

PILLSBURY WINTHROP SHAW PITTMAN LLP
 1540 Broadway
 New York, New York 10036-4039
 (212) 858-1000 (Phone)
 (212) 858-1500 (Fax)
 Craig A. Barbarosh (CB 6977)
 Karen B. Dine (KD 0546)
 David A. Crichlow (DC 2116)
 Counsel for the Official Committee
 of Equity Holders of Solutia Inc., *et al.*

Hearing Date: March 14, 2006 at 11:00 a.m

UNITED STATES BANKRUPTCY COURT
 SOUTHERN DISTRICT OF NEW YORK

_____X		
In re:	:	Chapter 11
	:	
SOLUTIA INC., <i>et al.</i> ,	:	Case Nos. 03-17949 (PCB)
	:	
	:	(Jointly Administered)
Debtors.	:	
	:	
_____X		

THIS STATUS REPORT RELATES TO:

- | | |
|--|---|
| <input checked="" type="checkbox"/> All Debtors | <input type="checkbox"/> Axio Research Corporation |
| <input type="checkbox"/> Solutia Business Enterprises Inc. | <input type="checkbox"/> Solutia Investments, LLC |
| <input type="checkbox"/> Solutia Inc. | <input type="checkbox"/> Beamer Road Management Company |
| <input type="checkbox"/> Solutia Systems, Inc. | <input type="checkbox"/> Monchem, Inc. |
| <input type="checkbox"/> Solutia Overseas, Inc. | <input type="checkbox"/> Solutia Inter-America, Inc. |
| <input type="checkbox"/> CPFilms Inc. | <input type="checkbox"/> Solutia International Holding Inc. |
| <input type="checkbox"/> Solutia Management Company, Inc. | <input type="checkbox"/> Solutia Taiwan, Inc. |
| <input type="checkbox"/> Monchem International, Inc. | <input type="checkbox"/> Solutia Greater China, Inc. |

**STATUS REPORT OF THE OFFICIAL
 COMMITTEE OF EQUITY SECURITY HOLDERS**

The duly-appointed official committee of equity security holders (the “Equity Committee”) of the above-captioned debtors and debtors-in-possession (collectively, the “Debtors”), respectfully submits this status report to apprise the Court of the background, substance and significant impact on these cases of the outcome of an adversary proceeding brought by the Equity Committee (the “Equity Committee Adversary Proceeding”) against

Pharmacia Corporation (“Old Monsanto”) and Monsanto Company (“New Monsanto”). The issues raised in the Equity Committee Adversary Proceeding focus on what has become a core issue in the Debtors’ Plan of Reorganization (the “Plan”) -- the appropriate allocation among Old Monsanto, New Monsanto and Solutia of environmental, tort and retiree liabilities relating to the historical business of Old Monsanto (“Old Monsanto Legacy Liabilities” or “Legacy Liabilities”). Solutia’s alleged responsibility for these Legacy Liabilities derives from indemnity obligations that Old Monsanto imposed on Solutia at the time it was created (the “Spin-off”). These indemnity obligations cover environmental cleanup liabilities, toxic tort claims and natural resource damages associated with various discontinued businesses that Old Monsanto operated and discontinued prior to the Spin-off.

1. At the time of the Spin-off, Old Monsanto’s vision of the future was built around the growth of its life science businesses. However, the economic risks posed by these Legacy Liabilities were a serious threat to Old Monsanto’s ability to obtain the future financing necessary to expand those operations. As a result, a key objective of the Spin-off was to move these Legacy Liabilities off of Old Monsanto’s balance sheet so that they would not stifle the future growth of life sciences. Solutia provided a solution for Old Monsanto.

2. Old Monsanto’s overriding goal in the Spin-off was to maximize the amount of the Legacy Liabilities that it could remove from its balance sheet. Old Monsanto disregarded whether Solutia was properly capitalized to satisfy these Legacy Liabilities. The Equity Committee submits that Old Monsanto knowingly spun-off Solutia with insufficient capital in light of the magnitude of the Legacy Liabilities being transferred.

3. In fact, Old Monsanto knew far more about the magnitude of the Legacy Liabilities than it disclosed in connection with the Spin-off. To gain the market confidence

required to effectuate the Spin-off, Old Monsanto affirmatively misrepresented the economic risks associated with the Legacy Liabilities. These affirmative misrepresentations indicate that Old Monsanto knew, but was determined to conceal, that it was creating a company destined to fail over the long-term.

4. In this regard, the Equity Committee has conducted an investigation into Old Monsanto's knowledge of the magnitude of the Legacy Liabilities at the time of the Spin-off and Old Monsanto's affirmative misrepresentations relating to its Legacy Liabilities. Based on the work completed to date, the Equity Committee submitted to the Court on or about January 31, 2006, its ***PRELIMINARY LEGACY ENVIRONMENTAL LIABILITIES REPORT***, which sets forth the preliminary findings and supporting evidence related to this investigation ("Legacy Liabilities Report"). The Equity Committee respectfully requests that the Court read its Legacy Liabilities Report because it provides the factual context for the Equity Committee Adversary Proceeding. The Legacy Liabilities Report also demonstrates that Solutia was undercapitalized at the time of the Spin-off, explains why it took seven years following the Spin-off before it filed for bankruptcy protection, and explains why Solutia's failure was unavoidable in light of Solutia's initial undercapitalization.

5. Since the Spin-off, Solutia has paid substantially more to address its Legacy Liability indemnity obligations than what Old Monsanto represented to be the high side risk to Solutia's shareholders at the time of the Spin-off. In light of Old Monsanto's conduct in connection with the Spin-off, the Equity Committee contends that Old Monsanto and New Monsanto should not be allowed to extract any more from Solutia and its shareholders under the Legacy Liability indemnity than the economic risk portrayed in the rosy (but false) picture that Old Monsanto painted for investors in 1997.

6. The Equity Committee submits that this overview is critical for this Court's evaluation and analysis of the Debtors' Plan and the accompanying Disclosure Statement (the "Disclosure Statement"), because the Plan purports to settle the Equity Committee Adversary Proceeding for a tiny fraction of its real value.¹ The Equity Committee respectfully represents as follows:

The Equity Committee Adversary Proceeding

7. The Equity Committee engaged in an investigation (pursuant to Federal Rule of Bankruptcy Procedure 2004) and analysis regarding the circumstances and structure of the Spin-off of Solutia by Old Monsanto. The Equity Committee's investigation included extensive legal analysis and the review of documents produced by the Debtors, Old Monsanto, New Monsanto, and Goldman Sachs in response to the Equity Committee's 2004 Motions.

8. In addition, in light of the significant impact of the environmental liabilities that were assigned to Solutia as part of the Spin-off, the Equity Committee retained an independent environmental consultant, which was approved over the strenuous objection of the Creditors' Committee, to assist the Equity Committee in its analysis of the current and historic environmental liabilities of the Debtors.

9. As a result of its analysis and investigation, the Equity Committee discovered that after depriving its chemicals business of necessary cash for capital expenditures for several years

¹ The Equity Committee reserves its rights to object to any and all aspects of the Disclosure Statement and/or Plan. While the Equity Committee believes it important to address as quickly as possible the issues relating to the Equity Committee Adversary Proceeding so that discovery can proceed, the issues relating to the Global Settlement described herein are by no means the Equity Committee's only objections to the Disclosure Statement and Plan. For example, the Equity Committee submits that the projections and estimates of value presented by the Debtors are based on assumptions designed to significantly undervalue the Debtors' businesses and give the false appearance that there is no equity value in the enterprise for Solutia's existing public shareholders.

prior to the Spin-off, Old Monsanto determined that the most effective method to further insulate its burgeoning life sciences business from significant environmental and other Legacy Liabilities was to create a new corporate entity (i.e., Solutia) in which Old Monsanto could transfer substantial debt obligations and enormous Legacy Liabilities (including liability for pollution and remediation at sites that were closed and that Solutia would never use, as well as retiree liabilities for workers who would never work for Solutia). As such, Old Monsanto structured the Spin-off by allocating to Solutia an excessive share of the liabilities and inadequate capital, leaving Solutia with little hope of surviving over the long term. The only saving grace that kept Solutia from failing immediately was the fact that the cash demands for these Legacy Liabilities were to be spread over a long time period and the markets did not appreciate the risks because the Legacy Liabilities were largely contingent liabilities that only Old Monsanto knew and never disclosed. Other factors contributing to Solutia's undercapitalization are described further in the Equity Committee Adversary Proceeding.

10. Old Monsanto rationalized its one-sided allocation of Legacy Liabilities by asserting that it was requiring Solutia to assume liabilities associated with the "chemicals" business. However, the reality is that the production of most, if not all, of the "chemicals" that give rise to the most significant Legacy Liabilities had ceased many years before the Spin-off and that those "chemicals" had no more connection with the businesses transferred to Solutia than those businesses that remained with Old Monsanto. Indeed, in some cases, the historical "chemicals" at issue (such as herbicides containing dioxin produced in Nitro, West Virginia) were more closely aligned with the agriculture business retained by Old Monsanto, yet Old Monsanto still forced those liabilities on Solutia.

11. Solutia was undercapitalized from its inception and could not service the substantial liabilities that were transferred to it from Old Monsanto. Old Monsanto's awareness and concern regarding its undercapitalization is evidenced by, among other things, Old Monsanto's failure to disclose the full extent of the Legacy Liabilities being foisted off on to Solutia to either the debt rating agencies that determined Solutia's investment grade credit rating or to the then and future public shareholders of Solutia.

12. Based on a review of the documents, it appears that in structuring the Spin-off, Old Monsanto knew or should have known that significant residual environmental contamination existed at its historical chemicals plants due to Old Monsanto's failure to invest in environmental controls at the time it manufactured such infamous chemicals and other hazardous materials as dioxin, agent orange and PCBs. However, the true risks associated with Old Monsanto's historical production of these infamous chemicals had never been disclosed to its own shareholders/investors, including the risks that certain events, if they occurred, could cause the environmental liabilities to exceed the \$1 billion range.

13. Instead, the information Old Monsanto provided to the public in connection with the Spin-off and the ultimate sale of Solutia stock was incomplete and misleading. The public disclosures painted a picture of a company with manageable environmental and tort exposure in the \$250 million range. In particular, the disclosures made to unsuspecting equity holders failed to adequately describe the significant environmental challenges and costs that Old Monsanto knew it faced.

14. Full disclosure to its investors of the truth about the scope of Old Monsanto's environmental liability exposure at the time of the Spin-off would have jeopardized Old Monsanto's ability to successfully transfer these significant liabilities to Solutia. In the end, Old

Monsanto dumped all of these legacy environmental and related tort risks into Solutia without properly disclosing the true nature of the risks to prospective equity investors in the public markets and without transferring sufficient assets to Solutia to service these liabilities, thus rendering Solutia undercapitalized and insolvent on the date of the Spin-off.

15. Not only did Old Monsanto force Solutia to assume these and other significant Legacy Liabilities, it required an indemnity from Solutia to protect Old Monsanto from the risk that it would choose to or be required to pay any amounts on account of those Legacy Liabilities. Compounding this inequity, Old Monsanto and New Monsanto required Solutia to grant the same indemnity to its subsequently spun-off company, New Monsanto, in 2002. New Monsanto provided no consideration to Solutia for this new indemnity obligation.

16. Old Monsanto and New Monsanto now seek to reap further benefits from Solutia (at the expense of Solutia's creditors and public shareholders) on account of the onerous and unconscionable indemnity provisions they required at the time of the Spin-off and thereafter. The Equity Committee objects to these efforts.

17. As a result of its investigation, the Equity Committee initiated the Equity Committee Adversary Proceeding seeking to disallow the claims asserted by Old Monsanto and New Monsanto and to avoid and challenge the indemnity provisions and ultimately require Old Monsanto and New Monsanto to bear the exclusive financial burden of the Legacy Liabilities they created.

18. The causes of action alleged in the Equity Committee Adversary Proceeding include various legal theories to disallow and avoid the claims asserted by Monsanto and Old Monsanto and, perhaps more importantly, also include various claims to *reallocate* financial

responsibility for the Legacy Liabilities back to Old Monsanto and/or New Monsanto where it properly belongs.

19. The Equity Committee Adversary Proceeding asserts that based on the wrongful and inequitable conduct of Old Monsanto in connection with the Spin-off and New Monsanto in connection with Solutia's granting New Monsanto the indemnity on which many of New Monsanto's claims in this case are based, the proofs of claim filed by Old Monsanto and New Monsanto against the Debtors should be (i) disallowed and/or (ii) recharacterized and subordinated.

20. Moreover, based on the inequitable conduct of Old Monsanto and New Monsanto, through the Equity Committee Adversary Proceeding, the Equity Committee also seeks the following relief:

- A declaration by this Court that the provisions of the Distribution Agreement and Amendment thereto that provide for the assumption of the Legacy Liabilities by Solutia as well as the indemnities of Old Monsanto and New Monsanto, respectively, should be declared unconscionable and therefore void and unenforceable.
- A declaration that the estate has a right of contribution under CERCLA against Old Monsanto and New Monsanto for 100% of the liabilities relating to the environmental contamination caused by Old Monsanto and/or New Monsanto.
- A declaration that the estate is entitled to an implied indemnity in contract and/or in tort from Old Monsanto and New Monsanto for any claims made relating to the Legacy Liabilities, including environmental contamination and tort claims.

21. Both Old and New Monsanto have filed motions to dismiss the Equity Committee Adversary Proceeding that remain *sub judice*. The issues are fully briefed, the Court has heard oral argument on those motions, and the record is complete. The Equity Committee remains confident that the detailed allegations of the complaint in the Equity Committee Adversary

Proceeding, as bolstered by the evidence provided through even the limited discovery permitted to the Equity Committee, will survive the motions to dismiss.

22. If successful, the Equity Committee Adversary Proceeding could result in billions of dollars of value being effectively returned to these estates.

The Plan of Reorganization and The “Global Settlement”

23. On February 14, 2006, Debtors filed their proposed Plan and Disclosure Statement. Confirmation of the Plan is premised on approval of a “Global Settlement” that, among other things, purportedly resolves the Equity Committee Adversary Proceeding. The Equity Committee is not a party to this “Global Settlement” and does not support it.

24. Debtors justify the settlement of the Equity Committee Adversary Proceeding based on consideration to be provided by New Monsanto. However, these so-called contributions from New Monsanto are largely illusory and do not come close to justifying the settlement and resolution of a litigation that could return far more value to these estates.

25. According to the Debtors, New Monsanto is providing the following contributions:

- \$250 million to fund Funding Co. Funding Co will then fund \$175 million Retiree Trust, \$50 million towards environmental liability related to Shared Sites and \$25 million for miscellaneous Legacy Liabilities;
- Backstop of the Rights Offering (using the same \$250 million that will fund Funding Co) and waiver of the \$12.5 million Backstop Fee;
- Assumption of financial responsibility, as between Solutia and New Monsanto for Tort Claims;
- Assumption of financial responsibility, as between Solutia and New Monsanto for the Category B Sites;
- Assumption of a limited amount of the financial responsibility, as between Solutia and New Monsanto, for the Shared Sites;

- Resolution and settlement of the various adversary proceedings pending against New Monsanto, including the Equity Committee Adversary Proceeding, and the proofs of claim filed by New Monsanto; and
- Assumption of certain operational agreements between Solutia and New Monsanto.

26. In reality, New Monsanto's alleged contributions are much less than advertised, for the following reasons:

27. *First*, the \$250 million of New Monsanto's contribution to Funding Co is not to be paid on account of any of its responsibility for the Legacy Liabilities, but is payment for 22.7% of the New Solutia Stock pursuant to the Rights Offering. If the Rights Offering is fully subscribed by the unsecured creditors, New Monsanto will not contribute a single penny of the \$250 million.

28. It is this very same \$250 million that funds the entirety of the Retiree Trust of \$175 million, \$50 million of Legacy Environmental Liabilities and \$25 million of miscellaneous Legacy Liabilities. Thus, if the Rights Offering is fully subscribed by third parties, then New Monsanto will not make any contribution whatsoever towards any of those items. Even if New Monsanto funds the Rights Offering, it will receive equity in Reorganized Solutia that is being valued at the same amount of \$250,000,000, but is probably worth much more.

29. *Second*, adding insult to injury, New Monsanto has been granted a \$12.5 million fee from Solutia on account of New Monsanto's willingness to backstop a Rights Offering that results in New Monsanto paying nothing towards the Retiree Trust and reducing its exposure to the Legacy Liabilities by another \$75 million. It is no wonder that New Monsanto is now prepared to waive such a fee so long as such waiver is also counted towards its alleged contribution.

30. *Finally*, New Monsanto's only legitimate contributions that can arguably be on account of the potential liability it faces in the Equity Committee Adversary Proceedings are (i) acceptance of the Tort Liability, (ii) acceptance of responsibility for the Category B Legacy Environmental Liabilities, (iii) its additional \$50 million (of which \$32 has already been contributed towards the Shared Sites; and therefore credited), and (iv) its acceptance of responsibility to share 50/50 with Reorganized Solutia for the Shared Sites *after* Reorganized Solutia has spent \$325 million for such liabilities. Notably, Old Monsanto created all of these Legacy Liabilities long before the Spin-off and forced both Solutia and New Monsanto to indemnify it for those liabilities. Solutia did not create any of these Legacy Liabilities and is liable only the basis of its contractual indemnity to Old Monsanto.

31. Based on its investigation and analysis to date of the Legacy Environmental Liabilities, the Equity Committee submits that the largest dollar exposure in the future relates to the Shared Sites. By dividing responsibility for these Shared Sites as proposed in the Plan, the bulk of the economic responsibility for these liabilities will be borne by Reorganized Solutia, not New Monsanto. Indeed, of New Monsanto's alleged first \$100 million to be contributed, \$50 million comes from the Rights Offering and so may not represent New Monsanto's own cash or, to the extent New Monsanto does make that contribution in cash, New Monsanto will receive stock in Reorganized Solutia for such contribution.

32. In stark contrast to the "Shared Sites" for which New Monsanto places the greater financial burden on Solutia, New Monsanto's liability relating to the Category B Sites will be far less expensive over time. These Category B Sites represent sites that were sold or abandoned long before the Spin-off and represent some of the sites with the smallest exposure of the many Old Monsanto sites creating the Environmental Legacy Liabilities.

33. In return for New Monsanto's paltry contribution under the Plan, New Monsanto will receive full releases and injunctive protections from significant portions of the Environmental Legacy Liabilities, including NRD claims, as well as a release from the Retiree Legacy Liabilities. New Monsanto will also receive up to 22.7% of the New Common Stock on account of these same "contributions."

34. Even more disturbing than New Monsanto's illusory contributions, Old Monsanto makes no legitimate contribution whatsoever. Old Monsanto merely releases the claim it filed in the bankruptcy. Old Monsanto's claim was merely a claim for anything covered by its indemnity from the Spin-off. Of course, New Monsanto made the same claims for which it is at least making a paltry contribution to resolve. However, for no monetary contribution whatsoever, Old Monsanto receives releases and injunctions that protect it from all of the Legacy Liabilities.

35. Old Monsanto may not have gone as far as to require New Common Stock in return for its "contribution" but, because its claims overlap almost entirely with claims also made by New Monsanto, Old Monsanto has effectively required Solutia to pay twice on the same claims.

36. Remarkably, Solutia seeks to settle the Equity Committee Adversary Proceeding (which could bring billions of dollars of value to the estate) for only a negligible contribution by New Monsanto and Old Monsanto.

37. On its face, the Equity Committee believes that there is no way such a settlement can survive scrutiny under Rule 9019 of the Federal Rules of Bankruptcy Procedure or that a Plan based on such settlement can satisfy the standards for confirmation under the Bankruptcy Code.

38. Even based on the limited discovery to date, the Equity Committee submits that there is sufficient evidence of the potential liability of Old Monsanto and New Monsanto for claims made in the Equity Committee Adversary Proceeding to require this Court to reject the Global Settlement proposed in the Plan and allow the Equity Committee to prosecute its Adversary Proceeding against Old Monsanto and New Monsanto.

39. However, to fully explore the Equity Committee's challenge to the Debtor's Disclosure Statement and Plan (as well as the Equity Committee's necessarily overlapping Adversary Proceeding), the Equity committee believes that the following discovery, all long sought and all outstanding, is critical: (i) written discovery addressed to the Debtors, New Monsanto, Old Monsanto, and the Committee of Unsecured Creditors (including interrogatories, requests for production of documents, and, as to Old Monsanto only, requests for admissions), all of which written discovery has been served, and (ii) depositions of the corporations (Solutia, New Monsanto, and Old Monsanto) pursuant to Rule 30 (b) (6), and the oral depositions naturally flowing therefrom, including those of corporate decision makers and experts.

40. Only with this additional discovery, and the presentation of a full evidentiary record in support of the Equity Committee's claims, will this Court be in a position fairly to evaluate the settlement and compromise of the Equity Committee Adversary Proceeding proposed by the Plan. Further, in order for this Court and all interested parties to be fully informed, the foregoing discovery should be completed before the Court conducts a hearing to consider the adequacy of the Disclosure Statement.

Dated: March 9, 2006
New York, New York

Respectfully submitted,

/s/ Craig A. Barbarosh

Craig A. Barbarosh (CB 6977)

Karen B. Dine (KD 0546)

David A. Crichlow (DC 2116)

PILLSBURY WINTHROP SHAW PITTMAN LLP

1540 Broadway

New York, New York 10036

Telephone: (212) 858-1000

Facsimile: (212) 858-1500

Counsel for the Official Committee
of Equity Holders of Solutia Inc., *et al.*