements”). As of the Petition Date, approximately \$40 million

¹² LaSalle and Marathon each have 50% of the commitment liability under the Revolving Credit Agreement, except with respect to letters of credit, as to which Marathon issues 100%.

(including \$14 million in letters of credit) and \$84 million in borrowings were outstanding under the Revolving Credit Agreement and Term Loan Agreement, respectively.

74. The Lenders assert that the Debtors' obligations under the Credit Agreements are secured by a jointly-held senior lien on substantially all of the Debtor's assets pursuant to the Guarantee and Collateral Agreement and related documents dated as of July 18, 2006 (collectively, the "Security Documents").

B. THE DEBTORS' PROPOSED USE OF CASH DURING THE INTERIM PERIOD

75. According to the Budget filed today with the court today, the Debtors expected to have cash needs of approximately \$2.99 million for operating and other business expenses during the week ending January 26, 2007,¹³ which they proposed to pay using cash resources as of the Petition Date of approximately \$1,163,000 and anticipated cash generated from operations aggregating approximately \$1,520,000 million.

76. Currently there is approximately \$900,000 in post petition cash collections held at LaSalle, which will also be required by the Debtors

77. The Debtors seek authority to use cash collateral in which the Lenders and the Loggers/Haulers assert an interest through February 9, 2007, pursuant to the amounts set forth on the Budget, if an agreement can be reached, and also request the Court to schedule a final hearing prior to February 9, 2007 (ideally on February 6, 2007) regarding the Debtors' continued use of cash collateral.

78. If no agreement can be reached, the Debtors seek authority to use cash collateral in which the Lenders and the Loggers/Haulers assert an interest through February 16, 2007, pursuant to the amounts set forth on the Budget, and also request the Court to schedule a final hearing prior to February 16, 2007.

¹³ A portion of the Debtors' cash needs relate to obligations arising prior to the Petition Date. By separate motions for payment of certain employee obligations, and payment of certain critical vendors, the Debtors seek authority to pay such prepetition amounts.

VII.
CASH MANAGEMENT

79. Debtors move for an order authorizing the continued use of certain bank accounts, cash management systems and investment policy (the “Motion”) pursuant to Section 105(a) of Title 11 of the United States Code (the “Bankruptcy Code”).

80. In the ordinary course of their businesses, the Debtors collectively use over 20 separate bank and investment accounts in a system designed to provide efficient and economical cash management. To maintain and preserve the value of the Debtors’ businesses, and to avoid damage to customer, vendor and employee relations, it is important that there be no drastic disruption in the Debtors’ financial dealings. As explained below, a denial of the Motion would not benefit any creditor constituency, but could cause significant harm to the Debtors’ respective business operations, to the detriment of all parties in interest in these cases. The Debtors therefore respectfully request that the Motion be granted.

A. BANK ACCOUNTS

81. In the ordinary course of business prior to the Petition Date, the Debtors maintain the cash management systems and the bank accounts (the “Bank Accounts”) described below.

1. PALCO

82. Pursuant to the Credit Agreements, PALCO’s receivables are wired to a concentration account (Account No.500007399) at LaSalle Bank (the “ Loan Account”). These receivables may come directly from customers to account (No. 1534 5503 7579) at U.S. Bank of California (“U.S. Bank”), into which PALCO deposits miscellaneous payments received locally from customers at its office in Scotia, California (the “U.S. Bank Collection Account”). The U.S. Bank Collection Account is a “lock box” account, and subject to restrictions imposed under the Credit Agreements.

83. Available funds wired to the LaSalle Loan Account on a daily basis are then used to pay amounts owed to the Lenders under the Credit Agreements. Subject to availability under the line of credit, the Lenders then advances funds to pay PALCO expenses, which are paid through a PALCO operating account at US Bank (No. 1534 0092 5191), which is used to make wire transfers for the payment of obligations under PALCO’s pension and 401(k) plans, insurance premiums, and miscellaneous vendors who request payment by wire transfer as well as to vendors via checks. Payments are made from this account on a “zero balance account” basis (i.e., funds are placed into such accounts periodically as required for current expenditures) to fund the following accounts maintained at U.S. Bank: (i) a payroll account (No. 1534 0092 5209), (ii) an administrative (executive) payroll account (No. 1534 0092 5167), (iii) a workers’ compensation account (No. 1534 0092 5183) and (iv) an account for payments owed to employees for health care expenses (No. 1534 0092 5225). Approximately \$12 million in funds flow through this payables account on an average monthly basis.¹⁴

2. BRITT

84. Britt maintains a depository account at US Bank (No. 1534 5503 7561), which is a “lock box” account subject to restrictions under the Credit Agreements. All collections received by Britt are deposited into this account. Available funds from this account are “swept” on a daily basis to Lenders pursuant to the Credit Agreements, and applied to the obligations owed thereunder. An aggregate of approximately \$3.4 million per month is deposited into this account.

85. Subject to availability under the line of credit under the Credit Agreements, funds are then advanced by Lender to PALCO to fund an operating account held by Britt at Bank of America (No. 1459 02 9536), which is subsequently used to pay miscellaneous accounts payable and to fund a payroll account (No. 4050 01 6161) maintained at Wells Fargo Bank and a health

¹⁴ If there are no funds remaining after payment of amounts owed to Lenders, PALCO will borrow funds under the Credit Agreement to pay its expenses. These borrowed funds will be disbursed initially to the LaSalle Concentration Account.

care plan account (No. 1459 12 7947) maintained at Bank of America. Approximately \$ 3.4 million in funds flow through the operating account on an average monthly basis.

3. SALMON CREEK

86. Salmon Creek has only one operating account at Wells Fargo Bank (No. 4945-04-1770), which receives its deposits, and from which it makes payments. There has been very little activity in this account. Salmon Creek also maintains an investment in a certificate of deposit, as described *infra*.

4. SCOTIA DEVELOPMENT

87. Scotia Development has only one operating account at American Bank (No. 4100 097 68), which receives its deposits, and from which it makes payments. There has been very little activity in this account.

5. SCOTIA INN

88. Scotia Inn has only one operating account at US Bank (No. 1534 5501 9783), which receives its deposits, and from which it makes payments. There has been very little activity in this account.

B. REQUEST TO MAINTAIN BANK ACCOUNTS AND CASH MANAGEMENT SYSTEMS

89. The Debtors believe that their Chapter 11 operations will be smoother and more orderly, with a minimum amount of disruption, if they are allowed to maintain the Bank Accounts described above post-petition, with the same account numbers; *provided, however*, that checks dated, issued or initiated from any of the accounts prior to the Petition Date which have not been honored as of the Petition Date will not be honored unless authorized by an order of this Court.

90. Promptly after the filing of the Debtors' bankruptcy petitions, the Debtors orally informed each of the banks mentioned above (collectively, the "Banks") of the commencement of these cases, and directed the Banks not to honor any then-outstanding checks. In addition, counsel for the Debtors has provided counsel to the Banks a copy of the Voluntary Petitions

commencing the Debtors' bankruptcy cases. The Debtors intend promptly to provide the Banks with a list of outstanding checks as of the Petition Date.

91. The Debtors submit that all parties in interest, including the Debtors' employees, vendors and customers, will be best served by allowing the Debtors to retain the existing Bank Accounts, thereby avoiding the disruption and delay to their payroll activities and other operations that would necessarily result from closing the Bank Accounts and opening new accounts. The benefits to the Debtors' business operations and all parties in interest will be considerable, given the number of Bank Accounts that the Debtors maintain, as well as the crucial role of these Bank Accounts in the Debtors' existing cash management systems.

92. Accordingly, the Debtors respectfully request that, with regard to the existing Bank Accounts, the Court waive the requirements of the United States Trustee Guidelines (the "Guidelines"), which mandate, among other things, the immediate closure of a debtor's prepetition bank accounts, the opening of new bank accounts, the printing of new bank signature cards or checks with a "Debtor in Possession" designation on them, and the establishment of specific accounts for amounts owed to taxing authorities. Moreover, the Debtors request that their checks not be required to include a legend referring to their status as debtors in possession. The Debtors make the same request with regard to any other payment instruments currently in use or used by the Debtors during the pendency of this case. For similar reasons, the Debtors also request authority to maintain some of their Bank Accounts at banks which are not included in the "List of Approved Depositories" promulgated by the Office of the U.S. Trustee. The Bank Accounts are maintained with Banks that are each substantial financial institutions with ample resources, and would most likely be acceptable depository banks within the geographical region in which they are located.

93. Approximately \$15.4 million flows through the Debtors' Bank Accounts and cash management systems every month. The cash management systems described above constitutes the Debtors' ordinary business practices, and the Debtors view them as essential.

94. The cash management systems also provide significant benefits to the Debtors' operations, including, *inter alia*, the ability to (i) efficiently control corporate funds, (ii) ensure the maximum availability of funds when necessary, (iii) reduce borrowing costs and administrative expenses by facilitating the movement of funds, and (iv) develop timely and accurate account balance information.

95. If the Debtors are not permitted to maintain and utilize the existing Bank Accounts and to continue to use their existing forms of checks and other payment instruments, the resulting harm will likely include significant (i) disruption in the ordinary financial affairs and business operations of the Debtors, including their cash management systems, (ii) delay in the administration of the Debtors' estates, and (iii) costs to the estate to immediately close all of the Bank Accounts, open new accounts and implement new systems (including cash management procedures). Debtors particularly wish to avoid disruption with their payroll and employee benefits systems, which are an integral part of their cash management systems.¹⁵

96. Accordingly, the Debtors seek authority to continue their cash management systems, as it will facilitate the necessary cash transfers among the various Bank Accounts and related transactions, and will greatly simplify the tracking of interbank and intrabank disbursements and other administrative aspects of the Debtors' operations during the pendency of these chapter 11 cases. The Debtors intend to continue to maintain records of all transfers within the cash management systems, so that all transfers and transactions will be properly documented and accurate balances will be maintained.

97. As noted above in connection with the Debtors' request to maintain their Bank Accounts, closing the Bank Accounts and opening new accounts potentially would impair the Debtors' post-petition business continuity and result in disruption and delay to payroll activities and general operations. Given the linkage between the Bank Accounts and the cash management

¹⁵ The continuation of the employee benefits systems that the Debtors have in place is the subject of a separate motion filed concurrently herewith.

systems, the identical concerns weigh in favor of maintaining the existing cash management systems. Thus, entry of an order authorizing the Debtors to maintain their present cash management systems is in the best interests of the Debtors, their creditors and all other parties in interest, including the Debtors' respective employees, vendors and customers.

C. THE DEBTORS' INVESTMENT POLICIES

98. The Debtors generally do not have excess funds to invest. As of the Petition Date, the only funds invested by any of the Debtors was a required or restricted certificate of deposit in the amount of approximately \$2.4 million maintained by Salmon Creek with Bank of America (CD # 14364-00150). This CD is required per the Headwaters Agreement relating to Enforcement of AB 1986 dated Feb 25, 1999. It is pledged to the benefit of several California state agencies.

99. The Debtors propose to continue maintaining this prepetition investment (the "Investment Policy") during these Chapter 11 cases which is maintained with a substantial financial institution.

D. BOOKS AND RECORDS AND BUSINESS FORMS

100. In the ordinary course of business, the Debtors use certain books, records and business forms including purchase orders and invoices (collectively, the "Business Forms"). By virtue of the nature and scope of the Debtors' business operations, the Debtors request that they be permitted to continue to use their Business Forms without alteration or change, including their existing check stock. Further, the Debtors have a computerized record-keeping system and will be able to track and separate prepetition versus postpetition periods and transactions. In view of the time delay, added expense and confusion that would be involved in creating new books and records and business forms, it is imperative that the Debtors be permitted to use their existing systems, accounts and business forms in order to avoid disruption to normal operations of its business.

VIII. UTILITIES

101. By this Motion, the Debtors seek entry of an Order (i) prohibiting those utility companies providing utility services to the Debtors (each a “Utility” and, collectively, the “Utilities”) from altering, refusing or discontinuing services to, or discriminating against, the Debtors on account of unpaid prepetition invoices; and (ii) establishing procedures for determining requests by the Utilities for “adequate assurance of payment” within the meaning of § 366.

102. Numerous Utilities provide the Debtors with traditional utility services, such as telephone and communications services, electric, water, sewer, gas and other similar services that are necessary for the continued operation of the Debtors’ day-to-day business operations. A list of all identified Utilities is attached as Exhibit “A” to the Utilities Motion (the “Utility Service List”).¹⁶ In some cases, the Debtors have paid a security deposit to a Utility. The Debtors have made a good-faith effort to identify all Utilities and list them on the Utility Service List.

103. Uninterrupted utility services are critical to the ability of the Debtors to operate and maintain the value of its business for the ultimate distribution herein and to maximize value for the benefit of its creditors. Without consistent, uninterrupted utility services, the Debtors could not operate their business. Such a cessation would substantially disrupt operations, result in a loss of revenues and potentially jeopardize the Debtors’ efforts to reorganize.

IX. CRITICAL VENDORS

104. The Debtors utilize a number of loggers, haulers and other providers of specialized goods and services in their forest products operations (collectively, the “Vendors”).

105. Given the Debtors’ relatively remote geographic area, their unique regulatory concerns and the highly specialized nature of their operations, they typically cannot substitute the

¹⁶ The inclusion of any entity on, or the exclusion of any entity from, the Utility Service List is not an admission by the Debtors that such entity is or is not a “utility” within the meaning of § 366, and the Debtors reserve their rights to contend that any entity listed on Exhibit A is not a utility. The Debtors request that this Motion apply to all Utilities regardless of whether they are currently identified on the Utility Service List.

goods and services provided by the Vendors that meet the Debtors' requirements for quality, quantity, technical specifications and reliability, on a timely basis. To the extent such goods and services can be replaced, it almost certainly would be at significantly increased costs. Thus, the continuation of the Debtors' business on a postpetition basis will largely depend on the goods and services provided by the Vendors.

106. During the prepetition and post petition periods, the Debtors undertook to identify and select the Vendors that were critical to their business. The list initially compiled was critically examined by the Debtors, with a goal of paring down the number of persons designated as "Critical Vendors."

107. Primarily, the Debtors attempted to identify which Vendors were critical because they provide supplies or services that are: (i) essential to the Debtors' business; and (ii) unique to the particular Vendor, such that arranging alternative means for obtaining the goods or services, if possible, would be unreasonably costly and time consuming. As a result of this process, the Debtors determined the Critical Vendors whose continued supply of goods and services are needed to avoid severe, and possibly fatal, disruptions to the Debtors' business. In addition, the Debtors evaluated which Vendors:

- (a) have the apparent right to impose statutory or other liens on the Debtors' property;
- (b) have the apparent entitlement to an administrative expense claim pursuant to Section 503(b)(9) of the Bankruptcy Code by virtue of supplying goods to one of the Debtors in the ordinary course of such Debtor's business within 20 days before the Petition Date; and
- (c) have apparent reclamation rights pursuant to Section 546(c)(1) of the Bankruptcy Code by virtue of having sold goods to one of the Debtors in the ordinary course of the Vendor's business within 45 days before the Petition Date, while such Debtor was insolvent

108. The Debtors have concluded that their survival depends upon the continued supply of uninterrupted goods and services from the Critical Vendors listed on Exhibit A attached to the Motion, and, as such, payment of the prepetition debts owed to the Critical Vendors will preserve the value of the Debtors' business and ease the administrative burden on their estates. The amount of prepetition debt that the Debtors are seeking authorization to pay Critical Vendors totals approximately \$1,575,000 reflecting amounts already billed to the Debtors. There may be additional amounts the Debtors owe to Critical Vendors for other goods and services provided prior to the Petition Date which have not yet been invoiced. Because the sums owing to the Critical Vendors are dwarfed by the potential disruption that would occur if relationships with such Vendors were terminated, the Debtors submit that approval of the requested payments to the Critical Vendors is appropriate.

109. Accordingly, the Debtors request that this Court enter an order (the "Order") providing that when feasible and appropriate, in the Debtors' business judgment, the Debtors are authorized to satisfy, according to customary terms, up to one hundred percent (100%) of the prepetition debt owed to a Critical Vendor on the condition that, by accepting payment under the terms of the Order, the Critical Vendor agrees to continue extending credit and supplying materials, equipment, goods and/or services to the Debtors in accordance with prepetition practices.

CONCLUSION

Debtors commenced this chapter 11 cases to restructure their secured debt structure and to focus on core operations with the goal of emerging as stronger, healthier companies. To preserve the value of their businesses, Debtors' immediate objective is to maintain "business as usual" following the commencement of these cases, thereby minimizing any adverse effect of the chapter 11 filing on Debtors' operations. For the reasons described herein and in the First Day Pleadings, I believe that the prospect for achieving these objectives for the benefit of creditors

and other parties in interest will not be possible unless this Court grants the relief requested in the First Day Pleadings.

I declare under penalty of perjury that the foregoing is true and correct.

Executed this ____ day of January, 2007.

Gary L. Clark