

**UNITED STATES BANKRUPTCY COURT  
FOR THE DISTRICT OF DELAWARE**

In re	:	CHAPTER 11
	:	
NORTHWESTERN CORPORATION,	:	
	:	Case No. 03-12872 (KJC)
Debtor	:	

**MEMORANDUM**<sup>1</sup>

**BY: KEVIN J. CAREY, UNITED STATES BANKRUPTCY JUDGE**

**Procedural Background**

Before the Court is the Motion of NorthWestern Corporation, filed on March 17, 2008, pursuant to Sections 105 and 1142 of the Bankruptcy Code and Bankruptcy Rules 3020 and 9019, for an Order authorizing and approving the settlement agreement by and among the following parties:

- (i) NorthWestern Corporation, the reorganized debtor (the “Debtor” or “NorthWestern”),
- (ii) Clark Fork and Blackfoot, LLC, (“CFB”)
- (iii) the Plan Committee, appointed under the Debtor’s confirmed plan (described below), on behalf of itself and the holders of Allowed Claims in Class 7 and Class 9 under, and as defined in, the plan;
- (iv) Paul Hastings Janofsky & Walker LLP (“Paul Hastings”), individually and in its capacity as the former counsel to NorthWestern and CFB in the chapter 11 case;

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<sup>1</sup>This Memorandum constitutes the findings of fact and conclusions of law, as required by Fed.R.Bankr.P. 7052. This Court has jurisdiction over this matter pursuant to 28 U.S.C. §§ 1334 and 157(a). This is a core proceeding pursuant to 28 U.S.C. 157(b)(1) and (b)(2)(B) and (O).

- (v) Bank of New York, individually and in its capacity as the initial and predecessor trustee under the QUIPS Indenture (described below),
- (vi) Michael Hanson and Ernie Kindt, individually and in their respective capacities as former officers of CFB and, in the case of Hanson, in certain actions as a current officer of NorthWestern,
- (vii) Magten Asset Management Corporation (“Magten”), a holder of QUIPS Claims (as described below), and
- (vii) Law Debenture Trust Company, individually and in its capacity as successor trustee under the QUIPS Indenture.

(docket no. 3676) (the “Motion”).

The Ad Hoc Committee of Class 7 Debtholders (the “Ad Hoc Committee”) filed an objection to the Motion on April 1, 2008 (docket no. 3678) (the “Objection”). The Debtor filed a reply to the Objection, which was joined by Magten Asset Management Corporation (docket nos. 3698 and 3700). Riverside Contracting LLC also filed a limited objection to the Motion on May 6, 2008.

On May 6, 2008, the Debtor filed a Notice of Filing Fully Executed Amended and Restated Global Settlement Agreement and Release, which superseded Exhibit B to the Motion (docket no. 3711)(the “Global Settlement Agreement”). The Debtor also filed an Amended Proposed Order which superseded the proposed order attached as Exhibit A to the Motion (docket no. 3712). A hearing to consider the Motion to Approve the Global Settlement and the objections was held on May 7, 2008.

The parties agreed that there were no disputed facts.<sup>2</sup> (Tr. at 8-9). No one appeared in support of the Riverside Contracting limited objection and, for that reason, it will be overruled. (Tr. at 45).

The Ad Hoc Committee argues that the Global Settlement should not be approved because it violates the terms of the confirmed plan, and it is unreasonable and not in the best interests of creditors. I have reviewed the plan provisions at issue and, after consideration of the record made at the hearing and of parties' arguments, I conclude, for the reasons which follow, that the Global Settlement should be approved.

### **Undisputed Background Facts**

NorthWestern Corporation is one of the largest providers of electricity and natural gas to customers in throughout Montana, South Dakota and Nebraska. NorthWestern filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code on September 14, 2003. The Bankruptcy Court confirmed the Debtor's Second Amended and Restated Plan of Reorganization Under Chapter 11 of the Bankruptcy Code dated August 18, 2004 (the "Plan") by order dated October 19, 2004 (the "Confirmation Order"). The Confirmation Order was affirmed on appeal by the United States District Court for the District of Delaware (the "District Court") on September 29, 2006.

NorthWestern emerged from bankruptcy on November 1, 2004, when the Plan became effective (the "Effective Date"), and the Plan was substantially consummated as of December 29,

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<sup>2</sup>Counsel for the Ad Hoc Committee agreed there were no factual disputes "subject to the proffer being consistent with what I've discussed with counsel." (Tr. at 9). After NorthWestern made the proffer of the testimony of Tom Knapp, former general counsel of NorthWestern, (Tr. at 6 and 21), counsel for the Ad Hoc Committee declined the court's invitation to cross-examine the witness. (Tr. at 24).

2004.

“QUIPS Claims” are defined in the Plan as allowed claims by holders of those 8.45% Junior Subordinated Debentures of the Montana Power Company due 2036, issued under the QUIPS Indenture. The QUIPS Indenture is an indenture dated as of November 1, 1996, between The Montana Power Company, as issuer, and The Bank of New York, as trustee, as amended and supplemented from time to time. NorthWestern became obligated on the QUIPS notes when, on November 15, 2002, approximately ten months before the chapter 11 filing, NorthWestern executed an Assignment and Assumption Agreement for the QUIPS notes as part of a series of transactions involving the transfer by CFB to NorthWestern of substantially all of the transmission and distribution assets acquired from the Montana Power Company and NorthWestern’s assumption of substantially all of the liability of CFB (this is known as the “Going Flat Transaction”).

The Plan classified the QUIPS Claims in Class 8(b) and provided that holders of QUIPS Claims could opt to receive either (i) a specified distribution of common stock issued by NorthWestern under the Plan (the “New Common Stock”) plus warrants, or (ii) a pro rata share of recoveries, if any, upon resolution of the QUIPS Litigation. The QUIPS Litigation is an adversary proceeding brought by Magten and Law Debenture Company of New York, in its capacity as indenture trustee, against NorthWestern to set aside the Going Flat Transaction as a fraudulent transfer. The litigation is now pending in the Delaware District Court at case number 04-1494 before Judge Farnan.<sup>3</sup> Magten and other QUIPS Claim holders elected or were deemed

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<sup>3</sup>The litigation was removed to District Court upon the filing of a Motion to Withdraw the Reference (Adv. No. 04-5334, docket no. 58, 12/8/2004).

to accept Option 2. Under Option 2, their claims are treated as Class 9 General Unsecured Claims, and will receive distributions only upon entry of a final order resolving the QUIPS Litigation (unless otherwise agreed to by NorthWestern).

Under the Plan, Class 7, Unsecured Note Claims, and Class 9, general unsecured claims, received a *pro rata* share of the New Common Stock. Section 7.5 of the Plan established a “Disputed Claim Reserve” (sometimes referred to as the “DCR”) for claims that were unresolved as of the Effective Date, which was initially funded with 4.4 million shares of New Common Stock. NorthWestern also established two separate “sub-reserves” within the DCR - - one for the QUIPS Claims and one for the claim of PPL Montana, LLC. Pursuant to a settlement reached in September 2005, PPL withdrew its claim and the shares of New Common Stock in the PPL sub-reserve were released into the Disputed Claim Reserve. Section 7.7 of the Plan provides for surplus distributions of unclaimed property or excess New Common Stock in the DCR to holders of Allowed Claims. At the time the Motion was filed, NorthWestern asserted that the Disputed Claim Reserve held 3,144,642 shares of New Common Stock, along with all dividends issued and interest earned in respect of such shares. (Motion, p. 6).

The sub-reserve for the QUIPS Claims was established pursuant to a Stipulated Order, dated November 3, 2004, between NorthWestern and Law Debenture of New York. Pursuant to the Stipulated Order, NorthWestern agreed to set aside 787,339 shares of New Common Stock to satisfy \$25 million in QUIPS Claims if such claims were Allowed. The Stipulation did not cap recovery at \$25 million, but provided that any Allowed Claim in excess of \$25 million would be satisfied from remaining New Common Stock in the DCR.

In addition to the QUIPS Litigation, there are several other actions pending involving one

or more of the parties to the Global Settlement, that are listed on Exhibit 2 to the Global Settlement Agreement (the “Litigations”). The Litigations include, without limitation, claims by Magten and Law Debenture of New York (jointly, the “Magten Parties”) against NorthWestern, CFB, Paul Hastings, the former officers, and Bank of New York alleging, among other claims, that:

- (i) the Magten Parties are creditors of CFB,
- (ii) the Going Flat Transaction was a fraudulent transfer because, among other things, such transfer allegedly left CFB insolvent and unable to pay certain claims,
- (iii) the Confirmation Order was procured by fraud as a result of the alleged failure to adequately fund the Disputed Claims Reserve with a sufficient number of shares of New Common Stock to satisfy a potential full recovery on all pending claims against the estate which were outstanding on the Effective Date,
- (iv) the QUIPS Claimants suffered damages as alleged in the Litigations by virtue of the action or inaction of Bank of New York, in its capacity as the initial trustee under the QUIPS Indenture,
- (v) Paul Hastings aided and abetted breaches of fiduciary duty by corporate officers while serving as counsel to NorthWestern and CFB in connection with the Going Flat Transaction, and
- (vi) the Former Officers are liable for breach of fiduciary duty in connection with the Going Flat Transaction.

NorthWestern, CFB, Paul Hastings, the former officers, and Bank of New York dispute all of the claims in the Litigations. Certain defendants in the Litigations, including Bank of New York and the former officers, have asserted that NorthWestern is legally obligated to indemnify them against certain claims, damages and awards arising out of the Litigations.

But for the Global Settlement Agreement, a trial on the QUIPS Litigation was scheduled to commence in District Court on March 5, 2008, with a trial on the litigation against the former

officers (the “Officer Litigation”) to commence thereafter. In connection with that trial and the Officer Litigation, the District Court would also adjudicate, among other things, separate motions for summary judgment of NorthWestern and the defendants to the Officer Litigation, and approximately 15 motions in limine. These litigation matters are being held in abeyance by the District Court pending the disposition of the Motion. Oral argument and related proceedings before the Third Circuit Court of Appeals involving litigation by the Magten Parties against Paul Hastings, have also been held in abeyance pending disposition of the Motion.

Settlement negotiations among the Parties have spanned more than two years and include a prior “global” settlement that was not approved by the Bankruptcy Court in 2005. Twice during 2005 and twice during 2007, the Magten Parties, NorthWestern, and the Plan Committee engaged in exhaustive mediation efforts to resolve the Litigations, including pursuant to the District Court’s Mediation Procedures Order and the Third Circuit Appellate Mediation Program.

During the settlement negotiations, NorthWestern and the Plan Committee entered into a certain “Dispute Resolution Agreement” dated November 28, 2007 (the “Plan Committee Settlement Agreement”), to resolve certain disputes between NorthWestern and the Plan Committee, including (i) NorthWestern’s appeal to the Third Circuit of the District Court’s decision regarding the Plan Committee motion, filed on September 29, 2005, seeking a distribution from the DCR, (ii) the dispute between the Plan Committee and NorthWestern concerning NorthWestern’s alleged right to pay its legal fees and expenses from the DCR, and (iii) the dispute between the Plan Committee and NorthWestern concerning the status and treatment of Bank of New York’s indemnification claims. Initially, approval of the Plan Committee Settlement Agreement was a condition precedent to the Global Settlement

Agreement, but the amendments dated May 5, 2008, provide that:

In the event the pending motion to approve the Amended Global Settlement Agreement (the “GSA Motion”) is granted, then the hearing on the [Plan Committee Settlement] Motion shall be adjourned until a Final Order is obtained with respect to the GSA Motion. In the event an order approving the Amended Global Settlement Agreement becomes a Final Order, this Amended Agreement shall be obviated, and the Motion withdrawn, upon the consummation of the Amended Global Settlement Agreement.

(Amended and Restated Dispute Resolution Agreement, dated May 5, 2008, ¶8). Accordingly, because the Global Settlement Agreement will be approved, any consideration of a motion for approval of the Plan Committee Settlement will be continued as requested.

### **The Global Settlement Agreement**

The Global Settlement Agreement contains the following essential terms:

- (i) a distribution to the Magten Parties of New Common Stock from the Reserve with a value, when added together with all cash dividends and interest accrued thereon in respect of the Magten Parties Shares, of \$23 million (the “Settlement Proceeds”),
- (ii) the Settlement Proceeds will be distributed to the Magten Parties according to the following allocation:
  - (a) \$5,692,441.37 to the Indenture Trustee Account, \$3,500,000 of which is to reimburse the Indenture Trustee for all fees, expenses and charges incurred in connection with the chapter 11 case and the Claims, and \$2,192,441.27 to be distributed pro rata to the QUIPS Claimants (excluding Magten);
  - (b) \$17,307,558.63 to the Magten Account, \$14,609,770.74 of which is to reimburse Magten for all fees, expenses and charges incurred in

connection with the chapter 11 case and the Claims (professional fees and otherwise), and the remaining \$2,697,787.89 represents Magten's pro rata share of the Settlement Proceeds after payment of Magten's and Law Debenture's fees and expenses.

- (iii) Payment of \$4 million to NorthWestern by Paul Hastings' and one or more of NorthWestern's insurance carriers in accordance with separate written agreements,
- (iv) dismissal with prejudice, or similar resolution, of all of the Litigations,
- (v) comprehensive releases, including a covenant to never bring a lawsuit in respect to the released claims, provided by various Parties and others, including the QUIPS Claimants, for the benefit of the Parties and certain related persons, and
- (vi) supplemental distribution to holders of Class 7 and Class 9 claims from the Disputed Claims Reserve.

### **Discussion**

The Ad Hoc Committee objects to the Global Settlement Agreement, arguing that its terms violate the provisions of the confirmed Plan, and that the agreement is not reasonable or in the best interests of creditors.

NorthWestern, and other parties who support the Global Settlement, have argued that the Ad Hoc Committee's objection should not be heard because, first, the Ad Hoc Committee is not a QUIPS Claimant and, therefore, lacks standing to object to allocation of the Settlement Proceeds and, second, that the Ad Hoc Committee should not be heard because its members have failed to file adequate disclosure statements under Bankruptcy Rule 2019. While these

arguments may have some merit, I need not resolve these issues because I have decided that the Ad Hoc Committee's objection to the Global Settlement should be overruled and the Global Settlement should be approved.

A. **The Global Settlement does not violate or modify the provisions of the confirmed Plan.**

The Ad Hoc Committee argues that two provisions of the Global Settlement contravene the terms of the Plan.<sup>4</sup> First, the Ad Hoc Committee objects to any payment to NorthWestern for attorney fees and expenses, arguing that the Plan does not allow such payments from the Disputed Claims Reserve. The amendments to the Global Settlement Agreement, however, revised the original agreement and now provide that NorthWestern will be paid by third party insurers. NorthWestern will not receive any payment from the Disputed Claim Reserve, nor will it, as argued by the Committee, receive a "kick-back" from Magten, after Magten receives its distribution from the DCR. The Ad Hoc Committee has not provided any evidence or even argued that payments to NorthWestern from third-party insurers violates any Plan provision. Therefore, I reject the Committee's argument that the Global Settlement's proposed payments to NorthWestern violate the Plan.

Second, the Ad Hoc Committee argues that the allocation of the Settlement Proceeds violates or modifies the provision of the Plan that allowed a QUIPS Claimant to opt to receive "a Pro Rata Share of recoveries, if any, upon resolution of the QUIPS Litigation" (Plan, §4.8(b)(ii)).

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<sup>4</sup>The Ad Hoc Committee's original objection also argued that the proposed distribution of \$23 million *cash* to the Magten Parties violated the Plan, which required distribution to claimants of New Common Stock. However, the Committee's counsel agreed at oral argument that new terms in the Amended Global Settlement Agreement moot this argument. (Tr. at 28).

Although “Pro Rata Share” is defined in the Plan, the term “recoveries” is not.<sup>5</sup> The Plan language does not support the Ad Hoc Committee’s view that deducting attorney fees and costs from the recoveries prior to a pro rata distribution is contrary to the Plan’s terms. Therefore, I conclude that the proposed allocation of the Settlement Proceeds does not violate or modify a provision in the Plan.

**B. The Global Settlement Agreement meets the requirements for approval under Bankruptcy Rule 9019.**

“Pursuant to Bankruptcy Rule 9019(a), the authority to approve a compromise settlement is within the sound discretion of the bankruptcy court. In exercising this discretion, the bankruptcy court must determine whether the compromise is fair, reasonable, and in the best interest of the estate.” *Key3media Group, Inc. v. Pulver.Com, Inc. (In re Key3media Group, Inc.)*, 336 B.R. 87, 92 (Bankr.D.Del. 2005)(citations omitted). When considering whether a proposed settlement is fair and equitable, the Third Circuit has instructed that the Court should consider four criteria: (1) the probability of success in litigation, (2) the likely difficulties in collection, (3) the complexity of the litigation involved and the expense, inconvenience and delay necessarily attending it, and (4) the paramount interest of the creditors. *Will v. Northwestern Univ. (In re Nutraquest, Inc.)*, 434 F.3d 639, 644 (3d Cir. 2006). The second factor is not relevant here, but upon consideration of the other three factors, I conclude that the settlement is fair and equitable and should be approved.

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<sup>5</sup>“Pro Rata Share” is defined in the Plan as “a proportionate share, so that the ratio of the consideration distributed on account of an Allowed Claim in a Class to the amount of such Allowed Claim is the same as the ratio of the amount of the consideration distributed on account of all Allowed Claims in such Class to the amount of all Allowed Claims in such Class.”

The Ad Hoc Committee, relying on arguments put forth in NorthWestern's summary judgment papers before the District Court, argues that NorthWestern has a high probability of succeeding on the merits of the fraudulent transfer litigation. The Committee contends that it is unreasonable to pay the Settlement Proceeds of \$23 million from the DCR, because that amount represents 60% of the QUIPS Claimants maximum possible recovery under the Plan.

NorthWestern argues in response that the proposed settlement is approximately half of what the QUIPS Claimants could recover if they obtained a judgment of \$50 million, and note that the plaintiffs have taken the position that their claim could be higher. In addition to consideration of the settlement amount, NorthWestern emphasizes the importance of ending the on-going profusion of litigation that has held up distributions from the DCR to other creditors for years.

This criteria was discussed in the decision *In re Coram Healthcare Corp.*, 315 B.R. 321, 330 (Bankr.D.Del. 2004) by Judge Walrath as follows:

In approving a settlement, the court does not have to be convinced that the settlement is the best possible compromise. *Nellis v. Shugrue*, 165 B.R. 115, 123 (S.D.N.Y.1994). Rather, the court must only conclude that the compromise or settlement falls within the reasonable range of litigation possibilities. *In re Penn Central Transp. Co.*, 596 F.2d 1102, 1114 (3d Cir.1979). That is, the settlement need only be above "the lowest point in the range of reasonableness." *Official Unsecured Creditors' Comm. of Pa. Truck Lines, Inc. v. Pa. Truck Lines, Inc. (In re Pa. Truck Lines, Inc.)*, 150 B.R. 595, 598 (E.D.Pa.1992).

The settlement amount - - whether 50% or 60% of the claim asserted by the Magten Parties in the fraudulent transfer litigation - - is within the range of reasonableness. It is less than the amount set aside in the sub-reserve for the QUIPS Litigation. The Plan Committee, on behalf of the Class 7 and Class 9 Unsecured Creditors, supports the settlement and the reasonableness of

the amount.<sup>6</sup> (Tr. at 51). Moreover, the Global Settlement resolves more than the fraudulent transfer litigation. It also resolves the Magten Parties' appeal of the order directing NorthWestern to make a surplus distribution from the DCR, Law Debenture's appeal of an order denying its request for payment of fees incurred as the trustee under the QUIPS Indenture, the Magten Parties' adversary proceeding to revoke the confirmation order, as well as other litigation involving claims with respect to which NorthWestern may have an obligation to indemnify other parties. Finally, the Global Settlement resolves the remaining claims against the DCR and allows for distribution of the surplus to other unsecured creditors. These considerations cause me to conclude that the Global Settlement falls well within the range of reasonableness.

In considering the third criteria for approval of the settlement, the *Nutraquest* Court noted that “[i]t is axiomatic that settlement will almost always reduce the complexity and inconvenience of litigation.” *Nutraquest*, 434 F.3d at 646. Given the number of outstanding lawsuits and claims at issue here, the vigor with which they have been asserted, and that more than three years have passed since confirmation and the parties were just beginning trial on the QUIPS Litigation in District Court, there is no doubt that the Global Settlement avoids the inconvenience, expense, and delay of the Litigations. Uncontroverted evidence offered in support of the Motion indicates that, over the course of the Litigations, NorthWestern incurred legal fees and professional expenses of approximately \$10 million. (Tr. at 21). Further, NorthWestern expected that it could incur an additional \$5 - \$8 million if the settlement is not approved. (*Id.*). Despite the Ad Hoc Committee's opinion on the merits of the outstanding

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<sup>6</sup>The Plan Committee noted, however, that it took no position on the allocation of the Settlement Proceeds among the QUIPS Claimants. (Tr. at 52).

summary judgment motion, a decision in the Debtor's favor cannot be assured, nor would it necessarily guarantee an end to litigation. The Global Settlement does.

The final criteria to consider is the paramount interests of creditors. The creditors most effected - - the QUIPS Claimants - - have not pursued any objections to the Global Settlement. Furthermore, the Global Settlement allows for a settlement and withdrawal of all the pending litigation. This allows for a final distribution of the remaining funds the Disputed Claim Reserve and, therefore, the Global Settlement benefits all creditors that will share in that distribution. The Plan Committee's support of the Global Settlement weighs heavily in favor of approval.

### **Conclusion**

For these reasons, I conclude that the Global Settlement is fair and equitable to the parties and to other creditors of the bankruptcy estate. At the hearing already scheduled for July 10, 2008 at 2:00 p.m., the Court will consider comments to the Amended Proposed Order submitted by the Debtor on May 6, 2008.

BY THE COURT:



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KEVIN J. CAREY  
UNITED STATES BANKRUPTCY JUDGE

Dated: July 10, 2008