



- Board of Directors
Legal and Claims Committee

5/12/2015 Board Meeting

8-5

Subject

Report on *In Re Tronox Incorporated, et al.*, Chapter 11, United States Bankruptcy Court, Southern District of New York, Case No. 09-10156 (MEW), and authorize increase in maximum amount payable under contract with Manatt, Phelps and Phillips, LLP for legal services by \$100,000 to a maximum amount of \$540,000

Executive Summary

This letter requests an increase in the maximum amount payable under contract with Manatt, Phelps and Phillips, LLP (Manatt) for legal services by \$100,000 to a maximum amount of \$540,000. Metropolitan and the Central Arizona Water Conservation District (CAWCD) jointly hired Manatt in August 2009 to provide local assistance in Tronox's bankruptcy in the Southern District of New York, as well as to advise on Comprehensive Environmental Response, Compensation, and Liability Act (CERCLA) matters. With Manatt's assistance, Metropolitan is also monitoring the investigation and remediation of the Tronox facility and associated groundwater contaminant plume near Henderson, Nevada (Tronox Site), which is a source of perchlorate in the Colorado River. In addition, Manatt is helping to monitor the distribution of funds from the settlement of the Adversary Action which Tronox (the estate) and the United States brought against Anadarko and Kerr-McGee, as well as assisting with the defense of a subrogation claim by certain AIG insurance entities (AIG). To date, Metropolitan and CAWCD have paid Manatt approximately \$400,000 for its legal services. Having almost exhausted this funding, staff is requesting an additional \$100,000, half of which will be paid by CAWCD, to continue this ongoing work.

Details

When staff last reported on this matter in April 2014, the Adversary Action had recently settled for \$5.15 billion, which is the largest recovery for the cleanup of environmental contamination in United States history. The settlement provides that the Nevada Environmental Response Trust (Trust) will receive approximately \$1.1 billion to clean up the Tronox Site. Metropolitan, CAWCD, the Southern Nevada Water Authority (SNWA), the Nevada Division of Environmental Protection (NDEP), and others are continuing to work together to: (i) review and comment on the Trust's Remedial Investigation/Feasibility Study Work Plan (RI/FS Work Plan) to determine the most efficient and cost-effective methods to remediate the Tronox Site; (ii) monitor the distribution of the settlement proceeds; (iii) monitor and assist in resolution of claims against the Trust funds; and (iv) monitor the Trust's work plan, remediation activities and budget. Metropolitan and CAWCD jointly contracted with Manatt to assist in these efforts. To date, Metropolitan and CAWCD have paid Manatt approximately \$400,000 for its legal services.

Background

Since August 2009, Manatt has assisted Metropolitan and CAWCD with their participation in Tronox's bankruptcy action, monitoring the Adversary Action and the settlement of that case, and the remediation of the Tronox Site. Perchlorate was first discovered in the Colorado River in 1997 at Metropolitan's intake and traced back to the Tronox Site. The Tronox Site was constructed by the U.S. Department of Defense (DoD) during World War II and used for the production of military supplies and various other products over many years, resulting in significant contamination of the site. Kerr-McGee owned and operated the Tronox Site for several

years. Kerr-McGee also owned many other businesses around the country which involved the use of hazardous and toxic chemicals. From 2000 through March 2006, Kerr-McGee engaged in a process of corporate reorganization that resulted in the creation of Tronox as a spin-off successor corporate entity with the responsibility for essentially all of Kerr-McGee's environmental and pension liabilities. "Old Kerr-McGee" was divested of the liabilities, and a "New Kerr-McGee" was created that was free from such liabilities. Shortly thereafter, Anadarko acquired New Kerr-McGee.

Tronox Bankruptcy

In January 2009, Tronox filed for bankruptcy. One of the main reasons that Tronox filed for bankruptcy was to obtain relief from its environmental obligations across the country, including at the Henderson, Nevada site. As part of the bankruptcy proceeding, Tronox filed an Adversary Action against Kerr-McGee and Anadarko, alleging fraudulent conveyance of the nationwide environmental liabilities from Kerr-McGee to Tronox. Tronox asserted that Kerr-McGee transferred environmental liabilities to Tronox that greatly exceeded the value of the businesses and other assets it received or its capacity to generate sufficient income to pay its environmental debts. Tronox included the Adversary Action as an asset in the bankruptcy.

At the time of the bankruptcy, out of concern that there would be inadequate funding to remediate the Tronox Site after the bankruptcy, Metropolitan joined with SNWA and CAWCD to form the "Colorado River Authorities," which enabled the three agencies to participate in the bankruptcy action. Metropolitan and the other agencies coordinated with the U.S. Department of Justice (DOJ) and the NDEP to reach a settlement of the bankruptcy case that provides adequate funding for remediation of the Tronox Site. In February 2011, the bankruptcy court confirmed a settlement that provided the following assets to assist with long-term remediation efforts at the site: (1) approximately \$81 million in cash; (2) approximately 25 percent of an 88 percent environmental share of any net recovery in the Adversary Action; and (3) 100 percent of certain Nevada real estate assets. Because Tronox would no longer have the obligation to remediate the Tronox Site upon conclusion of the bankruptcy, the Trust was created by the court. The Trust has full responsibility to clean up the site. Manatt is assisting Metropolitan and CAWCD on a number of matters with the Trustee, including monitoring: (a) the use of assets from the bankruptcy settlement towards remediation at the Tronox Site; (b) the distribution of the settlement proceeds from the Adversary Action; and (c) a subrogation claim by AIG.

Remediation Activities

A groundwater pump and treat system has operated continuously at the Tronox Site since 2002. Perchlorate concentrations in the Las Vegas Wash have decreased by more than 90 percent due in large part to the operation of this system. Also, perchlorate levels at the Colorado River Aqueduct intake at Lake Havasu have similarly declined and are less than California's current maximum contaminant level for perchlorate of 6 micrograms per liter. In accordance with CERCLA, the Trust started a remedial investigation at the site in 2014. The remedial investigation activities currently underway include soil and groundwater sampling, evaluation of potential risks to human health and the environment, and determining the movement and behavior of chemicals in groundwater by using a groundwater model. It is expected that the remedial investigation will continue through the first half of 2016, and then a feasibility study will be conducted for the remainder of 2016 and into 2017. The purpose of the feasibility study is to develop, compare, and evaluate cleanup options and technologies before selecting the final cleanup method. Full remediation of the site is anticipated to take several decades. In its work with the Trust to develop a plan for full remediation of the Tronox site, NDEP is considering potential future federal regulation of perchlorate, an analysis of the spread of the core plume from the Tronox site within a larger regional area that contributes to the perchlorate load in the Las Vegas Wash, and methods to assess and remediate the perchlorate located within the soil beneath existing structures on the Tronox Site.

Adversary Action

On December 12, 2013, the bankruptcy judge issued a 166-page opinion, finding that Kerr-McGee acted with "intent to hinder or delay creditors" when it spun off and transferred almost all the environmental liabilities to Tronox. The court tentatively ruled that damages could range from about \$5 billion to more than \$14 billion, plus attorneys' fees and costs. Anadarko and Kerr-McGee argued in response that the amount of damages should be reduced to as low as \$850 million, whereas plaintiffs requested approximately \$20.7 billion in damages. On

April 3, 2014, the case settled for \$5.15 billion, the largest recovery for the cleanup of environmental contamination in United States history. The settlement agreement went into effect on January 21, 2015. On January 23, 2015, the defendants in the Adversary Action paid \$5.15 billion, plus interest from April 3, 2014, to the Litigation Trust. Of this amount, the Trust is entitled to receive approximately \$1.1 billion, which can only be used to clean up the Tronox Site. To date, the Trust has received approximately \$900 million.

Additional Issues

The Litigation Trustee initially withheld approximately 40 percent of the settlement proceeds for potential tax liability. Manatt assisted the Colorado River entities in working with NDEP and the Trust to seek release of additional funds. The Litigation Trustee subsequently reduced the holdback of funds to 15 percent of the settlement for potential tax liabilities.

During the process to approve the Settlement, AIG asserted that it is entitled to recover from the Trust funds in excess of \$250 million that AIG previously paid for certain cleanup costs. Manatt is helping Metropolitan and CAWCD to advise the Trust in responding to AIG's subrogation claim.

After the settlement was approved, NDEP determined that a more regional approach is required to remediate the sources of perchlorate that contribute to perchlorate loading in the Las Vegas Wash. The State of Nevada has proposed the creation of a "Bureau of Industrial Site Cleanup" to take the lead on oversight, direction and implementation of the entire scope of cleanup activities to be funded under the settlement. Funds from the settlement would be used for the new Bureau.

On March 12, 2015, the bankruptcy court dismissed the Adversary Proceeding. However, the bankruptcy court and the district court will continue to retain jurisdiction to resolve disputes in connection with the settlement and to enforce the settlement agreement.

Manatt's Legal Expertise

Manatt has prior experience working on a number of matters with the Trustee and is assisting Metropolitan and CAWCD with regard to the Trust's management of the cleanup of the Tronox Site. Although Metropolitan and CAWCD have a significant interest in the activities of the Trust and the remediation of the Tronox Site, they are not legal beneficiaries of the Trust. Manatt also continues to help Metropolitan and CAWCD to achieve their objectives of protecting their source water in the Colorado River from contamination and to maximize the cash and other assets that are available from the settlement of both Tronox's bankruptcy and the Adversary Action in order to continue pumping and treating the groundwater and to ensure the complete remediation of the Tronox Site.

Manatt also has significant experience with complex insurance disputes and defending against subrogation claims. Manatt is assisting Metropolitan and CAWCD to advise the Trust in defending against AIG's subrogation claim.

Requested Board Action

In order to fund Metropolitan's and CAWCD's continued participation in this work, this letter requests board authorization to increase the authorized payment pursuant to the contract with Manatt by \$100,000 to a maximum amount of \$540,000. The \$100,000 in additional expenditures would be shared equally with CAWCD so that Metropolitan would not spend more than \$50,000.

Policy

Metropolitan Water District Administrative Code Section 6431: Authority to Obtain Expert Assistance

California Environmental Quality Act (CEQA)

CEQA determination for Option #1:

The proposed action is not defined as a project under CEQA because it involves continuing administrative activities (Section 15378(b)(2) of the State CEQA Guidelines). In addition, the proposed action is not subject to CEQA because it involves other government fiscal activities, which do not involve any commitment to any

specific project which may result in a potentially significant physical impact on the environment (Section 15378(b)(4) of the State CEQA Guidelines).

The CEQA determination is: Determine that the proposed action is not subject to the provisions of CEQA pursuant to Sections 15378(b)(2) and 15378(b)(4) of the State CEQA Guidelines.

CEQA determination for Option #2:

None required

Board Options

Option #1

Adopt the CEQA determination that the proposed action is not subject to the provisions of CEQA, and authorize amendment of the contract for legal services with Manatt, Phelps and Phillips LLP for the *In Re Tronox Incorporated, et al.* matter to increase the maximum amount payable by \$100,000 to a maximum amount of \$540,000. The \$100,000 is to be shared equally with CAWCD.

Fiscal Impact: \$50,000

Business Analysis: Approval will provide Metropolitan with legal representation to work with the Trust for the Tronox Site, NDEP, and DOJ to protect the Colorado River from a resumption of contamination from the Tronox Site.

Option #2

Do not amend the subject contract.

Fiscal Impact: Unknown at this time

Business Analysis: Metropolitan would not have outside counsel assistance in working with the Trust to address the cleanup of contamination at the Tronox Site and to assist with the remaining issues relating to the distribution of the settlement proceeds from the Adversary Action.

Staff Recommendation

Option #1



Marcia L. Scully
General Counsel

4/23/2015
Date