July 19, 2018

Ben Owens, Division Chief
Office of Surface Mining Reclamation and Enforcement
Pittsburgh Field Division
3 Parkway Center
Pittsburgh, PA 15220

Lanny Erdos, Chief
Ohio Department of Natural Resources
Division of Mineral Resources Management
2045 Morse Road, Building H-2
Columbus, Ohio 43229-6693

RE: Citizen complaint and request for inspection and enforcement action regarding insufficient bonding for Westmoreland Coal Company’s Ohio mines participating in the RFF

To Division Chief Ben Owens and Chief Lanny Erdos:

In accordance with Sections 517(h) and 521(a) of the Surface Mining Control and Reclamation Act (“SMCRA”), Sierra Club and the Ohio Environmental Council (collectively, the “Groups”) submit the following citizen complaint and request for inspection and enforcement action regarding insufficient reclamation bonding at Westmoreland Coal Company’s coal mining operations in Ohio. Westmoreland relies on Ohio’s Reclamation Forfeiture Fund (“RFF”) to satisfy its reclamation bonding obligations. As discussed below, the Groups have reason to believe that Ohio’s RFF contains inadequate funds to cover the costs of reclamation should Westmoreland forfeit its permits, and therefore Westmoreland is conducting surface coal mining operations without sufficient reclamation bonding as required by SMCRA and the Ohio Surface Mining Act.

Westmoreland’s mines that are inadequately bonded include mines with the following permit numbers associated with its Oxford Mining Company, LLC, subsidiary: 287, 661, 796, 838, 981, 1086, 1131, 2097, 2198, 2226, 2238, 2245, 2254, 2277, 2290, 2292, 2295, 2315, 2318, 2319, 2324, 2325, 2334, 2340, 2361, 2364, 2369, 2373, 2376, 2377, 2379, 2386, 2387, 2393,
2398, 2403, 2404, 2408, 2415, 2416, 2418, 2419, 2420, 2421, 2423, 2425, 2444, 2445, 2449, 2450, 2451, 2463, 2467; Buckingham Coal Company, LLC, subsidiary: 1163, 2223, 2269, 2276, 2331; Daron Coal Company, LLC, subsidiary: 1181; Harrison Resources, LLC, subsidiary: 2289; and Oxford Conesville, LLC, subsidiary: 2414.

The Groups hereby provide notice of this complaint to both the Ohio Division of Mineral Resources Management ("DMRM") and the federal Office of Surface Mining Reclamation and Enforcement ("OSMRE"). Should the DMRM fail to take appropriate action within 10 days, the Groups request that OSMRE issue a notice of violation to Westmoreland and that the notice require Westmoreland to either post a substitute financial assurance for each of its Ohio permits or immediately cease coal removal operations and immediately commence reclamation. In addition, DMRM and OSMRE must ensure that no new permits are issued to Westmoreland that rely on the RFF to satisfy SMCRA’s bonding requirements. The groups are aware that OSMRE continues to assess the adequacy of Ohio’s SMCRA program under its Part 733 authority, but does not believe that the Part 733 process obviates the need for immediate action to address the ongoing violations at Westmoreland’s mines.

In accordance with 30 C.F.R. § 842.12(d), the Groups request that OSMRE report the results of any inspections within 10 days from the date of the inspection or, if OSMRE chooses to not conduct an inspection, to explain the reasons for that decision within 15 days from the date on which this letter is received.

This citizen complaint and request for inspection is supplementary to the complaint sent on June 18, 2018, regarding the adequacy of the RFF as a whole. By filing the present complaint the Groups are not withdrawing or otherwise abandoning the June 18, 2018, complaint.

The Ohio RFF has only $15.1 million available to cover new reclamation costs

The bedrock requirement of SMCRA is that every active coal mining operation must maintain a reclamation bond or participate in an adequately funded alternative bonding program “sufficient to assure the completion of the reclamation plan if the work had to be performed by the regulatory authority in the event of forfeiture.” 30 U.S.C. § 1259(a); S. REP. NO. 95-128, at 78 (1977) (Senate Committee on Energy and Natural Resources referring to
SMCRA’s bonding scheme as “one of the most important aspects of [a] program to regulate surface mining and reclamation.”). Congress passed SMCRA in 1977 in large part to address the problem of unreclaimed mine sites and the attendant “social and economic costs on residents in nearby and adjoining areas.” 30 U.S.C. § 1201(h).

Permittees who participate in the RFF must post a bond in the amount of $2,500 per acre of land, irrespective of actual projected reclamation costs. In the event of forfeiture, any difference between that amount and the actual cost of reclamation will be made up by the RFF.

DMRM retained Pinnacle Actuarial Resources to evaluate the solvency of the RFF. In a June 2017 report, Pinnacle calculated the “present value of potential expected liability of the Fund” to be $25,107,115.\(^1\) That liability estimate includes $5.8 million in reclamation costs at already forfeited mines, and an estimate of additional forfeitures and related costs.\(^2\) At the time of its report, Pinnacle concluded that the RFF was adequately funded because it contained $25.9 million in assets, meaning that the RFF assets exceeded the potential expected liability.\(^3\) Subtracting the $5.8 million that is already pledged to address reclamation costs at the Valley Mining forfeitures for which Ohio is already obligated,\(^4\) the RFF had only $20.1 million available to cover any new reclamation costs arising from new forfeitures.

Shortly after the Pinnacle report was finalized, Ohio transferred $5 million out of the RFF for use in the state’s general fund, with no plans or commitment to replace those funds.\(^5\) That transfer reduced the available funds in the RFF further, to approximately $15.1 million.

**Westmoreland Coal Company’s mines will cost Ohio between $33.4 million and $150 million to reclaim in the event the company forfeits its permits.**

Westmoreland has 63 permits participating in the RFF.\(^6\) Should Westmoreland become insolvent and forfeit its Ohio permits, the cost to the state could range between $33.4 million

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\(^2\) Id. at 4, 29.
\(^3\) Id. at 10.
\(^4\) Id. at 28-29.
\(^5\) Letter from Lanny Erdos, Chief, DMRM, to Ben Owens, Chief, OSMRE’s Pittsburgh Field Division, dated September 21, 2017.
\(^6\) Id. at Exhibit 7.1a.
and $150 million. Under any scenario, the cost to Ohio will exceed the $15.1 million currently available in the RFF. This would wipe out the RFF, and pass significant costs on to Ohio taxpayers.

The Pinnacle report contains exhibit 7.1a., which provides a list of the reclamation liabilities for each company participating in the RFF.\textsuperscript{7} The total “performance security estimate” for Westmoreland is listed as $150,070,000. This is the estimated total reclamation cost for all of Westmoreland’s mines, based on information from engineers with the Ohio Department of Natural Resources’ Division of Mineral Resources Management.\textsuperscript{8}

Because Westmoreland’s mining and reclamation operations are at varying stages at its individual mines, it is possible (though far from certain) that the actual reclamation costs will be lower than the total potential costs listed as the “performance security estimate.” To calculate the likely reclamation costs, it is instructive to look at the most recent bond forfeiture in Ohio. This provides an opportunity to gauge the real world costs of reclaiming forfeited permits. In 2014, Valley Mining forfeited six permits.\textsuperscript{9} The total estimated cost to the RFF of reclaiming those six permits is $5.8 million.\textsuperscript{10} This amount is above and beyond whatever has already been paid from Valley Mining’s surety bonds or other financial assurances. On a per-permit basis, this comes out to $966,667 per permit. For Westmoreland’s 63 permits, this works out to a total cost of $60,900,021. Alternatively, we can assess the per-acre cost. Valley Mining’s six mines covered a total area of 2,598 acres.\textsuperscript{11} That provides a per-acre cost of $2,244. The Pinnacle Report calculates 14,888 bond acres for all of Westmoreland’s Operations.\textsuperscript{12} The total reclamation cost for Westmoreland’s mines, based on the per-acre cost for the Valley Mining reclamation, thus comes out to $33,408,672.\textsuperscript{13}

\textsuperscript{7} Pinnacle report, Exhibit 7.1.a.
\textsuperscript{8} Id. at 13.
\textsuperscript{9} Id. at 14.
\textsuperscript{10} Id. at 29; see also ODNR’s “Forfeiture Reclamation Plan”, available at http://minerals.ohiodnr.gov/portals/minerals/pdf/bond%20forfeiture/coalforfeitures_5-yr_plan.pdf
\textsuperscript{11} ODNR’s “Forfeiture Reclamation Plan”
\textsuperscript{12} Pinnacle report, Exhibit 7.1.a.
\textsuperscript{13} The Pinnacle report provides a “net reclamation cost” figure for Westmoreland’s mines of $4,259,358. The report does not explain the factual basis for this cost estimate, nor does it provide any justification for the use of a figure that is less than 3% the “total performance security estimate.”
Even the lowest estimate for reclamation costs at Westmoreland’s mines based on actual data, therefore, is more than twice the amount currently available in the RFF. A default and forfeiture by Westmoreland would exhaust the RFF and leave Ohio’s taxpayers responsible for covering between $18.3 million and $134.9 million.

Furthermore, any new mining permits issued to Westmoreland that are allowed to rely on the RFF to satisfy SMCRA’s bonding requirements would only increase the potential burden on Ohio taxpayers. The Groups are aware that Westmoreland’s subsidiary Oxford Mining Company has applied for a new permit for a coal mine in the Perry State Forest.\(^\text{14}\) Given the RFF’s current status as significantly under-funded, and given Westmoreland’s already substantial reclamation obligations, DMRM and OSMRE must not allow Westmoreland to increase the liability for the RFF. Instead, Westmoreland must be required to post a surety bond for the full actual estimated reclamation cost before any new permit may be issued.

**Westmoreland is in severe financial distress and likely to enter bankruptcy.**

The risk of forfeiture by Westmoreland of all of its Ohio permits is not mere conjecture or speculation. Westmoreland is in significant financial distress, and has warned its investors that it may enter bankruptcy in the near future.

In its most recent Form 10-K filing with the SEC, Westmoreland stated that “We may seek protection from our creditors under Chapter 11 of the United States Bankruptcy Code (‘Chapter 11’) or an involuntary petition for bankruptcy may be filed against us.”\(^\text{15}\) Westmoreland’s stock currently trades at $0.14 a share, down 99.7% from a high of $43.59 in August 2014. Meanwhile, Westmoreland has continued to accumulate debt.\(^\text{16}\)

Westmoreland also recently announced that it is losing one of its largest customers in Ohio. In an SEC Form 8-K filing from June 21, 2018, Westmoreland stated that AEP Generation Resources Inc. “had declined its bid to supply coal to AEP’s Conesville Power Plant Units 5 and 6 after the expiration of the parties' current contract on December 31, 2018.”\(^\text{17}\)

\(^\text{14}\) https://abc6onyourside.com/on-your-side/6-on-your-side/families-and-business-owners-near-perry-state-forest-upset-over-proposed-coal-mine
\(^\text{15}\) https://www.sec.gov/Archives/edgar/data/106455/000010645518000028/wlb201710-k.htm
\(^\text{16}\) http://wyomingpublicmedia.org/post/brink-what-could-come-westmoreland-bankruptcy#stream/0
further noted that this contract represented 14% of its revenues in 2017. A recent analysis by S&P Global Market Intelligence found that Westmoreland’s “once-lauded business model for mining and selling coal continues to show signs of vulnerability in today's energy market.” The analysis noted that Westmoreland’s predominant business strategy of focusing on mines located close to the plants that purchase their coal is extremely vulnerable to market fluctuations and plant retirements because “when those customers’ need for coal falls, moving those tons elsewhere can be difficult.”

Other industry watchers have similarly identified Westmoreland’s business model as an ongoing threat to the company’s viability. In a recent Argus Media story, “Doyle Trading Consultants head of market analytics Andy Blumenfeld cited the mine-mouth model as the "number one" cause of [Westmoreland’s] financial troubles.” Those financial troubles include the fact that “six of Westmoreland’s mines may be forced to close in coming years because their primary customers are retiring, and the company already is struggling to pay down debt.”

Structural factors inherent to current energy markets will continue to doom Westmoreland’s prospects, because “[a] power market environment in which natural gas offers a cheap alternative for power generation and other operational vulnerabilities compound against Westmoreland’s financial struggle to cover upcoming debt maturities.” Indeed, a vice president and senior credit officer with Moody’s Investors Service recently stated that “Westmoreland is clearly our most distressed producer that we rate in the coal industry.”

Although a bankruptcy filing, by itself, would not automatically cause Westmoreland to forfeit its bonds, current market conditions could make it very difficult for Westmoreland to emerge from bankruptcy. As the market for coal continues to shrink, and as investors continue to highlight the particular vulnerabilities in Westmoreland’s business model, Westmoreland

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18 Id.
20 Id.
22 Id.
23 Id.
24 Id.
could have significant difficulty renegotiating its debt or securing the additional financing necessary to allow it to reorganize. The alternative will be for Westmoreland to liquidate, which would have the immediate effect of forfeiting each of its permits and passing the reclamation costs on to the RFF and—once the RFF is exhausted—to Ohio’s taxpayers.

**Conclusion and request for enforcement**

Westmoreland is at extreme risk of forfeiting its permits given its precarious financial position. Even the most conservative estimate of the reclamation liability that Westmoreland would pass on to Ohio in the event of forfeiture—$33.4 million—dwarfs the funds currently available for reclamation in the RFF—$15.1 million. The combination of Westmoreland’s imminent bankruptcy, the high reclamation costs associated with its Ohio mines, and the under-funded nature of the RFF make clear that the current bonding approach for Westmoreland’s Ohio mines fails to satisfy the SMCRA requirement that bonding be “sufficient to assure the completion of the reclamation plan if the work had to be performed by the regulatory authority in the event of forfeiture.” 30 U.S.C. § 1259(a).

Ohio and OSMRE must therefore (1) require Westmoreland to post additional surety bonds to reduce Ohio’s potential share of reclamation costs to below $15.1 million; (2) ensure that the amount of funds in the RFF is immediately increased to a level adequate to cover Ohio’s share of reclamation costs in the event Westmoreland forfeits its bonds; or (3) require Westmoreland to cease all coal mining in Ohio and immediately conduct reclamation operations. In addition, Westmoreland must not be allowed to rely on the RFF to secure any new mining permits or mine permit expansions. This includes the new proposed mine in the Perry State Forest. Instead, Westmoreland must be required to provide surety bonds for the full cost of reclamation for any new permits or permit expansions.

We look forward to your response to this citizen complaint and request for inspection and enforcement action.

Sincerely,

Peter Morgan
Senior Attorney
Sierra Club, Environmental Law Program
1536 Wynkoop St., Ste 200
Denver, CO 80202
303-454-3367
peter.morgan@sierraclub.org

On behalf of Sierra Club and the Ohio Environmental Council
Attachment 1:

S&P Global Market Intelligence, “Loss of large coal contract only latest challenge to hit struggling Westmoreland,” June 25, 2018
Loss of large coal contract only latest challenge to hit struggling Westmoreland

Monday, June 25, 2018 10:55 AM MT

By Taylor Kuykendall

Westmoreland Coal Co.'s once-lauded business model for mining and selling coal continues to show signs of vulnerability in today's energy market.

The company disclosed June 22 that the largest customer for its Buckingham mine in Ohio will not renew its contract for coal for a nearby power plant after it expires December 31 of this year. The company's low-cost business model, with mines often located near the plants that use its coal, was once viewed favorably. However, low natural gas prices and a shrinking coal fleet have led to plenty of low-cost competition on the market, exposing vulnerabilities in the strategy.

"Westmoreland has shown the minemouth model is not without risks," said Joe Aldina, director of U.S. coal at PIRA Energy Group, an analytics and forecasting unit of S&P Global Platts. "They always said their counterparties were top credit-rated utilities and things like that, but if the plants they serve are being retired, they have few options because their mines don't have the option to serve the broader market."

American Electric Power Co. Inc. told S&P Global Market Intelligence it found another supplier and currently has no plans to retire the Conesville plant. The contract represented about 14% of the consolidated revenues of Westmoreland's master limited partnership, Westmoreland Resource Partners LP.

The company has touted its long-term contracts with nearby customers, but when those customers' need for coal falls, moving those tons elsewhere can be difficult. The company has said it typically enters into long-term, cost-protected supply contracts ranging from one year up to fifteen years.

"The close proximity of our mines and coal reserves to our customers reduces transportation costs and, we believe, provides us with a significant competitive advantage with respect to retention of those customers," Westmoreland Coal wrote in its most recent annual securities filing. "Most of our mines are in very close proximity to the customer's property, with economical delivery methods that include, in several cases, conveyor belt delivery systems linked to the customer's facilities."

S&P Global Ratings noted last fall that the expected termination of three coal contracts in accounted for about 17% of the company's 2016 production volume.

"Another contract expiring is not positive," S&P Global Ratings analyst Vania Dimova said in a June 22 interview. "The trend is not positive."

A power market environment in which natural gas offers a cheap alternative for power generation and other operational vulnerabilities compound against Westmoreland's financial struggle to cover upcoming debt maturities, Dimova added. Westmoreland Coal was recently downgraded by S&P Global Ratings over the "virtual certainty" of a default by the master limited partnership.

While lenders have shown willingness to work with Westmoreland, mounting challenges do leave open the possibility that a bankruptcy court restructuring could be on the horizon, said Benjamin Nelson, a vice president and senior credit officer with Moody's Investors Service. The company recently secured a new financing commitment in the form of a $110 million delayed draw term loan from an ad hoc group of its existing secured creditors. The loan could be converted into a post-petition financing package if it decides to seek Chapter 11 bankruptcy.

"Westmoreland is clearly our most distressed producer that we rate in the coal industry," Nelson said in an interview. "The biggest question is what do they do with their balance sheet and when?"
In 2015, an analyst with BMO Capital Markets said it was a "perfectly legitimate" question to ask if anything in coal was investable anymore. Westmoreland was held up as a different kind of company and likely to succeed, though now the same company finds itself struggling as much of the sector is seeing improvement.

"There's a few that are very lowly rated like Westmoreland that are on the distressed end," Nelson said of rated coal companies, noting Moody's has a stable view of the sector overall. "The others are doing better this year than last. A lot of what's driving that is some stability in thermal coal including increased stability of export as well higher [metallurgical] coal prices, so cash flow generation, probably for the coal industry should be a little bit better this year."

Representatives of Westmoreland did not respond to a request for comment.

This S&P Global Market Intelligence news article may contain information about credit ratings issued by S&P Global Ratings, a separately managed division of S&P Global. Descriptions in this news article were not prepared by S&P Global Ratings. The original S&P Global Ratings documents referred to in this news brief can be found here. S&P Global Market Intelligence and S&P Global Platts are owned by S&P Global Inc.