



Mining Committee Newsletter

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MESSAGE FROM THE CHAIR

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We are pleased to present the 2005-2006 winter Mining Committee Newsletter. We have included articles from expert practitioners on several cutting edge issues which we hope will be of assistance to mining law practitioners.

We will stay abreast of the status and progress of mining law reform to enable us to keep you up to date on mining law reform through internet communications, our spring newsletter and a teleconference which is being planned for early in the new year.

Feel free to contact me if you are interested in becoming more involved in the committee or if there are topics on which you feel we ought to be focusing on as part of our mandate. All the best in 2006.

**ABA Section of Environment, Energy,
and Resources**

**14th Section Fall Meeting
Oct. 4-8, 2006
San Diego, California**

PLAN TO ATTEND!

MESSAGE FROM THE EDITOR

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This issue offers several practical perspectives of the various environmental and financial issues relating to mine closure. In the first article, Joseph Zaluski and Lesly Davis describe how a coal mining entity can either complete or satisfy its permit obligations to avoid liability to the corporate entity or the individual operator. Denise Dragoo offers an analysis of Section 436 of the Energy Policy Act of 2005 which establishes a bond waiver provision for federal coal lease bonus payments. Then Bill Gorton provides an overview of the use of surety bonds to satisfy the reclamation obligations for permits issued under the federal Surface Mining Control and Reclamation Act. Lastly, James Pray evaluates the practical problems that arise when reclaiming surface mines after the original mining company has ceased operations or been forced out of business.

While these articles all relate to the coal industry, the concepts apply equally to other mining industries and I hope that you find these articles as insightful and interesting as I have. I want to thank our authors for their contributions and for making this issue a success.

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**EXITING THE COAL MINING BUSINESS:
IS IT TRUE THAT DEATH IS THE
ONLY WAY OUT?**

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I. Introduction

As a result of the nation's growing energy demands, the coal industry is experiencing renewed investment opportunities and growth. Coal producing entities responding to market conditions naturally place emphasis upon those financial, technical, regulatory and environmental (including health and safety) issues which impact coal production and ongoing operations. These are not, however, the only considerations of importance. Regardless of how well a coal mining operation is planned by an entity when entering the business, and ultimately run, every coal mining entity must some day face the reality of how to exit or close an operation. Mine closure, although often a secondary consideration in mine planning, is a complex issue replete with complicated business decisions and regulatory requirements. Failure to follow a mine closure plan, however, could seriously jeopardize an entity's economic status as well as expose the entity and certain of its individuals to serious liability.

This article focuses on mine closure in the context of how a coal mining entity completes or satisfies its obligations in regard to a particular coal mining permit, the goal being to close an operation without the possibility of ongoing entity or individual liability.

II. Mine Closure

In general, there are three methods which can be used by a coal mining entity to satisfy its obligations on a given permit and achieve liability-free mine closure. The first method is to finish all on-ground coal mining and complete the regulatory-approved mining and reclamation plan. This includes performing all necessary reclamation and obtaining a Phase III, or

final, bond release. The second method to achieve closure on a permit and eliminate the risks of ongoing liability is to transfer the mining permit, often by virtue of a sale of the stock or assets of a coal mining entity. Finally, mine closure can be achieved through overpermitting, the act of a related or unrelated entity assuming responsibility for a permitted area. Under all three scenarios, careful planning must be performed so that a coal mining entity or certain individuals related thereto can avoid ongoing responsibility and liability, including but not limited to, civil penalties, reclamation responsibilities, and the complexities of the ownership and control regulations and Applicant Violator System, both of which are discussed below.

A. Completion of Mining Obligations

The traditional method of completing coal mining obligations, whether surface or underground, is to complete all mining and reclamation and apply for a phased bond release on a given permit from the appropriate regulatory authority. Completion of mining and reclamation pursuant to an approved mining plan leads to “physical” mine closure. Upon issuance of a Phase III bond release, the coal mining entity is released from liabilities associated with the mine. To effectuate coal mine closure by virtue of this method, all mining must be completed and reclamation performed as approved by the applicable regulatory agency. Thereafter, bond releases can be pursued. A permittee may initiate an application of release for all or part of a performance bond applicable to a particular permit or increment after all reclamation, restoration and abatement work is completed. In Kentucky, the Environmental and Public Protection Cabinet (Cabinet), is required to inspect the permit and ascertain whether a bond release is appropriate and notify the permittee of its decision.

Generally, a Phase I release may be obtained when a permittee has completed all backfilling, grading, top soil placement, drainage control, and seeding and mulching in accordance with its approved reclamation plan. A Phase II release may be obtained when re-vegetation has been established, lands are not contributing suspended solids to stream flow, soil productivity has been restored and plans for the

management of permanent impoundments are implemented. Final reclamation, or Phase III reclamation, is deemed to have been completed on the entire permit area or increment when a permittee has successfully completed all surface coal mining reclamation operations in accordance with the approved reclamation plan such that the land is capable of supporting the post-mining land use and has achieved compliance with Kentucky’s coal mining program, KRS Chapter 350 and the regulations promulgated thereto. After a Phase I bond release is obtained, it is a minimum of five years until a Phase III release may be obtained.

Once a Phase III bond release is obtained, mine closure has essentially been achieved. A Phase III release releases the permittee, and certain individuals associated therewith, from further liability with one important exception. Under Kentucky mining law, the Cabinet is required to reassert jurisdiction over a permit if it is demonstrated that the bond release decision or written determination was based upon fraud, collusion, or misrepresentation of a material fact. Pursuant to Kentucky regulation 405 KAR 7:030 § 4, if any of these circumstances exist after a Phase III release is obtained, the Cabinet will reassert jurisdiction over the subject permit. This effectively reopens the permit and prevents mine closure in those situations in which the bond release was inappropriately obtained.

B. Transfer of Mining Obligations

The alternative to fulfilling mining obligations through the completion of mining and performance of reclamation is to transfer a mining permit, often by sale of the mining operation. A transfer of mining obligations can be effectuated through a sale of the stock or the assets of a coal mining entity. When the stock of a coal mining entity is sold, the entity’s name remains the same although with new owners. If the transaction involves a substantial sale of stock, as determined by the regulatory authority, the entity must go through the transfer process and have the permits transferred to itself. This requires the filing of new ownership and control information. In this situation, any outstanding violations and penalties will remain

with the permit holder even though the stockholders have changed.

In the event that a purchaser is interested in buying only certain assets rather than the entity itself, a purchaser may acquire only the assets and the liabilities desired. In an asset sale, the subject permits must be transferred with new ownership and control information filed. In this case, the seller remains responsible for any outstanding violations and penalties. The purchaser, however, must acknowledge any unperformed reclamation on the transferred permit and agree to complete the same. This is generally accomplished by virtue of a reclamation agreement or permit condition entered into between the regulatory authority and the asset purchaser. Failure to abide by the reclamation requirements set out in the reclamation agreement will subject the purchaser to liability for reclamation and penalties in its own right.

1. The Permit Transfer Process

One of the most important aspects of any sale or acquisition of a coal mining entity, is the actual permit transfer process. There are a litany of statutory and regulatory requirements that must be met in order to transfer a permit. The transfer process may also be impacted by the regulatory authority's "improvidently" issued permit regulations.

In a sale or acquisition of a coal mining operation, the applicable permits must be transferred to the purchaser. In Kentucky, the transfer process is set out in 405 KAR 8:010 § 22. Pursuant to the Kentucky program, the applicant or successor in interest must file a complete and accurate application which contains basic administrative information, including the names and address of the proposed permittee, a brief description of the action requested for approval, and ownership and control and financial disclosures requirements. The intent to transfer must be published once in a paper of general circulation in the area where the permit lies, and 15 days must pass to allow the Cabinet to receive any comments on the proposed transfer before the transfer permit may be issued. In addition, at the time of the filing of the application, the transfer applicant must file a reclamation bond in an

amount equal to the bond currently posted for that permit. Pursuant to 405 KAR 8:010 § 22(8), upon the filing of the appropriate transfer documents and associated bonds, the transfer applicant may continue uninterrupted mining. Furthermore, the applicant may continue to mine until the permit is actually transferred. Following the transfer, the original permittee is absolved of future liability.

2. Improvidently Issued Permits

Although adherence to permit transfer requirements will normally effectuate a complete transfer of a mining permit, the regulatory authority may review all issued permits, including transferred permits, to determine if the same have been "improvidently issued." In Kentucky, if the regulatory authority finds under 405 KAR 8:010 § 25 that a permit should not have been issued because of an unabated violation, delinquent penalty, or fee, it may suspend or rescind the permit. Upon permit suspension or rescission, the permittee must cease all coal mining operations under the permit, except for violation abatement, reclamation and other environmental protection measures. The regulation essentially provides the regulatory authority with a means of correcting the improper issuance of a permit and thereby imposing ongoing liability on the permittee or other responsible person.

3. Ownership and Control Requirements

Surface and underground coal mining is regulated pursuant to the Surface Mining Control and Reclamation Act of 1977 (SMCRA). Under the act, primary regulatory authority is vested in the federal Office of Surface Mining (OSM). That authority has been delegated to certain states, including Kentucky, for permitting and enforcement. While OSM has retained oversight authority in those states, and retains permitting power for federal lands, the primary duties of permit issuance, inspection and enforcement are the obligations of the state by virtue of the delegated regulatory authority.

One of the most significant provisions of SMCRA is 30 U.S.C. Section 1260(c). This provision prohibits permit issuance where a surface coal mining operation

“owned” or “controlled” by the applicant is currently in violation of SMCRA. The federal clearing house for ownership and control information is known as the Applicant Violator System. The consequences of a permit block is that further mining is compromised since the regulatory authority will not process necessary applications for amendment and permits.

Kentucky’s definition for “owned or controlled” and “owns or controls” is found at 405 KAR 8:001 § 1(76). (Federal definitions for “control or controller” and “own, owner, or ownership” are found at 30 C.F.R. § 701.5) The regulation provides definitions for those persons or entities deemed to have “per se” control or ownership of an operation. Persons or entities within the “per se” category are irrebuttably presumed to have an ownership and control relationship with the violator. The “per se” relationships are defined at 405 KAR 8:001 § 1(76)(a)1.-3. as follows:

- Being a permittee of a surface coal mining operation.
- Based on instruments of ownership or voting securities, owning of record in excessive of 50 percent of an entity.
- Having any other relationship that gives one person authority directly or indirectly to determine the manner in which an applicant, an operator or other entity conducts surface coal mining operations.

405 KAR 8:001 § 1(76)(b)(1)-(6) provides definitions for those persons or entities who are “presumed” to have ownership or control of a person or entity. An applicant may rebut an ownership and control presumption by demonstrating that the person subject to the presumption does not in fact have the authority directly or indirectly to determine the manner in which the relevant surface coal mining operation is conducted. The “rebuttable” relationships include:

- Being an officer or director of an entity.
- Being the operator of the surface coal mining operation.
- Having the ability to commit the financial or real property assets or working resources of an entity.

- Being a general partner in a partnership;
- Based on the instruments of ownership or the voting securities of a corporate entity, owning of record 10 to 50 percent of the entity.
- Owning or controlling coal to be mined by another person under a lease, sublease or other contract and having the right to receive such coal after mining or having authority to determine the manner in which that person or another person conducts a surface coal mining operation.

The purpose of these regulations is to induce, some would say coerce, remedial action for unabated violations under SMCRA and KRS Chapter 350. Under the regulations, an applicant is not required to perform a violator’s obligations. Practically, however, an applicant whose relationship falls within the broad definition of ownership or control must undertake the violator’s obligations under SMCRA or KRS Chapter 350 if it wishes to continue to do business in the coal industry. Failure to do so could result in a complete “permit block” for the applicant (or any other entity it owns or controls), including revisions or amendments to existing permits, having the eventual impact of shutting down an applicant’s business. Even an entity with an exemplary record of compliance could find its permits jeopardized and the life blood of its business threatened through a “permit block.”

4. The Applicant Violator System

The federal clearinghouse for ownership and control information is known as the Applicant Violator System (AVS). The AVS is an automated information system of applicant, permittee, operator, violation and related data maintained by states and OSM (the Kentucky clearing house is referred to as the Surface Mining Information System or “SMIS”). The AVS is programmed to identify “links” between known violators and applicants, individuals and other entities. Federal and state regulatory authorities who make permit eligibility decisions required by section 510(c) of SMCRA use this information. By checking the AVS for established links during the review of permit applications, regulatory authorities can determine whether an applicant has outstanding violations.

If a link is deemed to exist at the time of the permit application, including permit revisions and amendments, OSM will provide that information through the AVS to the state regulatory authority. Upon receipt of this information, the state may use that information to recommend a permit block until the link is rebutted, or until reclamation, penalties or a bond forfeiture resulting in the denial of the recommendation is resolved. The consequence of a permit block is that further mining is compromised since the regulatory authority will not process necessary applications for amendment and permits. The AVS must also be checked prior to awarding Abandoned Mine Land (AML) reclamation contracts.

The impact of both the ownership and control regulations and the AVS on mine closure is significant. Although neither the ownership and control regulations nor the AVS compel any entity or individuals to take remedial action or pay penalties or fees, both insure that these persons remain “responsible” for such outstanding obligations. Through imposition of indirect liability, *i.e.*, ownership and control links and “threatened” permit blocks through the AVS, those who seek to transfer their liabilities and thereby obtain mine closure are effectively prevented from escaping responsibility and ignoring outstanding obligations.

C. Overpermitting

A third and final mine closure method is through the use of overlapping permits. In this situation, an applicant for a subsequent permit for surface mining activities obtains the right to mine coal by partially or totally overlapping an existing bonded permit. In Kentucky, Reclamation Advisory Memorandum #56 (RAM 56) details the specific liabilities for the overlapping permittee. For example, if a permit applicant seeks a permit involving a partial or total overlap, the applicant, and any surety on his bond, must expressly agree that the applicant is responsible for reclamation of the entire permit area proposed in the permit application. The applicant cannot permit an overlap area for which he will not take responsibility. Once the permit is issued, the overlapping permittee is liable for, and his bonds must guarantee, reclamation for all of the permit area. This includes overlapping areas which may have been

previously disturbed. The permit applicant may not conduct surface coal mining operations prior to issuance of the overlapping permit. RAM 56 also provides that the overlapping permittee will not be held responsible for a notice of violation issued to the prior permittee. The Cabinet may, however, require the overlapping permittee to take certain interim remedial measures due to environmental conditions of the site.

By seeking and obtaining an overlapping permittee to partially or completely overlap a permit, the original permittee is relieved of responsibility for future reclamation and for bond coverage. An important caveat does exist. The original permittee must be cognizant of the fact that it will remain responsible for violations issued prior to overlap. Thus, the original permittee cannot completely escape all liabilities associated with the overlapped permit in an effort to obtain mine closure.

III. Mine Closure Liabilities

A. Alternative Enforcement Action

Although SMCRA contains comprehensive regulations governing permitting and performance standards, the act cannot assure compliance in and of itself. When a permittee fails to comply, the regulatory authority may compel compliance by the permittee through many enforcement mechanisms. These mechanisms include the threat or imposition of civil and criminal penalties, issuance of violations and cessations orders, and injunctive relief.

The regulatory authority may also choose to compel a non-permit holder to comply with SMCRA. Such an act may be taken independent of or simultaneously with enforcement action taken against a permittee. Various enforcement mechanisms are available to a regulatory authority seeking non-permit holder compliance with SMCRA. Aside from ownership and control links and AVS listings, one of the most effective measures to compel non-permit holders to comply with the act is to compel injunctive relief requiring the performance of remedial measures or reclamation under the act. Likewise, the penalty provisions of SMCRA provide that persons who willfully and

knowingly violate a permit condition, the federal or applicable state program, or who fail or refuse to comply with an order issued under the act, may be punished by a fine of not more than \$10,000.00, or by imprisonment for not more than one year, or both. In addition, the directors, officers or agents of corporations who willfully and knowingly authorize, order or carry out violations of the act may be subject to civil penalties, fines or imprisonment.

In a mine closure context, the permittee, as well as the directors, officers and agents thereof, should be cognizant of alternative enforcement actions which may be taken against the mining entity or individuals. To believe that a mine can simply “shut down” is naïve and ill-advised. Outstanding violations and reclamation as well as unpaid penalties can all lead to direct as well as alternative enforcement activities against a permittee or its directors, officers and agents. There is simply no “walking away” from a coal mine without the threat of ongoing regulatory enforcement activities for unresolved obligations.

B. Bond Forfeiture

The federal and state regulatory programs require that applicants for mining permits post performance bonds for those areas to be affected by the surface operations and facilities. The bonds are conditioned upon the faithful performance of all requirements in the regulatory authority’s mining program. Bonding may be effectuated by the posting of surety bonds or collateral bonds (cash deposits, certificates of deposits and letters of credit) or a combination of both.

Regulations provide for procedures and criteria by which a regulatory authority may forfeit a bond. Bonds for a permit area or increment may be forfeited for a number of reasons including, but not limited to, failure of a permittee to comply with the terms or conditions of the bond; failure to take corrective action; failure of a permittee to conduct surface coal mining and reclamation operations in accordance with the statutes and the regulations promulgated pursuant thereto; revocation of a permit for which a bond is posted; or failure of a permittee, surety or financial institution providing bonds to comply with a compliance schedule approved by the regulatory authority in an effort to

withhold forfeiture. A bond may also be forfeited if a permittee has become insolvent; cannot demonstrate its ability to continue its operations in compliance with the law; has failed to pay penalties or fines; or if a creditor of the permittee has attached or executed judgment against the permittee’s equipment, materials or facilities.

Forfeiture of a bond represents yet another method by which liability can attach preventing complete mine closure. Upon forfeiture, the permittee is entered into the AVS and subject to future permit blocks until reclamation obligations are satisfied. This ultimately makes the transfer of permits more complex and mine closure more unlikely.

C. Debarment

Environmental debarment enforcement efforts can have a drastic effect on the economic well-being of an entity, particularly when the business relies on federal contracts or grants. Suspension and debarment are administrative procedures to protect the government from undesirable contractors by excluding them from receiving new government contracts based on evidence that the contractor lacks “present responsibility.” Suspension is an interim refusal to deal with a contractor pending further information. Debarment is a disqualification of a contractor for a set amount of time. Suspension and debarment by one agency can be effective throughout the federal government. OSM has taken the position that the agency may prohibit contractors with unabated violations under SMCRA from entering into agreements to perform federally funded reclamation on abandoned mine lands. Other federal agencies have debarment policies which may require disclosure of unabated environmental violations, unpaid civil penalties or bond forfeitures. Thus, failure to remediate or pay civil penalties in a mine closure context, despite a seller’s best efforts to transfer its on-ground liabilities, could lead to debarment ramifications under current federal policies.

IV. Conclusion

There is an old axiom in the coal mining industry that the only way out is to die. The intricacies of coal mine closure certainly support that view of the business. If a

coal mining entity does not obtain mine closure by completing its mining and reclamation plan and obtaining a Phase III release, or by appropriately structuring a contract to sell or transfer its obligations, the regulatory authority has a plethora of enforcement techniques to compel satisfaction of regulatory obligations. Moreover, in many jurisdictions including Kentucky, the regulatory authority can deem a transferred permit to be improvidently issued or can reassert jurisdiction for a permit if a bond release is found to have been based upon fraud, collusion or misrepresentation of material fact. Under this framework, only careful technical, regulatory and legal planning can lead to closure of a coal mine without the threat of continued regulatory responsibility.

ENERGY POLICY ACT, SECTION 436: WAIVER OF BOND FOR FEDERAL COAL LEASE BONUS PAYMENTS

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Section 436 of the Energy Policy Act of 2005, Pub. L. 109-58 (the "Act"), provides some long-sought relief to the coal industry regarding bonding requirements for federal coal lease bonus payments. Under the Mineral Leasing Act, 30 U.S.C. § 201, et seq. (MLA), the U.S. Department of the Interior (DOI) must receive fair market value for the lease of federal coal reserves. The competitive coal leasing process allows qualified lessees to offer a bonus bid for coal tracts. Upon acceptance of the bonus bid and award of the lease, the lessee pays the bonus in five annual installments. 43 C.F.R. § 3422.4(c). The first installment is submitted with the bid and prior to enactment of the Act on Aug. 8, 2005, a bond was required to secure payment of the deferred bonus bid. Title IV of the Act amends the MLA, providing the secretary of the DOI discretion to waive financial assurance on the deferred bonus as to a lessee or successor in interest with a history of timely payment of: (1) non-contested coal royalties, (2i) advanced coal royalties in lieu of production and (3) bonus bid installment payments. The waiver applies to both existing leases issued prior to Aug. 8, 2005 and to future federal coal leases. MLA § 2(a)(4)(A) and (B), 30 U.S.C. § 201(a)(4)(A) and (B). In the absence of a bond or other form of financial assurance to guarantee payment, the Act authorizes the secretary to take harsh measures in the event that a lessee fails to timely pay the bonus bid. In such case, within 10 days after written notice of default, the lease is automatically terminated and all previous bonus payments are forfeited. MLA § 2(a)(5), 30 U.S.C. § 201(a)(5).

On Nov. 25, 2005, the federal Bureau of Land Management (BLM) issued interim guidance to implement § 436 of the Act in Instruction Memorandum No. 2006-045 (IM 2006-045). This guidance will remain in effect until new regulations are adopted regarding the financial assurance of the

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deferred bonus bid. Prior to enactment of § 436, the Bush administration provided lessees with some relief by reducing the amount of financial assurance from the full unpaid balance to one annual installment payment. WO-IM-2004-217. Under BLM's new policy, the requirement to secure one annual installment payment will continue in effect unless waived.

For leases existing on Aug. 8, 2005, lessees must submit an application to BLM to seek a waiver. The applicant must demonstrate that the lessee has a History of Timely Payment of non-contested royalties, advance royalties and bonus bid installment payments (HTP). The HTP application should provide the lessees' contact information, identify the subject mine, lease and surety bond, and list all federal coal leases and Surface Mining Control and Reclamation Act (SMCRA) permit numbers associated with the mine. For new leases issued after Aug. 8, 2005, BLM will waive the requirement of financial assurance to guarantee payment of the deferred bonus bid if BLM in consultation with the Minerals Management Service (MMS) determines that the lessee has an HTP. A new lease may only be issued with either a BLM determination that the lessee has an HTP or upon the lessee's provision of financial assurance covering one annual deferred bonus payment.

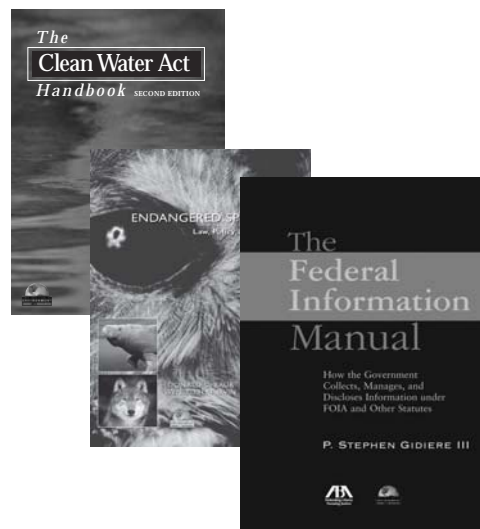
The HTP determination is based on the application submitted by a lessee to BLM. Following submission of the application, BLM requests MMS to review the applicant's payment history. The MMS will consider the lessee's payment history for the five years immediately preceding an HTP application. The MMS must determine that all applicable payments have been paid on time. Royalty payments are considered timely if paid by the date specified in the federal lease. Advance royalty payments must have been received within 35 days of the MMS order to pay date. Deferred bonus payments must have been received by MMS on or before the anniversary date of the lease.

BLM has also implemented a new policy regarding procedures governing the lessee's failure to timely pay the bonus bid. BLM is now required to verify with MMS that the annual deferred bonus bid installment payment has been timely received by MMS. This

verification is to occur within 30 days after the annual anniversary of the lease issuance date for coal leases with unpaid deferred bonus bids. If payment was not timely received, BLM must notify the Washington office to coordinate further action, including the possible termination of the lease and forfeiture of all bonus bid payments previously paid by the lessee.

BLM reports that the large coal operators in the Powder River Basin of Wyoming have all submitted applications for HTP determinations. These applications are currently under consideration by MMS, although no final HTP determinations have yet been issued. BLM anticipates that upon final HTP determination, bonus bid bonds in the range of several hundreds of millions of dollars will be released in the Power River Basin alone. This bond release should result in freeing up the bonding capacity of the insurance industry which could be applied to meet other bonding obligations of the mining industry, including federal lease bonds and reclamation bonds.

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RECLAMATION AFTER MINING COMPANY FAILURE

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This article addresses practical problems that arise when reclaiming surface mines after the original mining company has ceased operations or been forced out of business. This article is based on my experience working for surety companies in the state of Iowa. Active coal mining has come to an end in Iowa given the high sulfur content of Iowa's large coal reserves. This had left the state with a large number of unreclaimed coal mine sites.

Perhaps you have been retained by a surety company to handle legal matters arising from a reclamation project. Or perhaps you represent a new coal mining company which has purchased the prior operator and must now begin reclamation on completed sites. In either instance, it is possible that neither the surety company nor the new coal mining operator will have a clear understanding of what needs to be done on the site to achieve a successful reclamation. This can be a complicated undertaking when the former mining company is no longer in business. When this happens, there are several steps that the lawyer can suggest when assisting in the reclamation of a coal mining site on behalf of either a successor to a coal mining company or a surety attempting to reclaim a site to avoid bond forfeiture.

First, identify any former employees familiar with the reclamation plan, the mining activities on the site and any past reclamation activities. If available, these contacts may prove to be invaluable. Second, obtain possession of any documents that might assist in the reclamation. Although state and federal regulatory agencies will provide copies of the permit file and reclamation plans, there may be important information in the mining company files. Third, identify any permits that need to be maintained or renewed. Fourth, identify adjacent landowners and current landowners. If any time has passed between the granting of the

mining permit and the reclamation effort, it is quite possible that you may have to give notice to and work with new landowners. Sometimes those landowners may have a very poor or just plain wrong understanding of reclamation goals and procedures.

Obtain Cooperation from the Previous Operator

Although circumstances may not allow you to obtain the willing cooperation of a former mining company operator, if that cooperation can be achieved, then it is likely to be beneficial to your client. Even if managers are not cooperative, it may be possible to locate equipment operators with relevant knowledge. Also, coal mining operators are required to file regular reports with the regulatory agency as both mining and reclamation activities progress. However, these reports and maps may not be entirely accurate, or may not show the most recent changes. If possible, discrepancies between reclamation plans and existing field or mining conditions should be reviewed with the former operators. You may also be fortunate to find an agency inspector with relevant, recent knowledge of the site who is willing to lend some informal advice.

One of the most important types of information that can be obtained from former operators and managers is a frank evaluation of the accuracy of the written reclamation documentation for a site. Former operators may not harbor any loyalty to the former company now that they are either unemployed or working for a new company. As an example, it can be important to know whether erosion control structures were actually built as specified. Are the tile lines the specified diameter? Are they even in place or functional? Also, underground tile lines can be notoriously difficult to locate if they were not placed at the locations designated on the map. There may also be areas of the reclamation which contain exposed or barely covered acidic soils. Only a former employee may know where these soil types are located. You may also learn from former employees that short cuts were taken during the former reclamation that may jeopardize a successful reclamation and bond release. A knowledgeable and cooperative former employee can be an invaluable source of accurate information and commentary regarding a site.

Obtain Documents, Maps and Aerial Photographs

In addition to obtaining the cooperation of former operators and managers, it is important to gather documentation in the possession of the former operator before it disappears. If access to mining company files can be obtained voluntarily, then those records may include mining and reclamation maps and aerial photographs that can assist in the reclamation. The mining company files may also include reclamation maps with hand-drawn notations showing the most recent progress at a site that may not have made it into a formal updated filing with the agency. Getting the most recent information possible can be vital to achieving a cost-effective reclamation. There are several examples where this information can be helpful.

Current reclamation regulations require that the reclamation plan include restoring the land to the proper post-mining use. It may not be obvious from a visual walk-through where the mining operator has stockpiled topsoil. I have seen sites in which the topsoil stockpile was old enough that the trees on the pile were more than a foot in diameter. Without necessary records, it would have been difficult to locate the topsoil necessary for the reclamation work.

Aerial photography of a site taken during summer months may also disclose problems with vegetation that may not be apparent during winter months, allowing for better planning and estimation of reclamation costs. Such photographs may also show locations of exposed acidic soil or areas in which the surface has been affected by underground mining.

Missing information from the former operator can be replaced or supplemented with documentation from the regulatory agency. Most regulatory agencies overseeing mining will have access to fairly regular aerial photography of mining sites. For surface mines, these photographs can be very helpful. Aerial photography can not only show the mining or reclamation in progress, but can also disclose possible areas of erosion that need to be addressed. High-resolution aerial photography can either be found in large-format rolls or in digital form. Some mining sites

can be very large and aerial photography can be invaluable in determining the scope of work that is necessary to reclaim a site.

Expired Permits

Another step that needs to be taken when taking over an existing reclamation obligation is to be certain that you have identified all relevant National Pollutant Discharge Elimination System (NPDES) permits. If any permits are expired, or are set to expire, then you will need to either renew those permits in the name of a new entity or obtain a waiver from the agency in overseeing those permits. Changing water quality laws may make it more difficult to obtain a new permit.

Coordination of Information

Once you have obtained all of the available documents and information from the regulatory agencies, the former mining company and any cooperative former operators, you should make sure that this information is reviewed by whatever engineer or firm will be handling the reclamation project. In my experience, agencies are quite willing to meet with whoever is undertaking the reclamation project to discuss the reclamation plan. Inaccuracies between the reclamation plan and the reclamation as actually built should be identified as early as possible. If the actual situation does not match the reclamation plan, then you should consult with the engineer to determine if the as-built structures can meet the regulatory requirements. If they are acceptable from an engineering standpoint, but do not match the reclamation plan, then the reclamation plan should be amended to match the as-built design if this is acceptable to the regulatory agency. If not, then you will need to decide if it is cost-effective to either redo the reclamation work or challenge the permit amendment denial. You may also discover through your due diligence process that some erosion control structures approved by the regulatory agency are poorly constructed, inadequate or non-existent. It is your client's best interest to fix those deficiencies as soon as possible. It can cost much more to repair damage caused by poorly performing erosion control structures than it costs to replace the structure.

Identify and Meet with Owners of Surface Rights and Adjoining Landowners



One of the difficult challenges that rise in the wake of a failed mining operation is the wrath of angry landowners. Those landowners may have claims or even judgments against the former mining operation that include broken leases and missing royalty payments. It is important to establish communications with those landowners and to assure them that your client is not the same company as the company that had previously been mining the site. If your client is a new mining company, then this task may be even more complicated. If, on the other hand, your client is a surety company, then the landowners will need to understand that the surety bonds are not available to them, but can only be used to either reclaim the site or be paid to the agency holding the bond as a penalty. Some landowners may even retain counsel in an effort to make a claim on a bond, mistaking it for an insurance policy or indemnity fund.

All communications with landowners need to specify the distinction between the former operator and whoever is the current operator or surety company. Nevertheless, depending on the laws of your state, your client may need to renegotiate access rights to the mine site that your client is obligated to reclaim. Not all states have clearly developed laws governing the relationship between mineral right owners and surface right owners. Breaches of royalty payment obligations and leases by the former mining operator may complicate negotiations as well. In my experience, the offer by your client to restore the land to a new use is usually sufficient to gain the cooperation of the landowner.

If any time has intervened between the cessation of mining activities and the reclamation effort that your client will be handling, then you may also find that the current landowner is using the land for a use that is completely incompatible with an approvable post-mining land use. I have found instances in which row crops may be planted on highly erodible soil that was quickly removing what topsoil was left on the site after a previous reclamation effort. I have also found entire surface mining sites placed in the conservation reserve

program and replanted with grasses that are not on an approved post-mining use.

This issue was resolved by working with the Department of Agriculture and the agencies overseeing the mining regulations and amending the reclamation plan to match the conservation reserve planting requirements. Another problem that can arise given the passage of time is that temporary sedimentation ponds can also become favored water sources for cattle ranchers and duck hunting preserves for hunters. These ponds can be reengineered and, if they meet specifications, can be certified as permanent ponds. Otherwise, they must be removed. These issues can be avoided when there is an active presence by the mining company but can multiply once that mining company has gone out of business.



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The Mining Committee welcomes the participation of members who are interested in preparing this newsletter. If you would like to lend a hand by writing, editing, identifying authors, or identifying issues, please contact the editor Joseph M. Dawley at jdawley@bccz.com.

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RECLAMATION BONDS FROM THE SURETY PERSPECTIVE

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Introduction

Financial guarantees, most commonly in the form of corporate surety bonds, are required by state and federal law to fund reclamation should the permittee default. In the event of a mining company defaulting on its reclamation obligations, a bonding company may propose to perform the obligations of the permittee. The negotiations with the regulatory agencies, surface and mineral owners and other interested parties can create a very complicated scenario that requires an understanding of the law regarding environmental protection, bankruptcy and suretyship, along with technical expertise in land reclamation. Though presented in the context of the coal industry, the principles discussed below are generally applicable to the mining industry as a whole.

Surface Mining Control and Reclamation Act

The regulation of coal mining in the United States is governed by the federal Surface Mining Control and Reclamation Act (SMCRA). Several purposes of SMCRA include the establishment of a nationwide program to protect society and the environment from the adverse effects of surface coal operations, assuring the rights of surface landowners and other persons with a legal interest in the land are fully protected and assuring that adequate procedures are undertaken to reclaim surface areas as contemporaneously as possible with the surface coal operations.

Under SMCRA a mining company must file an application for a surface mining permit which includes detailed operations and reclamation plans and the posting of reclamation performance bonds. SMCRA has specific regulatory frameworks for bonding the reclamation plans and performance of the coal mine permittee. Bonds may be in the form of a corporate

surety bond, cash collateral or securities. The bonded obligations often include compliance with other environmental laws and regulations often including laws related to water quality, coal refuse disposal, mine subsidence and waste management.

Suretyship

Very few outside of the surety industry (including judges), fully understand exactly what a surety bond is. Many mistakenly regard “bonds” as insurance policies. Suretyship is not insurance. The distinction between the two concepts is as follows:

In suretyship: There is a three-party contract where a surety provides a financial guarantee only if the principal (permittee) fails to meet its obligation to the obligee (regulatory agency). The principal is required to reimburse the surety; therefore a surety expects no loss. The principal is the primary obligor and the surety is the secondary obligor. The surety relationship with a mining company is basically an extension of credit by the bonding company to the permittee.

In insurance: There is a two-party contract where an insurance company spreads the risk of losses over a group of insureds and expects to take a loss during the policy period. If an insured event occurs, the insurance company pays with no recourse against the insured.

Many principles of surety law apply along with the regulatory framework. For example, “subrogation” is an important concept that allows the surety to “step into the shoes” of either the permittee or the regulatory agency depending on the situation. A surety is entitled to assert all of the defenses of its principal. A surety who pays the debts of another is entitled to all the rights of the person he paid (obligee) to enforce his rights to be reimbursed. The doctrine of subrogation also allows a surety to step into the shoes of the government for whom the job was completed.

In a bankruptcy context, there are often conflicts between secured creditors (lenders) who want money from the bankrupt estate and the regulatory agency, permittee and surety who all want reclamation accomplished. The surety, for example, can argue the

state's position regarding the need for compliance with state law under § 959 of the bankruptcy code.

Bond Forfeiture

Until the recent surge in coal prices, numerous companies with large coal mine environmental obligations have been dissolved or become bankrupt in the last 10 years, including most recently Horizon Natural Resources, Lodestar Energy, LTV Steel, Bethlehem Steel, AEI Resources, Quaker Coal, Pen Holdings, Anker Energy and others. In such an event, notwithstanding a potential successful reorganization, coal operations that have stopped in mid-operation become "problem mines," and may be subject to bond forfeiture for various reasons.

Under SMCRA, the regulatory agency must notify the permittee and surety of its intent to forfeit the bonds and advise of conditions under which forfeiture may be avoided. By this time, however, it is usually very late in the game for the surety to be able to have significant influence over its bonded principal. Earlier notice to the surety when the agency anticipates a problem may have a more positive result and may avoid forfeiture altogether. As a matter of fact, during the SMCRA rulemaking process OSM recognized that "adequate latitude is available for the regulatory authority to withhold forfeiture if an operator or a surety agree to a compliance schedule for completing reclamation successfully."

Under SMCRA the agency can generally proceed to collect the bonds unless there have been actions to avoid forfeiture or an appeal has been filed; however, some states (*e.g.*, Kentucky) require a pre-payment of the bond in order to pursue the appeal.

Principles of surety law ordinarily allow a surety to either perform the bonded obligation in the event of a default or to pay the bond amount. Under SMCRA and most state programs surety reclamation is allowed. Based on our experience in the field, under the most complicated technical and legal scenarios, surety reclamation should be encouraged.

Surety Reclamation Workouts

Many of the most complicated matters facing the regulatory agencies and sureties have involved the large company bankruptcies or dissolutions with numerous sites involving all aspects of mining. The handling of these matter, particularly by the agency, affects other interests including landowners, neighbors, communities and environmental interests.

If the bond is forfeited and collected by the agency, the agency, usually through its abandoned mine reclamation program, may conduct reclamation under specific, time consuming and generally more expensive state procurement procedures.

It has been our experience that surety reclamation can provide more reclamation on the ground per dollar by using private sector resources, expedience and experience in bidding and contracting.

Recent successful surety reclamation projects have included:

- Open dragline pits
- Acid mine drainage passive system development
- Burning refuse piles
- Mine shaft closures
- Borehole sealing
- Prime farm land restoration
- Wetlands/habitat enhancement
- Preparation plant demolition
- Coal refuse/slurry impoundment reclamation
- PCB removal
- Aerial tram removal
- Contour mine reclamation
- Hydraulic seals to flooding deep mines.

Reclamation is conducted under a Consent Order and Agreement, Consent Agreement or Settlement Agreement which defines the scope of work, work schedule and bond release or "waiver of collection" schedule where the bond remains technically "forfeited."

A critical factor to the surety is “certainty” as to performance requirements since it will have conducted its own engineering/economic analysis regarding the project prior to signing an agreement to perform. The surety is not the permittee and is not subject to permitting requirements as is an operator.

Many of the larger cases are also subject to U.S. Bankruptcy Court jurisdiction therefore the surety, permittee and agencies must deal with a Trustee or Debtor in Possession and other creditors. Most real legal conflicts occur here due to the intersection of environmental law, surety law and bankruptcy law. There are inherent competing interests:

Goals of bankruptcy law: return funds to creditors;

Goals of SMCRA: get land reclaimed (*i.e.* put money in the dirt)

The surety and agency interests are usually aligned in bankruptcy proceedings, however, often the agency takes a back seat in the proceedings.

Problems in Negotiating Surety Agreements

Large multi-mine bankruptcies create very complicated situations, technically and legally, and require significant time and effort to understand relevant relationships and prospects for successful emergence from bankruptcy in order to develop strategy or for a coordinated approach with all parties in the event of a liquidation.

Due to usual negative history with the permittee leading to bond forfeiture the surety is often faced with an irritable audience at the agency and with landowners.

Very often, the principal/permittee is in arrears regarding royalty payments to the mineral owners, has left surface owners’ property in disrepair and has created bad relations with the regulatory agency.

More often than not, regulatory staff does not understand suretyship and often confuses the surety as a surrogate coal operator or an insurance policy issuer.

Regulatory staff often view the bond amounts as “agency money.”

Notwithstanding recent efforts by some states to require “full cost” bonding, it is not uncommon for the bond amount to not cover full reclamation since the operation was stopped in mid-stream.

Bankruptcy court jurisdiction may overlay the entire matter.

Landowners and mineral owners can be recalcitrant and litigious.

Bankruptcy court approval of any workout is necessary (remember, the primary environmental obligation is that of the bankrupt company).

When Reclamation Exceeds the Bond Amount

SMCRA allows the agency to pursue the permittee for excess costs if the bond amounts do not cover the reclamation costs. However, most agencies appear reluctant to pursue alternative enforcement, relying only on the bond as possibly supplemented by government funds.

Contrary to the goals of SMCRA, in recent experiences with a few states we were told “OSM won’t let the state enter a surety agreement if it’s for less than the entire permitted reclamation plan” even though there are discrete, identifiable reclamation tasks that must be accomplished: *e.g.*, eroding hollow fill on steep slopes; acid filled pits, where the surety would have been able to abate the hazard or make a substantial contribution to reclamation within the bond amount, but not reclaim the entire site.

In other cases, in resolution of appeals filed with the administrative hearing officers under SMCRA or in the bankruptcy cases we have been able to identify key tasks in the reclamation plan that required immediate attention or high priority and come to an agreement on scope of work and waiver of bond collection. In such cases, it’s a win for all parties and the state funds are preserved.

Benefits of Surety Reclamation

Facilitates the purposes of SMCRA in addressing the adverse effects of surface coal mining operations, protection of the environment and the rights of landowners.

Land gets stabilized; pollution gets abated using private sector resources instead of limited government resources (agency still has jurisdiction).

More actual reclamation activity can be conducted on a per dollar basis since there are no government procurement requirements in private contracts between the surety and contractors.

Surety can mitigate its loss.

Landowner gets property returned to stable status faster.

Surety is additional advocate for environmental protection in bankruptcy proceedings.

Conclusion

Addressing the many technical aspects of mine land reclamation and environmental remediation in the event of a permittee's default is complicated enough. When considered in the context of a bankruptcy with many other interested parties asserting aggressive legal positions regarding limited assets, environment compliance and liability, the matter may appear like a quagmire of legal and technical issues. The surety company must be a key player in reconciling many of the competing interests from a technical and legal perspective.

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AMERICAN BAR ASSOCIATION SECTION OF ENVIRONMENT, ENERGY, AND RESOURCES

Calendar of Section Events

Environmental Sciences V: Water Quality and Wastewater Treatment

March 23, 2006

Teleconference

Environmental Sciences VI: Site Remediation Technologies

April 6, 2006

Teleconference

Eastern Water Resources Conference

May 11, 2006

Miami, Florida

6th Biotech Roundtable: Traits Tolerances and Traceability

June 27, 2006

St. Louis, Missouri

ABA Annual Meeting

Aug. 3-8, 2006

Honolulu, Hawaii

14th Section Fall Meeting

Oct. 4-8, 2006

San Diego, California

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