

Kevin W. Barrett
Special Assistant Attorney General
for the State of West Virginia
Michael B. Hissam (VSB #76843)
BAILEY & GLASSER LLP
209 Capitol Street
Charleston, West Virginia 25301
Tel: (304) 345-6555
Fax: (304) 342-1110

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE EASTERN DISTRICT OF VIRGINIA
RICHMOND DIVISION**

<hr/>)	
In re))	Chapter 11
))	
ALPHA NATURAL RESOURCES, INC., <i>et al.</i> ,))	Case No. 15-33896 (KRH)
))	
Debtors.))	Jointly Administered
<hr/>)	

RESPONSE OF THE WEST VIRGINIA DEPARTMENT OF ENVIRONMENTAL PROTECTION TO THE REORGANIZED DEBTORS' MOTION TO APPROVE SETTLEMENTS WITH CONTURA ENERGY, INC. AND THE FIRST-LIEN LENDERS¹

Just three months into their reorganization, the reorganized debtors disclose for the first time that the five-year business plan projections promulgated in connection with their chapter 11 plan overstated the debtors' cash flows by a whopping \$100 million.² That is material in almost any circumstance. But it is devastating in this case, where the debtors' projected operating cash flow, even before anticipated capital expenditures, amounted to only \$146 million over the entire four and one-half year projection period.³

¹ By agreement, the reorganized debtors extended DEP's time to file a response to the motion to November 15, 2016 at noon.

² Doc 3525 at ¶ 8 ("The Reorganized Debtors estimate that the total amount of these unaccounted-for obligations could approach \$100 million.").

³ See Doc 2528 at p. 194.

Those projections, moreover, formed the very basis for the negotiations and confirmation of the debtors' chapter 11 plan.⁴ And they were of particular importance to DEP in that regard, as the reorganized debtors' ability to continue in existence and perform their extensive ongoing legal obligations to bond and reclaim both their active and shuttered mine sites in West Virginia was critical to DEP's willingness to enter into its settlement with the debtors.⁵ Indeed, DEP believes the reorganized debtors' ability to meet those original projections remains critical to the effectiveness of the DEP settlement, which stretches out the debtors' bonding and reclamation obligations in West Virginia for ten years or more.

As the reorganized debtors put it in their motion, "the Projections demonstrated the viability of Contura and the Reorganized Debtors."⁶ Although they decline to say as much, there is no doubt that the newly disclosed \$100 million shortfall seriously threatens the reorganized debtors' viability and ability to perform their legal obligations to bond and reclaim their remaining mine sites, just three months after they consummated the DEP and other regulatory settlements and plan.⁷

What's more, the \$100 million shortfall does not result from a failure to achieve the projections. In fact, the reorganized debtors say that, excluding the amounts paid with respect to newly disclosed expenses, they have generally met, and expect to continue to meet or exceed, their previous cash projections.⁸ Instead, the projections were simply wrong from the beginning.

⁴ See, e.g., Confirmation Order [Doc 3038] at ¶ S.

⁵ See Doc 3040 at 114 (making it an express condition to the DEP settlement that there be no material adverse changes to the reorganized debtors' business plan and projections).

⁶ Doc 3525 at ¶ 11.

⁷ The reorganized debtors vaguely hint at the issue when they state their belief that the two proposed settlements will allow them to continue business operations and fulfill their obligations under the various settlements with DEP and the other State and federal regulatory agencies. Doc 3525 at ¶ 37.

⁸ Doc 3525 at ¶ 7.

But they were not wrong because they failed to reflect reasonably unanticipated or unexpected expenses. The overwhelming majority of the so-called “unaccounted-for” obligations—some \$75 million—were the most routine of ordinary course expenditures for a coal mining company—royalties, payroll, taxes, and accounts payable that had already been incurred.⁹ The rest resulted from the express terms and provisions of the Contura asset purchase agreement, including a working capital adjustment, for the calculation of which, it would seem, the debtors had available all the necessary information at their disposal.¹⁰

Nor did these “unaccounted-for” obligations arise at some distant point in the future. They had already arisen, and indeed manifested themselves almost immediately after the closing. And, now, just three months later, the reorganized debtors have already expended at least \$36.7 million of the \$100 million in the “unaccounted-for” obligations to date.¹¹

In the end, every one of the nearly \$100 million in “unaccounted-for” expenditures identified to date appears to have been immediate and pending, known or certainly knowable, and entirely predictable.

Under all the circumstances, it is hard to imagine that a shortfall of this nature and order of magnitude was just a mistake. But, here, even more damning, the debtors’ senior management sat on both sides on these very issues and stood to benefit uniquely from consummation of the plan and the DEP settlement. During the pendency of the chapter 11 cases, the debtors’ senior management jockeyed for positions at Contura and then assumed those

⁹ Doc 3525 at ¶ 20-23 & Exh E.

¹⁰ Doc 3525 at ¶ 19. In fact, the Hopkins declaration attached to the motion states that “prior to the Closing, the Debtors expected a moderate working capital adjustment might be payable by Contura *to the Reorganized Debtors.*” Doc 3525 at p. 76, ¶ 11 (emphasis added).

¹¹ Doc 3525 at ¶ 23.

positions immediately upon consummation of the plan.¹² But as the debtors' senior management and the individuals ultimately responsible for producing the projections,¹³ they knew (or certainly had every reason to know) precisely what taxes, payroll, royalties and payables the debtors had already incurred and would become due, especially just weeks in the future. They also knew (or certainly had every reason to know) precisely what the Contura agreement required and would obligate the reorganized debtors to pay.¹⁴ The conclusion thus seems almost inescapable that the debtors' senior management knew about but did not disclose those impending "unaccounted-for" expenditures to ensure consummation of the debtors' Contura sale and chapter 11 plan for their own benefit and to secure the releases of environmental liability from DEP (and other regulatory agencies) they so desired.

The reorganized debtors' proposed settlements reduce, but do not eliminate, the "unaccounted-for" obligations and the shortfall. The projections appear to remain at least \$50 million short,¹⁵ a number that still vastly increases the reorganized debtors' risk of failure and exposes them even more than they otherwise already were to the vagaries and uncertainty of an unprecedented coal market. Putting their best face on the matter, the reorganized debtors express the hope that the market's recent improvement and newly implemented and anticipated cost

¹² See <http://conturaenergy.com/about/leadership/>. The profile of each member of "leadership" on Contura's website shows that each assumed his position at Contura in July 2016 after having served at Alpha Natural Resources in similar positions until that time.

¹³ See, e.g., Doc 3525 at *6 n. 2 (quoting from the debtors' disclosure statement to the effect that management considered the estimates and assumptions in the financial projections as "reasonable").

¹⁴ As noted insofar as concerns the working capital adjustment, the Hopkins declaration says, prior to the closing, the debtors actually expected payment from Contura. See *supra* n. 10. Incredibly, just twenty-seven days later, Contura, under the very same management as the debtors had operated prior to the closing, delivered a notice calculating the adjustment at \$18.8 million *owing by the Reorganized Debtors*. Doc 3525 at p. 76, ¶ 11.

¹⁵ See Doc 3525 at ¶ 36 (identifying \$27.6 million in waivers relating to unaccounted-for obligations and the provision of \$25 million in Distribution Cash; upon information and belief, the \$14 million tax credit was already included in the debtors' cash flow projections).

savings will put them back close to where they thought they would be by the end of 2017.¹⁶ DEP shares that hope, but notes that the risks are most acute between now and then, as the projections already showed the reorganized debtors with *negative* operating cash flow (again before anticipated capital expenditures) totaling more than \$48 million through the end of 2017.¹⁷ DEP also notes that, but for the ongoing unaccounted-for obligations, any cash flow improvements over the projections not only would have provided obviously needed cushion for the reorganized debtors' long-term survival but it might also have provided additional funding for reclamation through the payment of excess cash flow into the collateralized reclamation accounts that are at the heart of the DEP and other regulatory settlements.¹⁸

Despite the ongoing impact of the remaining unaccounted-for obligations on the reorganized debtors and the resulting risks to fulfillment of the DEP settlement even after the subject settlements, DEP chooses not to challenge the settlements. The reorganized debtors have negotiated settlements of their own possible claims with Contura and the first-lien lenders. That is their prerogative.

DEP, however, has its own independent set of legal rights and remedies. The proposed settlements do not— and cannot— affect those rights and remedies.

DEP expressly reserves its rights with respect to its own legal rights and remedies, including the right to seek to invalidate any prior releases.

¹⁶ See Doc 3525 at ¶¶ 18 & 37.

¹⁷ See Doc 2528 at p. 194.

¹⁸ See Doc 3040 at p. 34.

Dated: November 15, 2016

/s/ Kevin W. Barrett

Kevin W. Barrett
Special Assistant Attorney General
for the State of West Virginia
Michael B. Hissam (VSB #76843)
BAILEY & GLASSER LLP
209 Capitol Street
Charleston, West Virginia 25301
Tel: (304) 345-6555
Fax: (304) 342-1110
kbarrett@baileyglasser.com
mhissam@baileyglasser.com

Attorneys for the West Virginia Department
of Environmental Protection

CERTIFICATE OF SERVICE

I hereby certify that on November 15, 2016, I caused “**RESPONSE OF THE WEST VIRGINIA DEPARTMENT OF ENVIRONMENTAL PROTECTION TO THE REORGANIZED DEBTORS’ MOTION TO APPROVE SETTLEMENTS WITH CONTURA ENERGY, INC. AND THE FIRST-LIEN LENDERS**” to be filed with and uploaded to this Court’s CM/ECF system, which will send notification of such filing to all CM/ECF participants.

/s/Kevin W. Barrett _____