UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MISSOURI
SOUTHEASTERN DIVISION

In re: NORANDA ALUMINUM, INC., *et al*., Debtors.	Chapter 11 Case No. 16-10083-399 (Jointly Administered) Re: D.I. 671, 674

THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS' OMNIBUS OBJECTION TO

DEBTORS' MOTION FOR AN ORDER PURSUANT TO SECTIONS 105(A), 363 AND 503(C)(3) OF THE BANKRUPTCY CODE AND BANKRUPTCY RULE 6004 (A) AUTHORIZING AND APPROVING THE DEBTORS' (I) KEY EMPLOYEE INCENTIVE PLAN; (II) KEY EMPLOYEE RETENTION PLAN; AND (III) 2015 INCENTIVE COMPENSATION PLAN AND (B) GRANTING RELATED RELIEF

AND

DEBTORS' MOTION FOR AN ORDER PURSUANT TO SECTIONS 105(A) AND 363 OF THE BANKRUPTCY CODE AND BANKRUPTCY RULE 6004 AUTHORIZING AND APPROVING THE DEBTORS' MODIFIED SENIOR MANAGEMENT SEVERANCE PROGRAM FOR NON-INSIDER EMPLOYEES

The Official Committee of Unsecured Creditors (the "Committee") of the above-captioned Debtors, by and through its undersigned counsel, hereby objects (the "Omnibus Objection") to the *Debtors' Motion for an Order Pursuant to Sections 105(a), 363 and 503(c)(3) of the Bankruptcy Code and Bankruptcy Rule 6004 (A) Authorizing and Approving the Debtors' (I) Key Employee Incentive Plan; (II) Key Employee Retention Plan; and (III) 2015 Incentive Compensation Plan and (B) Granting Related Relief* (the "Bonus Compensation Motion") [Docket No. 671] and *Debtors' Motion for an Order Pursuant to Sections 105(a) and 363 of the Bankruptcy Code and Bankruptcy Rule 6004 Authorizing and Approving the Debtors Modified Senior Management Severance Program for Non-Insider Employees* (the "MSP Motion" and, collectively with the Bonus Compensation Motion, the "Compensation Motions") [Docket No.

674]. In support of its Objection, the Committee relies on, and incorporates herein by reference, the *Declaration of Jason Feintuch in Support of the Committee's Objection to the Bonus Compensation Motions* (the "Feintuch Declaration"), filed concurrently herewith, and respectfully represents as follows:

PRELIMINARY STATEMENT

1. The Compensation Motions, pursuant to which the Debtors seek to implement ***four*** separate compensation plans - a key employee incentive plan (the "KEIP"), a key employee retention plan (the "KERP), an incentive compensation program (the "ICP"), and a modified severance program (the "MSP" and, collectively with the KEIP, KERP and ICP, the "Compensation Plans") – represent further steps by the Debtors to push this bankruptcy in a direction which quickly monetizes value for the Debtors' Secured Lenders (defined herein) and provides no value for the Debtors' estates or remaining creditors. Pursuant to the Compensation Plans, the Debtors propose to pay more than $6.4 million in bonuses and compensation (and that does not include the cost of the MSP, which the Debtors did not disclose in the MSP Motion). For the reasons set forth herein, the Debtors' proposal is not in the best interest of the Debtors' estates and must be rejected.

2. First and foremost, the Debtors cannot demonstrate that any of the Compensation Plans will maximize value for the Debtors' estates. For example, one of the key metrics for the KEIP is a closing on the sale of the Downstream Business in accordance with the DIP Milestones. As this Court is well aware, the Downstream Business is the Debtors' only profitable business segment. This Court is also well aware that the Debtors' remaining business segments have been operating at substantial losses since before the Debtors' bankruptcy filing. Yet, the Debtors seek to sell their "crown jewel" before "fixing" the Upstream Business. The proposed sale of the Downstream Business will likely leave the Debtors' estates administratively

insolvent and will force the Debtors into a quick sale of the Upstream Business before they have adequate opportunity to restore that business to profitability. This strategy is, quite simply, backwards and contradicts all reason. However, it makes perfect sense from the standpoint of the Debtors' DIP Lenders, who are looking to cash out quickly by selling the profitable Downstream Business without regard to the fact that at this time the Upstream Business requires assistance from the Downstream Business in order to reorganize. As such, the Compensation Plans incentivize employees to support a hijacked process on a misguided course and should not be approved.

3. In addition, the KEIP does not satisfy applicable law as it does not require a "stretch" or "reach" for the proposed KEIP Participants (defined herein). Notwithstanding the Debtors' conclusory and self-serving statements in the Bonus Compensation Motion to the contrary, the proposed KEIP is a disguised retention bonus plan, not an incentive plan. The Debtors have not identified any specific tasks or roles that each of the KEIP Participants have undertaken or will perform that will enhance the sale process or reorganization value of the Debtors' businesses. Nevertheless, under the proposed KEIP, certain employees and senior management will be rewarded with at least $2.1 million in the aggregate, and more likely, at least $4.1 million in the aggregate, based on various Funding and Performance Metrics that are inappropriate, illusory and/or require no extraordinary effort beyond the routine duties and responsibilities of the KEIP Participants.

4. The KEIP also fails to tie any reward to KEIP Participants to improving the sale proceeds to a level approaching fair market value for the Downstream Business or resulting in a recovery to unsecured creditors. Given the absence of a clear link between the KEIP and any

demonstrable contribution by the KEIP Participants to the sale price, the proposed KEIP serves no legitimate purpose.

5. The proposed KEIP is also objectionable because the aggregate cost far exceeds industry standards based on a review of bankruptcy sale transactions of comparable size.

6. Similarly, the KERP cannot be approved under applicable law. The Debtors fail to meet their burden of showing that the KERP participants are not insiders. To the extent any KERP Participants are truly non-insiders, the proposed bonuses of approximately $900,000 to 34 employees of the Upstream Business are not justified by the facts and circumstances of these cases as required by the Bankruptcy Code and do not constitute a sound exercise of the Debtors' business judgment. Payments under the KERP are excessive, especially when added to the payments proposed under the KEIP, ICP and MSP.

7. The ICP and MSP are equally as objectionable as the KEIP and KERP. Both appear to be disguised KEIPs or KERPs as they seek to incentivize the Debtors' employees and senior management to remain with the company until the Debtors can complete the sale of the Downstream Business. However, the Debtors undoubtedly realized that to expand the scope of the KEIP and/or KERP would have failed because (i) the ICP and MSP do not set sufficient goals to legitimately incentivize employees to maximize value, and (ii) incorporating the benefits of these plans into the KEIP/KERP would have further inflated the already overly burdensome above-market KEIP and KERP bonus structures.

8. Moreover, there is simply no need for the ICP, which is essentially a KEIP/KERP for the Downstream Business, as it is in the best interests of these employees to remain in the Debtors' employ through closing on the sale of the Downstream Business in order to maximize their opportunity to be offered employment by the purchaser of that business. Further, the

Debtors propose to pay the ICP to employees that accept employment with the purchaser of the Downstream Business or that are terminated as a cause of the sale. At a minimum, the ICP must be modified such that payments pursuant to the ICP are terminated or substantially reduced if such employees are offered employment with the purchaser of the Downstream Business.

9. Finally, the MSP must not be approved because the Debtors have failed to provide sufficient details to permit a full analysis of the plan. In fact, it is impossible for the Court, or any party for that matter, to understand the MSP, not due to any level of complexity, but simply because the Debtors provide almost no information as to the scope or cost of the MSP and the benefit to the Debtors' estates. As such, it is impossible for the Court to consider whether or not the MSP is reasonable, in the best interest of the Debtors' estates or a sound exercise of the Debtors' business judgment.

10. As discussed throughout this Omnibus Objection, there is a very real possibility that the sale of the Downstream Business will leave the Debtors' estates administratively insolvent and unable to fund a sale process for the Upstream Business or confirmation of a chapter 11 plan. Since these Chapter 11 Cases are being administered solely for the benefit of the Secured Lenders, all expenses incurred by the Debtors through the Compensation Plans to incentivize employees to assist in this process should be borne by the Secured Lenders and not the unsecured creditors.

FACTUAL BACKGROUND

A. The Debtors' Businesses

11. The Debtors claim to be "one of the country's largest integrated producers of primary aluminum and high-quality rolled aluminum coils." *See* Declaration of Dale W. Boyles in Support of Chapter 11 Petitions and First Day Motions (the "Boyles Declaration") at

¶ 5 [Docket No. 5]. The Debtors operate their businesses through two main business lines: the "Upstream Business" and the "Downstream Business."

i. The Upstream Business

12. Through their Upstream Business, the Debtors are one of the largest U.S. producers of primary aluminum. *Id.* at 9. The Upstream Business is vertically integrated, consisting of three separate segments: (i) the St. Ann Segment consisting of the Debtors' bauxite mining operations in St. Ann, Jamaica; (ii) the Gramercy Segment consisting of the Debtors' alumina refinery in Gramercy, Louisiana; and (iii) the New Madrid Segment consisting of the primary aluminum reduction plant and fabrication facilities located in New Madrid, Missouri.

13. At this time, the Debtors' Upstream Business is not profitable and operates at a substantial loss. Pre-Petition, the Debtors sold nearly half of the bauxite mined from the St. Ann Facility to Sherwin Alumina Co., LLC ("Sherwin") under an unprofitable contract (the "Sherwin Contract") which was rejected by the Debtors by Order of this Court entered on April 7, 2016 [Docket No. 609]. [redacted]

14. [redacted]

[redacted]

15. For the fiscal year ended 2015, the Gramercy segment showed a profit of $12.5 million. Feintuch Declaration at ¶ 10. Nonetheless, future profitability of Gramercy is hampered by labor issues and the fact that its largest customer, Century Aluminum Co. ("Century Aluminum"), an affiliate of Sherwin's parent, has moved to terminate its contract to buy product from Gramercy. Docket No. 283.

16. Prepetition, commodity-grade aluminum produced in the New Madrid Facility was sold to the Debtors' Downstream Business or to other aluminum fabricators. According to the Boyles Declaration, "[t]he challenges confronting the Debtors were exacerbated when, on August 4, 2015, a molten metal explosion occurred in the casthouse of the New Madrid Facility, where molten aluminum is converted into commodity and value added products." "Additionally, on January 7, 2016, the Debtors lost power to two of the three pot-lines for smelting primary aluminum at the New Madrid Facility when an electrical circuit failed." *See* Boyles Dec. at ¶ 33. As a result of these events, the Debtors have shut down operations at the New Madrid Facility. In fact, the DIP Lenders (defined herein) insisted that the failure to close this facility by not later

than March 24, 2016 would be an event of default under the DIP Financing Agreement. *See, infra*, Final DIP Order, ¶ 18. [redacted]

17. In sum, at the present time, the Upstream Business is cash flow negative and unprofitable and will likely continue to burn cash until the complex issues related to the Government of Jamaica levy, sales of bauxite to Sherwin or another customer (or reduction in production levels), [redacted] and labor issues are resolved. The Committee is hopeful that the Debtors will favorably resolve these issues, but this will take time. And, the Debtors' current rushed sale process of the cash flow positive Downstream Business will severely curtail the time available to fix the Upstream Business.

ii. The Downstream Business

18. The "Downstream Business" is one of the largest aluminum foil producers in North America. Boyles Dec. at ¶ 13. The Downstream business produces heavy gauge foil products such as fin stock and semi-rigid container stock, light gauge converter foils, consumer foils and light gauge sheet products such as transformer windings and building products. *Id.*

19. [redacted]

[redacted]

B. The Debtors' Chapter 11 Cases and DIP Financing and Milestones

20. On February 8, 2016, (the "Petition Date"), each of the Debtors filed a voluntary petition for relief under chapter 11 of the Bankruptcy Code (these "Chapter 11 Cases").

21. On February 8, 2016, the Debtors filed the *Debtors' Motion for Entry of Interim and Final Orders to (I) Authorize Debtors in Possession to Obtain Post-Petition Financing Pursuant to 11 U.S.C. §§ 105, 362m 363 and 364, (II) Grant Liens and Superpriority Claims to Post-Petition Lenders Pursuant to 11 U.S.C. §§ 364 and 507, (III) Provide Adequate Protection to Pre-Petition Credit Parties, (IV) Modify Automatic Stay Pursuant to 11 U.S.C. §§ 361, 362, 363, 364 and 507, (V) Schedule Final Hearing Pursuant to Bankruptcy Rules 4001(B) and (C) and Bankruptcy Rule 4001-2; and (VI) Grant Related Relief* (the "DIP Motion") [Docket No. 32], seeking, among other things, approval to obtain $165 million in postpetition financing from (i) Bank of America, acting as administrative and collateral agent for itself and a syndicate of banks, financial institutions and other institutional lenders party to the Pre-Petition ABL Loan Agreement and (ii) certain lenders party to the Debtors' Pre-Petition Term Loan Agreement (collectively, the "DIP Lenders"). As of the Petition Date, the Debtors owed approximately $61.5 million on account of the Pre-Petition ABL Loan Agreement and $486 million on account of the Pre-Petition Term Loan Agreement. *See* DIP Motion, ¶ 13.

22. As a condition to obtaining postpetition financing, the DIP Lenders required the Debtors to meet certain milestones in these Chapter 11 Cases, many of which related to the sale

of the Downstream Business. As initially proposed in the DIP Motion, the Debtors were required to proceed with the marketing, auction, and sale of the Downstream Business by June 7, 2016, a mere one-hundred and twenty (120) days of the Petition Date (the "Proposed Sale Milestones"). *See* DIP Motion, ¶ 24.

23. On March 2, 2016, the Committee filed its objection to the DIP Motion (the "DIP Objection") [Docket No. 294], arguing, among other things, that the Proposed Sale Milestones were unnecessary given the financial condition of the Debtors' Downstream Business and prejudicial to the Committee as it prevented the Committee, and any other key constituents, from fully analyzing and considering the sale of the Downstream Business and whether it is the best path forward to maximize value of the Debtors' estates. *See* DIP Objection, ¶ 1.

24. In light of the DIP Objection, the Debtors and DIP Lenders agreed to extend the Proposed Sale Milestones by four (4) weeks to: (i) allow the Debtors' professionals additional time to market the sale of the Downstream Business; (ii) provide the Committee additional time to conduct due diligence in connection with the Debtors' businesses; and (iii) allow Committee professionals to determine the impact of the sale of the Downstream Business on the Debtors' estates, the Debtors' ability to reorganize the remaining portions of the Debtors' business, and the likelihood of a distribution to general unsecured creditors. The Committee expressly reserved its right to object to the Downstream Sale Process.

25. On March 11, 2016, the Court entered the *Final Order Granting Debtors' Motion to (I) Authorize Debtors in Possession to Obtain Post-Petition Financing Pursuant to 11 U.S.C. §§ 105, 362, 363, and 364; (II) Grant Liens and Superpriority Claims to Post-Petition Lenders Pursuant to 11 U.S.C. §§ 364 and 507; (III) Provide Adequate Protection to Pre-Petition Credit Parties; (IV) Modify Automatic Stay Pursuant to 11 U.S.C. §§ 361, 362, 363, 364, and 507; and*

(V) Grant Related Relief [Docket No. 392] (the "Final DIP Order"), which incorporated the settlement of the Committee's DIP objection.

C. The Debtors' Downstream Sale Process

26. On February 29, 2016, the Debtors filed the *Debtors' Motion for (I) An Order Establishing Bidding Procedures for the Sale of the Downstream Business and Granting Related Relief and (II) An Order Approving the Sale of the Downstream Business* (the "Sale Motion") [Docket No. 272]. By the Sale Motion, the Debtors sought approval of, among other things, the procedures (the "Bidding Procedures") by which they will solicit and select the highest or otherwise best offer for the sale of the Downstream Business, together with any assets, facilities, real property, personal property, plants, equipment, inventory, and accounts receivable associated therewith, and any one or more categories of the Debtors' assets (collectively, the "Downstream Assets") either through a sale to one purchaser or multiple sales to multiple purchasers. On March 21, 2016, the Bankruptcy Court entered an order (the "Bidding Procedures Order") [Docket No. 471] which approved the Bidding Procedures and incorporated the Downstream Business Milestones.

27. Pursuant to the DIP Order, upon the sale of the Downstream Business, the liens and claims of the Term DIP Lenders, ABL DIP lenders, Pre-Petition ABL lenders and the Pre-Petition Term lenders (collectively, the "Secured Lenders") shall attach to the proceeds from the sale of Downstream Business in accordance with the provisions of the DIP Order and the intercreditor agreement between the lenders (after giving effect to the reduction in debt of any party who purchases assets by means of a credit bid), and (A) the ABL DIP Lenders and Pre-Petition ABL Lenders, as applicable, shall receive at or promptly after closing of the sale of the Downstream Business all proceeds of ABL Priority Collateral sold in the Downstream Asset Sale, and (B) the Term DIP Lenders and Pre-Petition Term Lenders, as applicable, shall receive

at or promptly after closing of the Downstream Asset Sale all proceeds of Term Priority Collateral sold in the Downstream Asset Sale. The Secured Lenders also claim they are loss payees on the Debtors' insurance policies, and assert lien rights as to insurance proceeds, including the proceeds to which the Debtors may be entitled in light of significant casualties and losses at the New Madrid Facility.

28. On March 9, 2016, PJT Partners ("PJT"), the Debtors' investment banker, launched the marketing process for the sale of the Downstream Business. [redacted]

29. Since its formation, the Committee has repeatedly voiced vehement concerns regarding the sale of the Downstream Business and the Debtors' overall restructuring strategy in these Chapter 11 Cases. In short, the Debtors are running a backwards reorganization and sale process for the benefit of the DIP Lenders and to the detriment of all other creditors and constituencies in these Chapter 11 Cases.

30. [redacted]

[1] While Gramercy on its own reports a profit, it is best to consider the Upstream Business segments as a whole given the interrelatedness of operations.

[redacted] In contrast, the Upstream Business is not currently viable because it currently has a large negative cash flow and, as a whole, has incurred a net operating loss of $25.8 million for year ending 2015, excluding any allocation between Upstream and Downstream of the $30.4 million of corporate expenses. Feintuch Declaration at ¶ 16. Further, based on the Committee's review of the Debtors' financial projections and reports, the Debtors need the positive cash flow from the Downstream Business to afford them sufficient time to maximize the value of the Upstream Business. This time is required for the Debtors to, among other things, resolve the issues related to Sherwin, Century, the Jamaican levy and other matters that could positively affect the value of that business.

31. Simply put, the Debtors cannot justify selling the Downstream Business based on the currently contemplated rushed timeline, where more time is needed to resolve the issues that could favorably impact the value of the Upstream Business. The Committee is concerned that going forward on the current trajectory of a rushed process, which the Debtors' KEIP targets encourage, will result in a sale of the Downstream Business for less than the amount of the Debtors' secured debt. Unless the Debtors retain sufficient sales proceeds, the estates will be left administratively insolvent and unable to fund a sale or reorganization of the Upstream Business, or for that matter, any chapter 11 plan in these cases. As such, the Debtors are not acting within their sound business judgment in pursuing the sale of the Downstream Business or requesting approval of the Compensation Plans that incentivizes management to pursue that misdirected course of action.

D. The Debtors' Compensation Motions

32. On April 20, 2016, the Debtors filed the Bonus Compensation Motion seeking permission to implement the KEIP, KERP and 2015 Incentive Compensation Plan, and the MSP Motion for approval to implement the modified severance program.

i. The KEIP

33. The KEIP applies to five (5) senior level executives who are "insiders" of the Debtors under section 101(31) of the Bankruptcy Code (the "Insider KEIP Participants") and fourteen (14) alleged non-insider employees (the "non-Insider KEIP Participants" and, collectively with the Insider KEIP Participants, the "KEIP Participants"). The Insider KEIP Participants include: the Chief Executive Officer, the CCO/President of Flat Rolled Products, the Chief Financial Officer, the General Counsel/Vice President of Human Resources, and the Vice President of Manufacturing.

34. Under the proposed KEIP, the Debtors seek authority to pay aggregate bonuses (the "KEIP Bonuses") of $1,033,879 at the minimum threshold level (the "KEIP Threshold Bonus"), $2,067,758 at the target level (the "KEIP Target Bonus"), and $4,135,517 at the maximum level (the "KEIP Maximum Bonus"). Non-Insider KEIP Participants are entitled to a floor, or minimum payment, of one-third of their annual compensation.

35. The KEIP Bonuses are based on two types of metrics: (1) Funding Metrics; and (2) Performance Metrics. The Funding Metrics account for fifty (50%) percent of the value of the KEIP Bonuses. [redacted]

[redacted]

36. The remaining Funding Metrics are based on measuring cumulative cash flow against the DIP Budget for individual business operations as well as those operations on a consolidated basis (the "Cash Flow Funding Metrics"). The individual business operations to be measured include: (i) Flat-Rolled Aluminum Segment (or Downstream Business); (ii) St. Anne Segment (bauxite mining); (iii) Gramercy Segment (alumina refinery); and (iv) New Madrid Segment (aluminum reduction plant and fabrication).

37. The Performance Metrics, which account for the remaining 50% of the KEIP Bonuses, are individualized for each KEIP Participant and include:

- achieving sales targets per the budget through emergence date (the "Target Sales Metric");
- achieving established EH&S targets (for operating entities only) (the "EH&S Target Metric");
- increasing smelter grade alumina shipped to [redacted] Sales Metric");
- confirming a plan of reorganization or sale of the Upstream Business by a date certain (based on timing of motion) (the "Upstream Business Metric");
- reducing the pre-petition claims of critical vendors, foreign vendors, shippers and old lienholders by 50% (the "Critical Vendor Metric");
- maintaining business expenses $1 million below budget per location (the "Business Expense Reduction Metric");
- finalizing an environmental study in connection with closing the Upstream Business by May 29 (the "Environmental Study Metric");
- achieving a fabrication revenue of $180 million for the Downstream Business on an annualized basis for 2016 shipments (the "Target Fabrication Revenue Metric");
- resolution of insurance claims for the New Madrid facility (the "New Madrid Insurance Metric");

- achieving [redacted] of Chemical Grade Alumina at Gramercy Segment on annualized basis for 2016 (the "Gramercy Production Metric");
- meeting or staying under the benefits budget through emergence from Bankruptcy (the "Target Benefits Metric");
- [redacted]
- selling assets of New Madrid Segment by date certain (based on timing of motion) (the "New Madrid Asset Sale Metric");
- resolving Union negotiations by May 29 sufficiently to support 1113 process (the "Union Negotiations Metric"); and
- obtaining post-petition trade terms (including with metal suppliers) of at least 15 days payable outstanding from filing to emergence (the "Trade Terms Metric")[2].

38. Each KEIP Participant is assigned at least two, but no more than three, of the various Performance Metrics and each is given equal weight in calculating an individual KEIP Participant's KEIP Bonus.

39. The KEIP Bonuses are earned upon the earlier of (i) emergence from chapter 11, (ii) the closing of a sale of the applicable unit of the Debtors' Upstream Business pursuant to section 363 of the Bankruptcy Code, or (iii) the date of a wind down of such business unit.

40. Nowhere does the Motion explain what each KEIP Participant's role is relative to the various metrics.

ii. The KERP

41. The Debtors also seek authorization to pay thirty-four (34) employees of the Upstream Business (the "KERP Participants") $895,763 in KERP bonuses (the "KERP Bonuses"), with a per-participant cost averaging $26,346. The KERP Participants are assigned to one of three tiers, where the calculation of the KERP Bonuses is expressed as a percentage of

[2] Under the Debtors' KEIP, accomplishing trade terms of 15 days payables are two separate metrics; one for non-metal suppliers and the other for metal suppliers. Upon information and belief, the Debtors' reason for making two separate metrics was so that it could separately incentivize two different KEIP Participants. For purposes of this Omnibus Objection, however, both can be considered a single combined metric.

the employee's base salary. KERP Participants in KERP Tier A would receive 30% of their base salary, Tier B would receive 20%, and Tier C would receive 10%. The KERP Participants are eligible for the KERP Bonuses as long as they remain employed by the Debtors up to the payment date. The proposed KERP Bonuses are payable upon emergence from bankruptcy.

iii. The 2015 Incentive Compensation Program

42. The Debtors also seek authorization to pay $1.4 million to all non-insider on-site salaried employees in the Downstream Business (the "ICP" and "ICP Participants," respectively). The ICP is in addition to an already existing incentive compensation program in the amount of $4.3 million which the Debtors obtained authority to pay pursuant to their first day motions. The Debtors claim that maintaining and extending the ICP to the ICP Participants will reward them for 2015 performance of the Downstream Business and maintain morale and value of the Downstream Business until its sale. The ICP is payable to ICP Participants (i) who are offered and accept employment with the purchaser of the Downstream Business, or (ii) who are terminated without cause in connection with the sale of the Downstream Business.

iv. The Severance Programs

43. Pursuant to the Severance Compensation Motion, the Debtors seek authority to modify a prepetition severance program for senior managers (the "Modified Senior Management Severance Program") and a separate severance program for salaried employees that are ineligible to participate in the Senior Management Severance Program (the "Modified Salaried Employee Severance Program" and with the Modified Senior Management Severance Program, the "Modified Severance Programs" or "MSPs"). Pursuant to the Modified Severance Programs, the employee participants (the "Modified Severance Program Participants") will be entitled to the lesser of (a) what such Modified Severance Program Participant would have received under the

original severance program and (b) three (3) months' pay. Modified Severance Program Participants will include those eligible employees who are involuntarily terminated, other than for reasons related to misconduct, short-term reductions in force, or a refusal of reassignment. Noticeably absent from the Severance Compensation Motion is any estimate of how much the Modified Severance Programs will cost the Debtors and their estates.

OBJECTION

I. THE KEIP CANNOT BE APPROVED

A. The KEIP Is A Disguised Retention Plan That Is Prohibited Under Section 503(c)(1) Of The Bankruptcy Code

44. Section 503(c)(1) of the Bankruptcy Code strictly limits bonusing an insider of a debtor as a means to inducing that person to simply remain employed by the debtor. Section 503(c) of the Bankruptcy Code "was enacted to limit a debtor's ability to favor powerful insiders economically and at estate expense during a chapter 11 case." *In re Pilgrim's Pride Corp.*, 401 B.R. 229, 234 (Bankr. N.D. Tex. 2009). The provision supports "Congress's [sic] effort to eradicate the notion that executives were entitled to bonuses simply for staying with the Company through the bankruptcy process." *In re Global Home Prods.*, LLC, 369 B.R. 778, 784 (Bankr. D. Del. 2007) (internal quotation omitted).

45. Section 503(c)(1) establishes for insiders a "high hurdle[] to clear if payments are primarily designed for retention." *Global Home Prods*., 369 B.R. at 785. Specifically, under section 503(c)(1), a retention-type payment to an insider "shall neither be allowed, nor paid" absent a finding by the bankruptcy court, based upon evidence in the record, that: (a) the individual has a bona fide job offer from another business at the same or greater rate of compensation; (b) the services provided by the individual are essential to the survival of the

business; and (c) the payments meet the strict monetary test set forth in 503(c)(1)(C). 11 U.S.C. § 503(c)(1).

46. The Debtors' characterization of the proposed KEIP as a performance-based incentive program is not determinative of whether section 503(c)(1) of the Bankruptcy Code applies. Courts recognize that debtors often mischaracterize a retention program as an incentive program in order to escape the more stringent requirements of section 503(c)(1). *See In re Velo Holdings Inc*., 472 B.R. 201, 209 (Bankr. S.D.N.Y. 2012) ("Attempts to characterize what are essentially prohibited retention programs as 'incentive' programs in order to bypass the requirements of section 503(c)(1) are looked upon with disfavor"); *In re Hawker Beechcraft, Inc*., 479 B.R. 308, 312 (Bankr. S.D.N.Y. 2012) ("the threshold question . . . is whether the KEIP is a true incentive plan, or instead, a disguised retention plan."); *In re Dana Corp.*, 351 B.R. 96, 102, n3 (Bankr. S.D.N.Y. 2006). ("if [an incentive bonus plan] walks like a duck (KERP), and quacks like a duck (KERP), it's a duck (KERP).").

47. For a bonus plan to be incentivizing, it should be tied to significant goals that are difficult to achieve. *See, e.g., In re Dana Corp*., 358 B.R. 567, 583 (Bankr. S.D.N.Y. 2006) (court approved long-term incentive plan where benchmarks were "difficult targets to reach and [were] clearly not 'lay-ups'"); *Hawker Beechcraft*, 479 B.R. at 313-15 (court rejected proposed bonus plan where lowest levels of proposed metrics were "well within reach," including sales-price metric that was "hardly challenging"); *In re Residential Capital, LLC*, 478 B.R. 154, 171-72 (Bankr. S.D.N.Y. 2012) (court rejected proposed bonus plan where participants had to remain employed by debtors to receive payment, and additional challenging performance metrics were lacking). The proponent of a bonus plan must show that it is a performance-based "pay for

value" plan, not a "pay to stay" plan. *See Residential Capital*, 478 B.R. at 170 (citing *In re Global Home Prods.*, 369 B.R. at 783).

48. The additional work and requirements placed on insiders caused by filing a chapter 11 case and selling assets is not a sufficient reason for increased pay, as that would allow increased compensation in "virtually all chapter 11 cases." *Residential Capital*, 478 B.R. at 168. Courts are uncomfortable authorizing KEIP awards where more than half of the work required to trigger the bonus payments has already been performed. *Id.* at 171 (noting that 63% of the KEIP awards would vest upon the closing of transactions that were already negotiated and holding the result insufficient to render the KEIP primarily incentivizing).

49. When evaluating whether or not a debtor's compensation plan is truly an incentive program or merely a retention program, courts look to the primary purpose of the plan. *See Global Home Prods*., 369 B.R. at 785 (noting that section 503(c)(1) applies "if payments are primarily designed for retention"); *Velo Holdings,* 472 B.R. at 210. "The Court must . . . determine whether the proposed targets are designed to motivate insiders to rise to a challenge or merely report to work." *Hawker Beechcraft*, 479 B.R. at 313. The proponent of a KEIP bears the burden of proving that the plan is not a retention plan governed by section 503(c)(1). *Id.*

50. Notwithstanding the Debtors' conclusory and self-serving statements in the Bonus Compensation Motion to the contrary, the proposed KEIP is a disguised retention bonus plan, not an incentive plan. The KEIP "incentives" fail to motivate or incentivize the KEIP Participants to rise to any difficult future challenges. At best, the proposed KEIP Bonuses consist of oversized rewards for ordinary job performance. There is absolutely no legal or logical basis for allowing a bonus program designed to reward and "incentivize" employees for reaching benchmarks that are a virtual certainty. Of equal concern, as more fully discussed below, certain Funding and

Performance Metrics incentivize the KEIP Participants to work toward targets that would harm the Debtors' estates and diminish value for the other constituents in these Chapter 11 Cases. And, tellingly, payments under the KEIP are not made on reaching the benchmarks, but rather are paid on emergence from bankruptcy or the sale or wind down of the corresponding business segment as is typical in a KERP.

51. The decision by the bankruptcy court in *Hawker* is directly on point with respect to the Debtors' failure to set forth reasonable and meaningful performance goals with respect to the KEIP. In pertinent part, the *Hawker* court found that:

> the Debtors have failed to sustain their burden of proof. At the outset, they did not identify the roles of each member of the [senior leadership team] or why, individually or as part of a team, they will contribute services that are necessary to achieve the targets. Beyond that, although the KEIP includes incentivizing targets, the lowest levels are well within reach.

Hawker, 479 B.R. at 313. Similarly, here, the Debtors fail to articulate why they include each of the nineteen KEIP participants and why they fail to establish any challenging targets. The *Hawker* court made it clear that in order to pass muster, **all levels of an incentive plan must be incentivizing**. *Id*. at 313 (emphasis added).

52. Here, while some of the KEIP Participants may have worked hard in connection with the filing of the Debtors' petitions, the post-petition operations, or proposed sale of the Debtors' Downstream Business, the KEIP Participants' work in that regard falls well within the sphere of their fiduciary duties and responsibilities as senior management - for which they already have been, and continue to be, well compensated. In addition, the Debtors and their management have received and continue to receive assistance of able counsel, investment bankers and financial advisors throughout these cases to deal with the added bankruptcy burdens and to spearhead the sale process.

53. The Funding Metric related to the sale of the Downstream Business is the most problematic. It is both inappropriate under these facts and circumstances as well as completely illusory. First and foremost, the sale of the Downstream Business based on the current milestones is not in the best interest of the Debtors' estates. As discussed throughout this Omnibus Objection, there is a very real possibility that the sale of the Downstream Business will leave the Debtors' estates administratively insolvent and unable to fund a sale process for the Upstream Business or confirmation of a chapter 11 plan and, therefore, the Downstream Sale Metric is not a proper incentive for the KEIP Participants. Second, should the Court disagree with the Committee's position and conclude that the sale of the Downstream Business is a proper metric to consider, the Downstream Sale Metrics are set far too low and do no not constitute a reach to achieve. [redacted]

54. The Cash Flow Funding Metrics are similarly troublesome in that they do not constitute a "reach" and are easily attainable.

55. The Cash Flow Funding Metrics for the first quarter for each business was evaluated against the DIP budget, which by its very nature is a conservative projection that must be complied with in order to avoid a default under the DIP Loan. That these benchmarks are not

a "reach" is clearly evidenced by the fact that, per the Debtors' "Upstream Business Plan," each of the businesses achieved the maximum payout threshold for the first quarter.

56. For the period beginning April 1 through emergence from bankruptcy, cash flow will be measured against the Upstream Business Plan, without regard to first quarter performance. The Debtors' Upstream Business Plan is also not a reach given that it is based on conservative assumptions and was designed to be acceptable to the DIP Lenders as required by the Final DIP Order.

57. In addition, the Upstream Business Plan could be over or understated based on numerous assumptions. A change in circumstances could lead to KEIP Participants meeting or even exceeding KEIP targets without actually overachieving or even achieving the Upstream Business Plan metrics. For example, at St. Ann, a reduction in the levy imposed by the Government of Jamaica could significantly reduce the cost of production and hide a lot of other missteps with respect to cash flow outcomes. [redacted]

58. At Gramercy, the Cash Flow Funding Metrics could be exceeded simply as a result of an expected material increase in pricing for commercial grade alumina without any regard to actual performance by management. Similarly, the Cash Flow Funding Metric for the Downstream Business could be exceeded due to an anticipated increase in the pricing of LME, and cash flow forecasts at New Madrid could be exceeded simply by obtaining a favorable reduction in real estate taxes or power costs.

59. Further, the KEIP Bonuses based on Cash Flow Funding Metrics (based on allegedly positive DIP Budget variances), may actually serve to encourage actions not in line with the best interests of the Debtors' estates and creditors. Because the Cash Flow Funding Metrics are based on beating the DIP Budget or Upstream Business Plan by not using cash – even for appropriate uses, the KEIP Participants may cause the Debtors to shy away from paying active vendors, certain creditor settlements or critical vendor payments to meet acceptable cash variances in order to maximize their personal compensation under the KEIP. This is the exact opposite of how an incentive plan should be structured.

60. Similarly, various Performance Metrics proposed by the Debtors also incentivize the KEIP Participants to work toward results which may in fact harm the Debtors' estates, rather than benefit them. These inherently inappropriate Performance Metrics include the following:

- [redacted]

- *Union Negotiations Metric* – the Debtors provide no detail, limitations or parameters on the form or substance of a resolution with the Union to satisfy this Performance Metric. While resolution with the Union is important for the viability of the Downstream Business, it is not without limits and those limits must be well defined and disclosed in order to properly incentivize KEIP Participants, rather than to incentivize them to merely get to a deal quickly.

- *New Madrid Asset Sale Metric* – the Debtors fail to provide any minimum threshold pricing targets or timing for the sale of the New Madrid assets. Rather, this metric only requires a sale "within 90 days of filing sale process motion." To properly incentivize the eligible KEIP Participant(s), the Debtors must define minimum values and outside date to truly maximize value for the estates.

- *New Madrid Insurance Metric* - the Debtors fail to provide any minimum threshold or timing for the resolution of the insurance claims on account of the damage to the New Madrid facility. To properly incentivize the eligible KEIP Participant(s), the Debtors must define minimum values and outside dates to truly maximize value for the estates.

- *Target Benefits Metric* – this metric may actually serve to encourage actions not in line with the best interests of the Debtors' estates and creditors. Because the Target Benefits Metric is based on beating the DIP Budget by not using cash – even for appropriate uses such as medical benefits to employees, the KEIP Participants may cause the Debtors to shy away from paying medical benefits to employees to reduce the cash variance for fear of a reduction in their personal compensation under, the KEIP. This is likely to cause attrition and instability among the Debtors employees and is the exact opposite of how an incentive plan should be structured.

- *Sales Pipeline Metrics* – Certain sales pipeline metrics are flawed in that they attempt to incentivize employees based on sales targets and not profitability. This potentially incentivizes employees to sell product at low prices, damage the Debtors' profitability, and be rewarded for doing so.

61. The Committee also takes issue with various Performance Metrics which are not truly incentivizing because they do not require any real reach or challenging performance. Specifically, the following Performance Based Metrics include the following:

- *EH&S Target Metric* – the Debtors have not provided any detail on this metric so it is impossible to determine whether this metric constitutes a sufficient reach.

- [redacted]

- *Business Expense Reduction Metric* – This metric requires a $1 million expense reduction at both St. Ann and Gramercy. The proposed metric represents a cost savings of 1.3% of total costs at St. Ann and .4% of total costs at Gramercy and is no reach at all. The cost reduction is also fixed and doesn't vary over time or with production levels. Thus, the metric could be met simply by St. Ann or Gramercy experiencing a production issue that shuts the plants down. Although this would be a negative for the Debtors' estates, the expense reduction could be met due to lack of production.

- [redacted]

62. Lastly, the Committee objects to the KEIP to the extent certain Performance Metrics only require the KEIP Participants to perform such KEIP Participants routine duties and tasks intrinsic in their employment. Specifically those Performance Metrics include the following:

- *New Madrid Insurance Metric* – surely resolution of insurance claims is not a task that requires special incentive. The need to resolve insurance claims is not a product of or rendered any more difficult as a result of the Debtors' bankruptcy. This is a function that is ordinary and routine in any enterprise and is not deserving of any incentive.

- *Environmental Study Metric* – finalizing a necessary environmental study seems less like a value enhancing task, and more like a legal requirement incumbent on an enterprise such as the Debtors. Further, the Debtors fail to disclose what, if any, extraordinary effort this responsibility requires. Indeed, the Debtors have already contracted a third-party to perform the study. It is the Debtors' burden to demonstrate the justification for this metric, which they have not met.

63. In addition, the Upstream Business Metric is objectionable as it does not set a floor for sale price, nor any parameters for a plan of reorganization. As such, it does not specifically incentivize the KEIP Participants' performance, and does not necessarily require any active or challenging achievement on their part. Further, as previously stated, the Debtors have engaged numerous professionals in these Chapter 11 Cases including an outside CRO, legal restructuring counsel, financial advisors, and an investment bank. Any obligations by the eligible KEIP Participants would likely be derivative of their efforts and only reactive. Further, this is exactly the type of benchmark that would allow increased compensation in "virtually all Chapter 11 cases." *Residential Capital*, 478 B.R. at 168.

64. The KEIP should be denied because the low performance thresholds virtually guarantee the KEIP Participants big bonuses, including for achieving results without any clear connection to achievements by those KEIP Participants. The KEIP is nothing more than a disguised retention plan that is prohibited under section 503(c)(1) of the Bankruptcy Code.

B. The Proposed KEIP is Neither Justified By The Facts And Circumstances of The Chapter 11 Cases Nor A Sound Exercise of The Debtors' Business Judgment

65. Alternatively, even if the Court were to determine that the KEIP is appropriately labeled an incentive (and not a retention) plan—which the Committee disputes for the reasons set forth above—approval of the KEIP should still be denied because the KEIP does not meet the requirements of sections 363(b)(1) and 503(c)(3) of the Bankruptcy Code. The KEIP is not an exercise of the Debtors' sound business judgment under section 363(b)(1) of the Bankruptcy Code, and it is "not justified by the facts and circumstances of the case" as required by section 503(c)(3) of the Bankruptcy Code.

66. Section 503(c)(3) of the Bankruptcy Code states that notwithstanding section 503(b) (which provides for payment of administrative expenses), there shall neither be allowed, nor paid-

> other transfers of obligations that are outside the ordinary course of business and not justified by the facts and circumstances of the case, including transfers made to, or obligations incurred for the benefit of, officers, managers, or consultants hired after the date of the filing of the petition.

11 U.S.C. § 503(c)(3) (emphasis added).

67. Some courts hold that the "facts and circumstances" test under section 503(c)(3) is essentially no different than the lower threshold "business judgment" test that courts apply in determining whether to approve a debtor's transactions outside of the ordinary course of business under section 363(b)(1). *See, e.g., In re Borders Group, Inc.*, 453 B.R. 459, 473 (Bankr. S.D.N.Y. 2011). However, other courts reject this approach and hold debtors to a higher standard. *See In re Pilgrim's Pride Corp.*, 401 B.R. 229, 236–37 (Bankr. N.D. Tex. 2009) (standard for approval under section 503(c)(3) is higher than the business judgment test; if

payments to employees outside the ordinary course were only subject to the business judgment test, then the language of section 503(c)(3) would be rendered meaningless) (citations omitted).

68. The *Pilgrim's Pride* court stated "the test of section 503(c)(3) should not be equated to the business judgment rule as applied under section 363(b)(1)" because to do so would make section 503(c)(3) redundant. *Pilgrim's Pride,* 401 B.R. at 236. The *Pilgrim's Pride* court further asserted that "the conditioning of approval of covered transfers and obligations upon their being 'justified by the facts and circumstances of the case'" suggested that "Congress intended the court to play a more critical role in assessing transactions" that fell within the ambit of section 503(c)(3). *Id.* (internal citations omitted). Moreover, when a court applies the "simple business judgment test" it is "adjured to defer to the debtor in possession or trustee" and, therefore, "if a valid business reason is shown for a transaction, the transaction is to be presumed appropriate." *Id.* However, under section 503(c)(3), "even if a good business reason can be articulated for a transaction, the court must still determine that the proposed transfer or obligation is justified in the case before it." *Id.* at 237.

69. Accordingly, the Debtors must be required not only to show that there is a valid business reason for the proposed KEIP, which they have failed to do beyond conclusory statements, but also to demonstrate that the proposed KEIP Bonuses are justified in these cases and will serve the interests of the Debtors' estates and creditors. *See Pilgrim's Pride*, 401 B.R. at 237 ("[E]ven if a good business reason can be articulated for a transaction, the court must still determine that the proposed transfer or obligation is justified in the case before it. The court … must make its own determination that the transaction will serve the interests of creditors and the debtor's estate. Put another way, when a transaction is proposed between a debtor and its

insiders, the court cannot simply rely on the debtor's business judgment to ensure creditors and the debtor's estate are being properly cared for.").

1. The Proposed KEIP Is Not Justified By The Facts And Circumstances Of These Chapter 11 Cases

70. In the instant cases, the Debtors agreed early on with the Secured Lenders to embark on an expedited sale process to sell the cash flow positive and profitable Downstream Business. Under the milestones set forth in the DIP Financing Agreement, only after the sale process for the Downstream Business was well underway were the Debtors required to produce a business plan for the currently cash flow negative and unprofitable Upstream Business. [redacted]

71. Implementing an expedited sale process under the circumstances here would be an abuse of section 363. The Second Circuit Court of Appeals in *In re Lionel*, 722 F.2d 1063, 1071 (2d Cir. 1983), established a valid business purpose test for determining whether assets should be sold pursuant to section 363 of the Bankruptcy Code. The valid business purposed test listed non-exclusive factors to be considered in analyzing a sale motion, including the proportionate value of the assets to be sold to the value of the business as a whole, the amount of time elapsed since the petition date, the likelihood that a plan would be proposed and confirmed in the near future, the effects of the proposed sale on the prospects for reorganization, the proceeds to be obtained and whether the asset is increasing or decreasing in value. The *Lionel*

factors are based on the concept that the sale of assets is an incremental step in the plan process, not a means of disposing of the chapter 11 case in its entirety.

72. Because of the change in the way chapter 11 cases are run today, courts have suggested different criteria for evaluating section 363 sales. In *In re: General Motors*, 407 B.R. 463, 490 (Bankr. S.D.N.Y. 2009), the court continued to embrace the *Lionel* factors, but added four additional factors: (a) whether the estate has the liquidity to survive until plan confirmation; (b) whether the sale opportunity will still exist at plan confirmation; (c) if not, how likely is it that there will be a satisfactory alternative sale opportunity or a stand-alone plan alternative that is equally desirable or better for creditors; and (d) is there a material risk that by deferring the sale, the patient will die on the table.

73. Each of the foregoing factors militates heavily in favor of not proceeding with an expedited 363 sale process in these Chapter 11 Cases. Clearly, the "need for speed" here is not a "medical emergency." The rushed sale process is designed to liquidate the Debtors' most valuable business segment in order to repay the claims of the ABL DIP Lenders and afford the lenders in the DIP Term Facility and Pre-Petition Term Facility the opportunity to acquire the profitable Downstream Business through a credit bid. The Debtors should not be permitted to sell the cash flow positive and profitable Downstream Business under Section 363 of the Bankruptcy Code under these circumstances. Rather, the Debtors should address the reorganization or sale of their business segments through a plan of reorganization which will afford all creditors the full panalopy of rights afforded to them by Congress in enacting the Bankruptcy Code, including, but not limited to assurances that all administrative expenses will be timely paid.

74. Against this backdrop, the Debtors seek approval of a KEIP which could pay their executives as much as $4.1 million, together with other bonus programs that will add another $2.3 million of KERP and incentive compensation bonus payments to the Debtors' executives and employees. [redacted] In addition, the Performance Metrics established by the KEIP, do not appear to be incentives that require significant performance by Debtors' executives and employees, but rather appear to be simply requirements of their employment, including filling sales pipelines for the flat-rolled business and Gramercy Segment, idling the New Madrid Segment, achievement of sales targets, achieving EH&S targets, delivery of a transition services plan, reducing critical vendor payments, obtaining post-petition trade terms, meeting benefits budget, reducing expenses and finalizing an environmental study. Similarly, the Cash Flow Funding Metrics also do not appear to be a reach and are set too low so that they are easily achievable as evidenced by the fact that for the first quarter all participants achieved the Maximum Payout per the proposed KEIP.

75. The KEIP should, therefore, be denied as it is not justified under the facts and circumstances of these Chapter 11 Cases.

2. <u>The Proposed KEIP is Not a Sound Exercise of the Debtors' Business Judgment</u>

76. Even if the Court were to determine, as the Debtors urge, that the "business judgment" standard applies to approval of the KEIP, the KEIP fails to satisfy that standard as well. In determining whether a proposed compensation plan and the process of developing that

plan represent an exercise of a debtor's sound business judgment, bankruptcy courts examine the following six factors:

> (a) Is there a reasonable relationship between the plan proposed and the results to be obtained, *i.e.*, will the key employee(s) stay for as long as it takes for the debtor to reorganize or market its assets, or, in the case of a performance incentive, is the plan calculated to achieve the desired performance?
>
> (b) Is the cost of the plan reasonable in the context of the debtor's assets, liabilities and earning potential?
>
> (c) Is the scope of the plan fair and reasonable; does it apply to all employees; does it discriminate unfairly?
>
> (d) Is the plan or proposal consistent with industry standards?
>
> (e) What were the due diligence efforts of the debtor in investigating the need for a plan; analyzing which key employees need to be incentivized; what is available; what is generally applicable in a particular industry?
>
> (f) Did the debtor receive independent counsel in performing due diligence and in creating and authorizing the incentive compensation?

Global Home Prods., 369 B.R. 778, 786 (Bankr. D. Del. 2007) (*citing In re Dana Corp*., 358 B.R. 567, 576-77 (Bankr. S.D.N.Y. 2006).

77. Relationship Between KEIP and Results to be Obtained. The Debtors' proposed KEIP is not calculated to achieve the desired performance. As discussed above, most of the KEIP Funding Metrics (including the Downstream Sale Metric) and Performance Metrics are illusory and virtually guarantee that KEIP Bonuses will be paid to the KEIP Participants without creating any value for the Debtors' estates.

78. [redacted]

[redacted]

79. Additionally, the Bonus Compensation Motion does not explain how the Debtors' management and other employees who will receive the KEIP Bonuses will add any value to the Debtors' restructuring efforts beyond performance of their jobs. The Bonus Compensation Motion merely states that each KEIP Participant has "the ability to materially impact the efficiency and maximization of creditor recoveries." Bonus Compensation Motion, ¶ 27. However, most of the Performance Metrics (i) are incentivizing the KEIP Participants to take actions that may not be in the best interests of the Debtors' estates, (ii) fail to require any real reach beyond the Debtors' ordinary and historical performance, or (iii) reward KEIP Participants for performing routine duties and tasks appurtenant to their employment.

80. In other words, the Debtors have all but guaranteed their ability to receive the KEIP Bonuses based on the Funding Metrics and Performance Metrics. In addition to the lack of any detail, the Committee believes this simply cannot be supported by any meaningful analysis based on the shortcomings in the various Funding Metrics and Performance Metrics described

above. Accordingly, approval of the KEIP without tying the KEIP Bonuses to any meaningful increase in value with respect to asset sale(s) or business operations is simply not justified here. The Debtors have therefore failed to show a reasonable relationship not only between the KEIP Participants and procuring the highest and best bid for the Downstream Business, but also between the KEIP and the best interests of the Debtors' estates and creditors.

81. The Cost and Scope of the KEIP Is Not Fair or Reasonable. The Debtors have presented no evidence that the cost of the KEIP is reasonable in the context of their assets and liabilities. Given that the Debtors are insolvent, a payout of over $2 million in the aggregate to five insiders and over $2 million to another fourteen non-insiders, on top of generous base salaries and the other ICPs, is not fair or reasonable. Moreover, the KEIP discriminates unfairly by providing for disproportionately large bonuses to senior management. In any event, the fact that the proposed KEIP Participants oversaw the Debtors' pre-bankruptcy steep decline hardly justifies an extraordinary reward to such individuals at the expense of general unsecured creditors and others who supported the Debtors and are now left with large unsecured claims for which they will most likely receive a nominal recovery, if any.

82. Additionally, it remains unclear whether payment under the KEIP, or any of the ICPs will be waived or limited if a KEIP Participant secures new employment with the purchaser of the Downstream Business. Without full disclosure, the Court cannot properly evaluate the KEIP or the other ICPs in order to make an informed decision as to the appropriateness of the proposed ICPs. Payment to KEIP Participants should be adjusted to the extent a Plan Participant secures new employment with the purchaser of the Downstream Business.

83. There is No Evidence that the KEIP is Consistent with Industry Standards. The Debtors' evidence fails to establish that the proposed KEIP is within industry standards. Debtors

assert that they compared the proposed KEIP to KEIPs in bankruptcy cases filed by a peer group of 19 companies (the "Bankruptcy Peers"), and that the aggregate "target payout" under the proposed KEIP falls within the 67th percentile and the per-participant average target payout falls within the 42nd percentile of the payouts in the cases of the Bankruptcy Peers. The Debtors fail to specify whether the KEIPs in the cases of the Bankruptcy Peers were actually approved and whether the proposed payouts were actually made. In addition, the Debtors note that the Bankruptcy Peers were chosen based on the fact that the companies intended to continue operations.

84. In the instant cases, the Debtors do not appear to intend to continue operations as the proposed sale of the cash flow positive and profitable Downstream Business will likely leave these cases administratively insolvent and unable to fund a reorganization or even a sale of the Upstream Businesses. Thus, the peer group for purposes of comparing the proposed KEIP to industry standards should have included companies that did not intend to operate in the future. In addition, the Debtors make generous and unwarranted assumptions regarding the size and circumstances surrounding the KEIP. Most importantly, given the low thresholds proposed here, participants in the KEIP are likely to earn "maximum payouts" rather than "target payouts", so the maximum payout should be used for comparison purposes.

85. In analyzing the proposed KEIP, the Committee's financial advisor, Houlihan Lokey, identified a more applicable set of comparable transactions which were more recent (all in connection with bankruptcies filed after January 1, 2014) and better reflected the size and circumstances of the KEIP in these Chapter 11 Cases. *See* Exhibit I to Feintuch Declaration. Based on Houlihan Lokey's analysis, both the aggregate target payout and the

maximum payout under the proposed KEIP exceed all comparables identified by Houlihan Lokey. *See* Feintuch Declaration at ¶ 27.

86. Based on the Committee's analysis of comparable KEIPs, the Court should measure the KEIP costs as follows:

Total Aggregate KEIP Cost	Debtors' Comparables	Committee Comparables	Noranda KEIP Target	Noranda KEIP Maximum
25th Percentile	$598,369	$790,000	$2,067,758	$4,135,517
75th Percentile	$2,149,869	$1,423,235		

Per Participant KEIP Cost	Debtors' Comparables	Committee Comparables	Noranda KEIP Target	Noranda KEIP Maximum
25th Percentile	$57,190	$132,829	$108,829	$217,659
75th Percentile	$222,500	$210,625		

See Feintuch Declaration at ¶ 28.

87. Whether the Court adopts the Debtors' comparable analysis, the Committee's comparable analysis, or a blending of the two, it is clear that the total aggregate cost of the proposed KEIP is at the very upper range of the 75th percentile assuming target payouts, based on the Debtors' comparables, and far exceeds the 75th percentile, based on the Committee's comparables. *See* Feintuch Declaration at ¶ 29. When considering the payout of the KEIP Maximum Bonus under the proposed KEIP, which the Debtors are likely to hit given the low thresholds proposed, the total aggregate cost of the KEIP far exceeds all comparables. While the per-participant cost of the KEIP appears more modest, this metric is skewed because the 19 participant KEIP is oversized when viewed in the aggregate, and, in fact, by the Debtors' own analysis, ranks in the 90th percentile. *Id.* For the reasons cited, the facts and circumstances of

these Chapter 11 Cases simply do not warrant such an extraordinarily generous bonus compensation program.

88. There is No Satisfactory Evidence that the Debtors Investigated the Need for the KEIP. Although the Bonus Compensation Motion states that the Debtors worked with and relied on expensive expert guidance in designing the KEIP and in providing market diligence, the Bonus Compensation Motion simply makes conclusory statements regarding the necessity of the KEIP (particularly at the exorbitant levels proposed).

89. [redacted]

90. Such a process is not evidence of an investigation for the *need* for the KEIP the Debtors have proposed. Instead, it is evidence of the Debtors proposing a KEIP structure that they knew could be easily achieved. Perhaps the KEIP Bonuses are an ancillary benefit for insiders and senior management for going along with what is an already backwards restructuring and sale process being driven by the Secured Lenders for their sole benefit.

91. Based on the foregoing, the Debtors fail to make a sufficient showing that they performed a reasonable investigation for the need for the KEIP or that the KEIP is justified by the facts and circumstances of these Chapter 11 Cases or that it is an exercise of sound business judgment. The proposed KEIP merely provides the Debtors' executives with an opportunity to deplete the Debtors' assets at the expense of the Debtors' estates and creditors, and the KEIP must be denied.

II. THE DEBTORS HAVE NOT MET THEIR BURDEN TO DEMONSTRATE THAT THE BONUSES UNDER THE PROPOSED KERP ARE JUSTIFIED UNDER THE CIRCUMSTANCES OF THESE CASES OR ARE A SOUND EXERCISE OF THE DEBTORS' BUSINESS JUDGMENT

92. The Debtors fail to meet their burden of showing that (i) the KERP Participants are not insiders; and that (ii) to the extent some KERP Participants are truly non-insiders, the proposed bonuses (a) are justified by the facts and circumstances of these cases as required by section 503(c)(3) of the Bankruptcy Code and (b) constitute a sound exercise of the Debtors' business judgment under section 363(b)(1) of the Bankruptcy Code.

1. KERP Participants Appear To Be Insiders

93. The KERP should not be approved under section 503(c)(3) of the Bankruptcy Code absent evidence rebutting the presumption that KERP Participants holding officer titles participate in management. *In re Foothills Texas, Inc.*, 408 B.R. 573, 584-585 (Bankr. D. Del. 2009).

94. Here, although not detailed in the Motion, upon information and belief, many of the proposed KERP Participants have titles that include terms such as "Director," "Controller," and "Senior Manager." These proposed KERP Participants' titles appear to indicate that they are officers of the Debtors for purposes of 11 U.S.C. § 101(31), thereby subjecting the KERP to the stringent requirements of 11 U.S.C. § 503(c)(1). *See Office of the U.S. Trustee v. Fieldstone Mort. Co.*, 2008 WL 4826291 at *4 (D. Md. 2008) (finding that seven persons appointed by the board of directors to serve as officers under applicable state law "should have been sufficient to establish their officer status [under 11 U.S.C. §§ 101(31) and 503(c)) as a matter of legal interpretation . . ." and reversing an order approving a KERP).

95. In *In re Patriot Coal Corp. et al.,* Case No. 12-51502 (Bankr. E.D. Mo. 2013), the United Mine Workers Association (the "UMWA") and United States Trustee argued that several of the proposed participants in the "Patriot KERP" were insiders and thus did not qualify for participation in the Patriot KERP. Ultimately, certain employees originally included in the Patriot KERP that were approved, verified, or appointed by the board were appropriately excluded from the KERP:

> By agreement with the U.S. Trustee, the following individuals were removed from the [Patriot KERP]: the Senior Vice President of Operations, the Vice President of Safety, the Vice President and Associate General Counsel and Corporate Secretary, the Vice President of Operations, the Vice President and Treasurer, the Vice President of Investor Relations and the Assistant Secretary and Senior Counsel. As previously mentioned, the U.S. Trustee formed the belief that these individuals were insiders because they were appointed by Debtor Patriot Coal Corp.'s Board of Directors.
> . . . .
>
> The Court is satisfied that the appropriate individuals have been excluded from participation in the [Patriot KERP] in that the remaining participants are not insiders.

See *Order Authorizing Debtors to Implement Compensation Plans*, at pp. 10, 24, *In re Patriot Coal Corp. et al.*, Case No. 12-51502 (Bankr. E.D. Mo. May 16, 2013), ECF Docket No. 4001. Here, just as in *Patriot*, certain senior level employees that are proposed KERP Participants include the very types of employees removed from the Patriot KERP as they have significant authority over corporate policy, decisions, or corporate assets.

96. The Bonus Compensation Motion fails to demonstrate that each of the KERP Participants is not an "insider," to whom the strict requirements of section 503(c)(1) of the Bankruptcy Code apply. The Committee objects to retention bonuses under the KERP being paid to anyone who may be deemed to be an insider.

2. <u>KERP Bonuses Are Not Justified By The Facts And Circumstances And Are Not Reasonable</u>

97. The KERP should be denied absent evidence that payment of the proposed bonuses is truly necessary for retention of employees that are essential to a successful reorganization of the Debtors' businesses and the maximization of the value for the Debtors' estates and creditors. *See, e.g., In re Regensteiner Printing Co.*, 122 B.R. 323, 326 (N.D. Ill. 1990) ("Employees did not meet their burden of proving that their bonus payments were necessary to preserve the estate. . . . At a minimum, there should have been testimony to support findings as to whether the Employees would have rendered the necessary services without the bonuses.").

98. In particular, the Committee questions whether it is necessary for the Debtors to pay thirty-four individuals an average bonus of $26,346 per participant, for a total payout of nearly $900,000, in light of the other compensation programs proposed by the Debtors. While the Debtors argue that the proposed KERP is reasonable when compared to the carefully chosen comparable plans utilized by the Debtors' compensation consultant, viewed in conjunction with

the more than $4 million that will become payable under the KEIP, the multi-million dollar ICP, and the MSP, the total bonus compensation that the Debtors propose to pay is unreasonable.

99. Additionally, the Debtors are only one month away from the scheduled auction of the Downstream Business. Nevertheless, the Debtors propose to pay out all KERP bonuses without any reduction to the extent that the KERP Participants receive offers of continued employment from the purchaser of the Downstream Business (or other asset purchaser). At the very least, KERP benefits should be denied, or significantly reduced, for those employees who are offered continued employment by the purchaser of the Downstream Business (or other asset purchaser), as such employees will remain sufficiently incentivized by the opportunity to continue their employment with the successful purchaser. *See In re Allied Holdings*, 337 B.R. 716, 726 (Bankr. N.D. Ga. 2005) ("the purpose of the KERP is not to reward employees, but to retain the employees").

100. Finally, as set forth above, once the Downstream Business is sold, the Debtors will have insufficient capital or funding remaining to reorganize or run a sale process for the Upstream Business. To the extent that the Secured Lenders desire an orderly liquidation or even a going concern sale of the Upstream Business for their sole benefit, the costs thereof, including incentivizing employees to assist therein, should be borne by the Secured Lenders and not by the estates or their general unsecured creditors.

III. THE DEBTORS' PROPOSED ICP MUST NOT BE APPROVED AS IT IS NOT A SOUND EXERCISE OF THE DEBTORS' BUSINESS JUDGMENT OR, ALTERNATIVELY, MUST ONLY BE APPROVED IN MODIFIED FORM

101. Pursuant to the ICP, the Debtors seek authorization to pay an additional $1.4 million to all non-insider on-site salaried employees in the Downstream Business. The Debtors claim that maintaining and extending the ICP to the ICP Participants will reward them for 2015 performance of the Downstream Business and maintain morale and value of the Downstream

Business until its sale. The ICP is payable to ICP Participants (i) who are offered and accept employment with the purchaser of the Downstream Business, or (ii) who are terminated without cause in connection with the sale of the Downstream Business. The Debtors' reasons for the ICP are unpersuasive and do not demonstrate that it is a sound exercise of the Debtors' business judgment. In addition, the ICP appears to be a disguised KEIP or KERP for low level employees of the Debtors' Downstream Business.

102. First, the Debtors argue that it is essential that employees of the Downstream Business be incentivized not to leave at "this critical juncture." However, the Debtors' motion is devoid of any suggestion that employees are actually leaving or even that there is opportunity for them to find other employment. Moreover, the employees are no doubt aware that the Debtors are scheduled to sell the Downstream Business as a going concern within approximately four weeks. Surely the prospect of continued employment with any successful bidder is sufficient incentive for employees to remain in the Debtors' employ for the short term.

103. The Debtors' second argument - that the ICP is reasonable in light of the benefit to the Debtors' estates - fails for similar reasons. The Debtors have failed to establish that employees are leaving for other employment or that there is even opportunity for them to obtain alternate, comparable employment over the next four weeks. In the absence of a readily apparent risk that employees will actually leave the Debtors employ, there simply is no benefit to the estate that warrants denuding the estates of another $1.4 million.

104. The third justification offered by the Debtors for the ICP is that incentive based compensation for salaried employees of the Downstream Business was already approved by the Court and, therefore, the Court should approve the ICP for all employees of the Downstream Business to be "fair." This bootstrapping argument should be given no weight in measuring the

reasonableness of implementing the ICP Plan. The ICP for salaried employees was approved at the first day hearing when these cases were in a very different posture, and before the Committee was appointed. While it may have made sense for the Debtors to offer cash payments to incentivize employees to remain in their employ in the early uncertain stages of these cases, such incentives are no longer necessary given the short path to a going concern sale imposed in these cases and the prospect of future employment by any successful bidder.

105. Fourth, the Debtors assert that the ICP is within industry standards. However, they provide no evidence of benchmarks or comparables for the industry standard and, further, no data as to the reasonableness of the ICP in light of the KEIP, KERP, and MSP. In fact, based on the Houlihan Summary of Selected Historical KEIPs and KERPs, the proposed combined \$2.3 million payout through the KERP and ICP ranks in the 82nd percentile. *See* Feintuch Declaration at ¶ 30.

106. Finally, should the Court desire to approve the ICP, it should be approved only in a modified form. At the very least, ICP benefits should be denied, or significantly reduced, for those ICP Participants offered continued employment by the purchaser of the Downstream Business (or other asset purchaser), as such employees will remain sufficiently incentivized by the prospect of continued employment by the successful bidder after the sale of the Downstream business.

IV. THE MSP MOTION CANNOT BE GRANTED BECAUSE THE DEBTORS HAVE NOT PROVIDED SUFFICIENT INFORMATION FOR THE COURT TO DETERMINE IF CONTINUING THE MSP IS A SOUND EXERCISE OF THE DEBTORS' BUSINESS JUDGMENT

107. By way of the MSP Motion, the Debtors seek authority to implement the MSP to "maintain employee morale during these Chapter 11 Cases." *See* MSP Motion, ¶ 5. The MSP Motion, however, lacks sufficient information for the Court to evaluate the basis for the relief requested.

108. First, the Debtors fail to identify the senior employees to which the MSP applies (the "Eligible MSP Participants"). It is, therefore, impossible to determine whether or not the Eligible MSP Participants are insiders of the Debtors. Further, it is impossible to determine whether the Eligible MSP Participants are participants in any of the other Compensation Plan such as the KEIP, KERP, or ICP. If they are, the MSP is hardly necessary to maintain their morale.

109. Second, without identifying the Eligible MSP Participants and their salary information, it is impossible to determine the potential cost of the MSP. The Debtors do not provide an estimated or potential maximum cost to the Debtors' estates. The ISP Motion cannot be approved until there is full disclosure of such facts and data so that the reasonableness of all of the Compensation Plans can be considered in light of the others concurrently.

RESERVATION OF RIGHTS

110. The Committee reserves the right to supplement this Omnibus Objection prior to or at the hearing to consider approval of the Compensation Motions. The Committee further reserves the right to present evidence (including further charts and/or exhibits related to comparable KERP or KEIP plans, incentive compensation plans, or severance plans) and/or rely on evidence to be presented by others with respect to the Compensation Motions.

CONCLUSION

For the foregoing reasons, the Committee objects to approval of the Compensation Plans. Alternatively, the Committee requests that he Court approve the Compensation Plans only if the plans are paid for by the Secured Lenders as a carveout from their collateral as the plans benefit only the interests of the Secured Lenders.

[*Remainder of page intentionally left blank*]

For the foregoing reasons, the Committee respectfully requests that the Bonus Compensation Motion and MSP Motion be denied and/or modified as set forth above.

Dated: May 5, 2016

Respectfully Submitted,

LOWENSTEIN SANDLER LLP

Kenneth A. Rosen, Esq.
Jeffrey D. Prol, Esq.
65 Livingston Avenue
Roseland, NJ 07068
Telephone: (973-597-2500
-and -
Bruce S. Nathan, Esq.
David M. Banker, Esq.
1251 Avenue of the Americas
New York, NY 10020
Telephone: (212) 262-6700

Proposed Counsel to the Committee

-and-

SPENCER FANE LLP

/s/ Lisa A. Epps
Lisa A. Epps, Esq., 48554MO
1000 Walnut Street
Suite 1400
Kansas City, MO 64106
Telephone: (816) 474-8100
Facsimile: (816) 474-3216
lepps@spencerfane.com
- and-
Sherry K. Dreisewerd, Esq., 47908MO
Eric C. Peterson, Esq., 62429MO
Ryan C. Hardy, Esq., 62926MO
1 N. Brentwood Boulevard
Suite 1000
St. Louis, MO 63105
Telephone: (314) 863-7733
Facsimile: (314) 862-4656
sdreisewerd@spencerfane.com
epeterson@spencerfane.com
rhardy@spencerfane.com

Proposed Local Counsel to the Committee

CERTIFICATE OF SERVICE

I certify that on this 5th day of May, 2016, the foregoing was served as set forth on Exhibit A, attached hereto.

/s/ Lisa A. Epps

UNITED STATES BANKRUPTCY COURT
EASTERN DISTRICT OF MISSOURI
SOUTHEASTERN DIVISION

In re: NORANDA ALUMINUM, INC., *et al.*, Debtors.	Chapter 11 Case No. 16-10083-399 (Jointly Administered) Re: D.I. 671, 674

DECLARATION OF JASON FEINTUCH IN SUPPORT OF THE OFFICIAL COMMITTEE OF UNSECURED CREDITORS' OMNIBUS OBJECTION TO

DEBTORS' MOTION FOR AN ORDER PURSUANT TO SECTIONS 105(A), 363 AND 503(C)(3) OF THE BANKRUPTCY CODE AND BANKRUPTCY RULE 6004 (A) AUTHORIZING AND APPROVING THE DEBTORS' (I) KEY EMPLOYEE INCENTIVE PLAN; (II) KEY EMPLOYEE RETENTION PLAN; AND (III) 2015 INCENTIVE COMPENSATION PLAN AND (B) GRANTING RELATED RELIEF

AND

DEBTORS' MOTION FOR AN ORDER PURSUANT TO SECTIONS 105(A) AND 363 OF THE BANKRUPTCY CODE AND BANKRUPTCY RULE 6004 AUTHORIZING AND APPROVING THE DEBTORS' MODIFIED SENIOR MANAGEMENT SEVERANCE PROGRAM FOR NON-INSIDER EMPLOYEES

Jason Feintuch, pursuant to 28 U.S.C. § 1746, hereby declares as follows:

1. I am a Director at Houlihan Lokey, Inc. ("Houlihan"), the financial advisor to the official committee of unsecured creditors (the "Committee") appointed in the chapter 11 bankruptcy cases (the "Chapter 11 Cases") of the above-captioned debtors and debtors-in-possession (the "Debtors").

2. I submit this declaration (the "Declaration") in support of *The Official Committee of Unsecured Creditors' Omnibus Objection [(the "Omnibus Objection")] to Debtors' Motion for an Order Pursuant to Sections 105(a), 363 and 503(c)(3) of the bankruptcy Code and Bankruptcy Rule 6003 (A) Authorizing and Approving the Debtors' (I) Key Employee Incentive Plan; (II) Key Employee Retention Plan; and (III) 2015 Incentive Compensation Plan and (B)*

Granting Related Relief AND Debtors' Motion for an Order Pursuant to Sections 105(A) and 363 of the Bankruptcy Code and Bankruptcy Rule 6004 Authorizing and Approving the Debtors' Modified Senior Management Severance Program for Non-Insider Employees [Docket Nos. 671,674] (the "Bonus Compensation Motion" and the "MSP Motion," respectively, and collectively the "Compensation Motions").[1]

3. Except as otherwise indicated, all facts set forth in this Declaration are based upon: (a) my personal knowledge; (b) my review, or the review of employees of Houlihan under my supervision and direction, of the relevant documents related to the Compensation Motions and the Omnibus Objection; and (c) information supplied to me or other employees of Houlihan under my supervision and direction, by the Debtors and their professionals.

4. If called upon to testify, I could and would competently testify to the facts set forth herein.

A. Qualifications and Background

5. I received a bachelor's degree in economics from the Wharton School at the University of Pennsylvania. My business address is 245 Park Avenue, 32nd Floor, New York, NY 10167. I joined Houlihan in July of 2005 and I have extensive experience with chapter 11 cases and other distressed restructurings, having advised debtors, creditors' committees and other constituencies for approximately 10 years. I have extensive experience reviewing and negotiating debtor compensation programs.

[1] Capitalized terms used but not otherwise defined herein shall have the meaning ascribed to such terms in the Omnibus Objection.

6. Since Houlihan was retained as financial advisors to the Committee on February 23, 2106, I have reviewed the DIP Motion, the Final DIP Order, the DIP Financing Documents, and the Compensation Motions. Pursuant to the Compensation Motions which the Debtors seek to implement a key employee incentive plan (the "KEIP"), a key employee retention plan (the "KERP), an incentive compensation program (the "ICP"), and a modified severance program (the "MSP" and, collectively with the KEIP, KERP and ICP, the "Compensation Plans"). I have also reviewed certain financial information provided to the Committee's advisors by the Debtors on a confidential basis, including, but not limited to, the Debtors' Overview of Proposed Employee Programs-Incentive and Retention Plans (the "Bonus Compensation Plans Overview")[2], the Debtors' Business Plan Review dated April 8, 2016 (the "Upstream Business Plan")[3], and the Debtors' "DIP Sizing Model" dated February 4, 2016[4].

B. The Debtors' Businesses and Sale Process

The Upstream Business

7. At this time, the Debtors' Upstream Business, consisting of three vertically integrated separate segments: (i) the St. Ann Segment consisting of the Debtors' bauxite mining operations in St. Ann, Jamaica; (ii) the Gramercy Segment consisting of the Debtors' alumina refinery in Gramercy, Louisiana; and (iii) the New Madrid Segment consisting of the primary aluminum reduction plant and fabrication facilities located in New Madrid, Missouri, is not profitable and operates at a substantial loss.

8. Pre-Petition, the Debtors sold nearly half of the bauxite mined from the St. Ann Facility to Sherwin under an unprofitable contract (the "Sherwin Contract") with Sherwin Aluminum Co. ("Sherwin") which was rejected by the Debtors by Order of this Court entered on

[2] Annexed hereto as Exhibit A.
[3] Annexed hereto as Exhibit B.
[4] Annexed hereto as Exhibit C.

April 7, 2016 [Docket No. 609]. [redacted] For the fiscal year ended 2015, the St. Ann Facility recorded an operating loss of approximately $10.4 million. *See* Noranda Aluminum Holding Corporation Form 10-K for Fiscal Year Ended December 31, 2015 (the "2015 Annual Report")[6] at p. 28.

9. [redacted]

10. For the fiscal year ended 2015, the Gramercy segment showed a profit of $12.5 million. *See* 2015 Annual Report at pg. 28. Nonetheless, future profitability of Gramercy is hampered by labor issues and the fact that its largest customer, Century Aluminum, an affiliate

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[5] Annexed hereto as Exhibit D.
[6] Annexed hereto as Exhibit E.

of Sherwin's parent, has moved to terminate its contract to buy product from Gramercy. Docket No. 283.

11. Prepetition, commodity-grade aluminum produced in the New Madrid Facility was sold to the Debtors' Downstream Business or to other aluminum fabricators. According to the Boyles Declaration, "[t]he challenges confronting the Debtors were exacerbated when, on August 4, 2015, a molten metal explosion occurred in the casthouse of the New Madrid Facility, where molten aluminum is converted into commodity and value added products". "Additionally, on January 7, 2016, the Debtors lost power to two of the three pot-lines for smelting primary aluminum at the New Madrid Facility when an electrical circuit failed." *See* Boyles Dec. at ¶ 33. As a result of these events, the Debtors have shut down operations at the New Madrid Facility. In fact, the DIP Lenders (defined herein) insisted that the failure to close this facility by not later than March 24, 2016 would be an event of default under the DIP Financing Agreement. *See* Final DIP Order, ¶ 18. [redacted]

12. In sum, at the present time, the Upstream Business is cash flow negative and unprofitable and will likely continue to burn cash until the complex issues related to the Government of Jamaica levy, sales of bauxite to Sherwin or another customer (or reduction in production levels), [redacted] and labor issues are resolved.

<u>The Downstream Business</u>

13. The Debtors' own financial projections show that the Downstream Business will be significantly cash flow positive from operations for the foreseeable future. [redacted]

[redacted]

The Debtors' Downstream Sale Process

14. On March 9, 2016, PJT Partners ("PJT"), the Debtors' investment banker, launched the marketing process for the sale of the Downstream Business. [redacted]

15. Based upon my review of the Debtors' financial projections and other information received from the Debtors, I do not believe that the Downstream Business is a "melting ice cube" that must be sold quickly in order to maximize value. To the contrary, the Debtors' own projections show that the Downstream Business will continue to be profitable for the foreseeable future. [redacted]

[7] Annexed hereto as Exhibit F.

[redacted]

16. [redacted] In contrast, according to the Debtors' public filings, the Upstream Business is not currently viable because it currently has a large negative cash flow and, as a whole, has incurred a net operating loss of $25.8 million for year ending 2015, excluding any allocation between Upstream and Downstream of the $30.4 million of corporate expenses. *See* 2015 Annual Report at pp. 37, 71. Further, based on the Committee's review of the Debtors' financial projections and reports, the Debtors need the positive cash flow from the Downstream Business to afford them sufficient time to maximize the value of the Upstream Business. This time is required for the Debtors to, among other things, resolve the issues related to Sherwin, Century, the Jamaican levy and other matters that could positively affect the value of that business.

D. The Debtors' Compensation Motions

17. The Downstream Sale Metric is the most problematic. [redacted]

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[8] While Gramercy on its own reports a profit, it is best to consider the Upstream Business segments as a whole given the interrelatedness of operations.

[redacted]

18. The Cash Flow Funding Metrics are similarly troublesome in that they do not constitute a "reach" and are easily attainable.[9]

19. The Cash Flow Funding Metrics for the first quarter for each business was evaluated against the DIP budget, which by its very nature is a conservative projection that must be complied with in order to avoid a default under the DIP Loan. That these benchmarks are not a "reach" is clearly evidenced by the fact that per the Debtors' plan, each of the businesses achieved the maximum payout threshold for the first quarter and now benefit from a cushion which will carry forward.

20. For the period beginning April 1 through emergence from bankruptcy, cash flow will be measured against the Upstream Business Plan, without regard to first quarter performance. The Upstream Business Plan is also not a reach given that it is based on conservative assumptions and was designed to be acceptable to the DIP Lenders as required by the Final DIP Order.

21. In addition, the Upstream Business Plan is based on numerous assumptions that could prove to be over or understated. A change in circumstances could lead to KEIP participants meeting or even exceeding KEIP targets without actually overachieving or even

[9] The Committee has requested from the Debtors the March financial performance metrics in a format which would comport to the format used in the Upstream Business Plan. To date, the Debtors have not provided a meaningful response.

achieving the Upstream Business Plan. For example, at St. Ann, a reduction in the levy imposed by the Government of Jamaica could significantly reduce the cost of production and hide a lot of other missteps with respect to cash flow outcomes. [redacted]

22. At Gramercy, cash flow metrics could be exceeded simply as a result of an expected material increase in pricing for commercial grade alumina without any regard to actual performance by management. Similarly, the cash flow metric for the Downstream Business could be exceeded due to an anticipated increase in the pricing of LME, and cash flow forecasts at New Madrid could be exceeded simply by obtaining a favorable reduction in real estate taxes or power costs.

23. Similarly, based on my review of the Performance Metrics proposed by the Debtors, the Performance Metrics also incentivize the KEIP Participants to work toward results which may in fact harm the Debtors' estates, rather than benefit them. These inherently inappropriate Performance Metrics include the following:

- *GOJ Resolution Metric* the Debtors provide no detail, limitations or parameters on the form or substance of a resolution with the GOJ to satisfy this Performance Metric. While resolution with the GOJ is important for the viability of the Upstream Business, it is not without limits and those limits must be well defined and disclosed in order to properly incentivize KEIP Participants, rather than to merely incentivize them to get to a deal quickly.

- *Union Negotiations Metric* – the Debtors provide no detail, limitations or parameters on the form or substance of a resolution with the Union to satisfy this Performance Metric. While resolution with the Union is important for the viability of the Downstream Business, it is not without limits and those limits must be well defined and disclosed in order to properly incentivize KEIP Participants, rather than to incentivize them to merely get to a deal quickly.

- *New Madrid Asset Sale Metric* – the Debtors fail to provide any minimum threshold pricing targets or timing for the sale of the New Madrid assets. Rather, this metric only requires a sale "within 90 days of filing sale process motion." To properly incentivize the eligible KEIP Participant(s), the Debtors must define minimum values and outside date to truly maximize value for the estates.

- *New Madrid Insurance Metric* - the Debtors fail to provide any minimum threshold or timing for the resolution of the insurance claims on account of the damage to the New Madrid facility. To properly incentivize the eligible KEIP Participant(s), the Debtors must define minimum values and outside dates to truly maximize value for the estates.

- *Target Benefits Metric* – this metric may actually serve to encourage actions not in line with the best interests of the Debtors' estates and creditors. Because the Target Benefits Metric is based on beating the DIP Budget by not using cash – even for appropriate uses such as medical benefits to employees, the KEIP Participants may cause the Debtors to shy away from paying medical benefits to employees to reduce the cash variance for fear of a reduction in their personal compensation under the KEIP. This is likely to cause attrition and instability among the Debtors employees and is the exact opposite of how an incentive plan should be structured.

- *Sales Pipeline Metrics* – Certain sales pipeline metrics are flawed in that they attempt to incentivize employees based on sales targets and not profitability. This potentially incentivizes employees to sell product at low prices, damage the Debtors' profitability, and be rewarded for doing so.

24. Additional, various Performance Metrics are not truly incentivizing because they do not require any real reach or challenging performance. Specifically, these Performance Metrics include the following:

- *EH&S Target Metric* – the Debtors have not provided any detail on this metric so it is impossible to determine whether this metric constitutes a sufficient reach.

- *Critical Vendor Metric* – [redacted]

[10] Annexed hereto as Exhibit G.

- *Business Expense Reduction Metric* – This metric requires a $1 million expense reduction at both St. Ann and Gramercy. The proposed metric represents a cost savings of 1.3% of total costs at St. Ann and .4% of total costs at Gramercy and is no reach at all. The cost reduction is also fixed and doesn't vary over time or with production levels. Thus, the metric could be met simply by St. Ann or Gramercy experiencing a production issue that shuts the plants down. Although this would be a negative for the Debtors' estates, the expense reduction could be met due to lack of production.

- *Target Fabrication Revenue Metric* – [redacted]

25. These low performance thresholds virtually guarantee the KEIP Participants big bonuses, including for achieving results without any clear connection to achievements by those KEIP Participants.

26. Based on Houlihan's review of relevant comparables, the Debtors' evidence fails to establish that the proposed KEIP is within the range of reasonableness by comparable programs approved by other courts. The Debtors assert that they compared the proposed KEIP to KEIPs in bankruptcy cases filed by a peer group of 19 companies (the "<u>Bankruptcy Peers</u>"), and that the aggregate "target payout" under the proposed KEIP falls within the 67th percentile and the per-participant average target payout falls within the 42nd percentile of the payouts in the cases of the Bankruptcy Peers. The Debtors fail to specify whether the KEIPs in the cases of the Bankruptcy Peers were actually approved and whether the proposed payouts were actually made. In addition, the Debtors note that the Bankruptcy Peers were chosen based on the fact that the companies intended to continue operations.

27. In analyzing the proposed KEIP, Houlihan identified a more applicable set of comparable transactions which were more recent (all in connection with bankruptcies filed after

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[11] Annexed hereto as <u>Exhibit H</u>.

January 1, 2014) and better reflected the size and circumstances of the KEIP in these Chapter 11 Cases including those in which the debtors sold substantial portions of the debtors' business and operations pursuant to a section 363 sale. *See* Houlihan Summary of Selected Historical KEIPs and KERPs.[12] Based on Houlihan Lokey's analysis, both the aggregate target payout and the maximum payout under the proposed KEIP exceed all comparables identified by Houlihan Lokey.

28. Based on the Committee's analysis of comparable KEIPs, the Court should measure the KEIP costs as follows:

Total Aggregate KEIP Cost	Debtors' Comparables	Committee Comparables	Noranda KEIP Target	Noranda KEIP Maximum
25^{th} Percentile	$598,369	$790,000	$2,067,758	$4,135,517
75^{th} Percentile	$2,149,869	$1,423,235		

Per Participant KEIP Cost	Debtors' Comparables	Committee Comparables	Noranda KEIP Target	Noranda KEIP Maximum
25^{th} Percentile	$57,190	$132,829	$108,829	$217,659
75^{th} Percentile	$222,500	$210,625		

29. Whether the Court adopts the Debtors' comparable analysis, the Committee's comparable analysis, or a blending of the two, it is clear that the total aggregate cost of the proposed KEIP is at the very upper range of the 75^{th} percentile assuming target payouts, based on the Debtors' comparables, and far exceeds the 75^{th} percentile, based on the Committee's comparables. While the per-participant cost of the KEIP appears more modest, this metric is skewed because the 19 participant KEIP is oversized when viewed in the aggregate, and, in fact, by the Debtors' own analysis, ranks in the 90^{th} percentile.

[12] Annexed hereto as Exhibit I.

30. Upon review of the ICP, it is clearly intended to be an expansion of the KERP. While the KERP alone may be within industry standards, it is not in light of the $1.4 million ICP. The Debtors' propose a combined $2.3 million payout through the KERP and ICP, which ranks in the 82nd percentile of comparables in the Houlihan Summary of Selected Historical KEIPs and KERPs. Further, even if the KERP and ICP are considered individual compensation plans, the Debtors have not provided any comparable KERPs that were approved in conjunction with an additional compensation program such as the ICP.

31. For the reasons cited, the facts and circumstances of these Chapter 11 Cases simply do not warrant such an extraordinarily generous bonus compensation program.

I declare under penalty of perjury that the foregoing is true and correct to the best of my knowledge, information and belief.

Dated: May 5, 2016

/s/ *Jason Feintuch*
Jason Feintuch