



MONTANA LEGISLATIVE BRANCH

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TO: Legislative Finance Committee

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RE: Bankruptcy Court Proceedings

On September 15, 2003, NorthWestern Corporation, the parent company of NorthWestern Energy, filed for reorganization under Chapter 11 of the United States Bankruptcy Code in the District of Delaware. Certainly, this filing and the resulting financial restructuring will impact the state of Montana, its government agencies, and its citizens. Exactly how will remain to be seen, and will play out over many months. This report focuses on the potential impact to state government expenditures and budgets, and not on impacts to state revenues or bankruptcy issues in general. For further information on general bankruptcy issues, please see the July 3, 2003 memo from Al Brogan (legal counsel for the Public Service Commission) titled "General Information on Utility Bankruptcy."

PARTICIPATION WITHIN BANKRUPTCY COURT PROCEEDINGS

Several state agencies will have an interest in the final outcome of the bankruptcy proceedings, and will desire to monitor and influence, if necessary, the decisions of the court. Preparation for, and/or active participation in, the bankruptcy court proceedings will result in some level of increased expenditures. To appreciate the impact upon state agency budgets, it is necessary to understand the various levels of participation allowable within such a process. During the bankruptcy process, entities can participate in one of three categories:

- Creditor: An entity with a potential claim for payment against NorthWestern qualifies as a creditor. Only creditors on the Committee of Creditors are allowed to vote on whether to accept a restructuring plan. Per federal law, state agencies are not allowed on the Committee of Creditors, although this does not diminish their separate legal standing as creditors.
- Party in Interest: Parties in interest may file motions, make arguments, and generally participate in the process. A party in interest may not vote on whether to accept the restructuring plan. However, after the exclusive time period, creditors and parties in interest may file their own plan of reorganization.
- Intervener: Intervenors initially have the same standing as a party in interest, but the court may limit their participation.

It appears most likely that state agencies will participate as parties in interest and potentially have a substantial range of participation available to them in the NorthWestern Corporation bankruptcy proceedings.

INDIVIDUAL AGENCY INTERESTS AND ACTIONS

There are several state agencies with possible interest in the bankruptcy court proceedings. A basic discussion of these individual interests and agency actions to-date are discussed below.

Department of Revenue (DOR): DOR is the collector of property and corporation income tax from NorthWestern Energy. The largest potential concern involves the collection of property taxes. Prior to the Chapter 11 filing, NorthWestern paid approximately \$5 million in property taxes, which alleviated the main concern to the department. At this time, the department does not anticipate substantial involvement or costs.

Department of Natural Resources and Conservation (DNRC): DNRC has two primary concerns related to the Broadwater Power Project. DNRC is the state owner of Broadwater, located at Toston Dam. Broadwater is a “qualifying facility” under the federal Public Utility Regulatory Policies Act and is currently entered into a 35-year power purchase agreement with NorthWestern energy to sell power at “full avoided cost,” which is higher than current market rates. Therefore, the potential exists for the bankruptcy court to sever any/all qualifying facility contracts. In this case, DNRC has two primary concerns: 1) relative to their status as a creditor in the current contract, and 2) relative to the potential of losing the qualifying facility contract. To-date, the department has not taken legal action but is working with the state Attorney General, who will represent executive branch agencies in these proceedings.

Department of Environmental Quality (DEQ): DEQ is currently entered into a contract worth approximately \$50,000 for a pilot project to track energy bills/usage, primarily around the capitol complex and the University of Montana campus. The department is ready to bill for \$19,000. To-date, the department has taken no legal action, but is exploring options for participation in the bankruptcy proceedings.

Consumer Counsel (CC): The CC operates under a Montana State Constitution mandate, and is charged with “representing consumer interests in hearings before the public service commission or any other successor agency.” Per this direction, the CC has an active interest in the bankruptcy proceedings and final restructuring plan. Currently, the CC has contracted for outside legal counsel, with costs to be paid from the CC contingency appropriation (\$250,000 over the 2005 biennium). To-date the CC has not taken official legal action.

Public Service Commission (PSC): The PSC, under 69-3-102 MCA, is invested “with full power of supervision, regulation, and control of such public utilities...” and has a very active interest in the bankruptcy court proceedings and resulting restructuring plan. The PSC has also voted to oppose any attempt by the bankruptcy court to halt the commission's investigation into NorthWestern Corporation's finances. Additionally, although the PSC retains its ratemaking authority throughout the process, the bankruptcy preempts state law and the bankruptcy court

may preclude the commission from taking some ratemaking action. Therefore, it is conceivable that the PSC will need to act/react to attempt to avoid the federal preemption and maintain its full ratemaking authority. To-date the PSC has undertaken several actions, to include:

- Voted to enter into provisional contracts with outside legal counsel and financial experts using a line-itemed consultant appropriation (\$53,546).
- Filed two motions, which would allow the PSC's legal counsel to appear before the bankruptcy court and receive all documents related to the proceedings.
- Currently working on a third motion, which would enable the PSC and the Consumer Counsel to be recognized as parties in interest without objection from NorthWestern.
- Entered into discussions to obtain reimbursement from NorthWestern for the costs of PSC participation.

Once the consultant appropriation runs out, and if reimbursement through the court isn't obtained, the PSC may have legitimate budget concerns:

- Legislative legal staff has issued an opinion that neither budget amendment nor supplemental appropriations are allowed under statute for the PSC's state special revenue fund.
- Limited options may include use of federal funds, curtailment of bankruptcy-related costs, or increased appropriation via special session. An increase in the PSC appropriation and a corresponding rate increase will potentially affect customers of the companies paying the revenues into the SSR account.

OTHER ISSUES

In addition to the individual agency interests above, there are three other issues that will affect more than one of the above state agencies.

Milltown Dam: NorthWestern is still involved in negotiations regarding the cleanup of the Milltown Dam. A temporary order issued by the bankruptcy court allows NorthWestern to pay up to \$370,000 per month into the Clark Fork and Blackfoot, LLC, which is an entity within NorthWestern Corporation set up to maintain and operate the dam and negotiate issues related to the dam. Actions taken by the court in relation to the Milltown Dam may potentially impact DEQ, DNRC, the Department of Fish, Wildlife, and Parks, and the Department of Justice Natural Resource Damage program.

Coordination Among State Agencies: Last week, the Governor asked the Attorney General (AG) to file for party in interest status with the bankruptcy court to represent executive branch agencies. As part of the ongoing discussions, an issue was identified whereby the CC and PSC could potentially take a position opposite that of the state relative to the use of higher cost qualifying facility contracts in the NorthWestern Energy supply portfolio. In subsequent discussions, it was determined that due to this potential conflict of interest the AG would not be able to provide legal services in support of PSC or CC involvement in the court proceedings. Therefore, the PSC and CC will not be able to benefit from the reduced costs of AG legal services as compared to outside counsel.

Impact to Rate Payers: Although final utility rates are very much a concern of the state and individual taxpayers alike, it is too early into the bankruptcy process to attempt an estimate of the impact of the reorganization on rates to state agencies or individual taxpayers.

CONCLUSION

Several state agencies have valid and legal standing for some form of active participation in the NorthWestern Corporation bankruptcy proceedings. That participation will not be without costs, which will consist mainly of expenditures for legal and/or technical expertise. The extent of the participation, and therefore the cost to the state, remains unknown and will depend greatly on the events that occur as the court proceeds through the bankruptcy.

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