Frac Sand Sentinel

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This morning at the Chippewa County's Land Conservation and Forestry Department's monthly meeting, Johnne Smalley gave this presentation to the Committee members and attendees. She agreed to share it with you.

An excellent presentation!

She also shared some additional information on reclamation and bonding which you will find at the end of this newsletter.

My name is Johnne Smalley. I own and pay taxes on land in Wheaton Township in Chippewa County.

I am here today to find out what Chippewa County envisions for its future.

I have read Chippewa County's Comprehensive Plan, but I don't see the county following it. Page 173, Section 6.4 states:

Goal 1 - Maintain the physical condition, biodiversity, ecology, and environmental functions of the landscape, including its capacity for flood storage, groundwater recharge, water filtration, plant growth, ecological diversity, wildlife habitat, and carbon sequestration.

Goal 2 - Maintain the capacity of the land to support productive forests and agricultural working lands to sustain food, fiber, and renewable energy production.

How many acres of land have been removed from productive forests and agricultural working lands to support frac sand mines owned by and operated for the financial benefit of people that are not from our area, often not even from our state, and sometimes, not even from our country? How have all these frac sand mines maintained the physical condition, biodiversity, ecology, and environmental functions of the landscape, including its capacity for flood storage, groundwater recharge, water filtration, plant growth, ecological diversity, wildlife habitat, and carbon sequestration? What I'm seeing is a bunch of eyesores scarring our land, devastation of forested hillsides, businesses that were dependent on tourist trade closing, increased costs for agricultural businesses dependent on rail transport of fertilizers into the area and corn out of the area, decreased wildlife habitat resulting in increased crop destruction as the wildlife relocate into adjacent cropland, and tons of colloidal clay from their ponds washing into our trout streams and ruining the trout habitat. There are toxic levels of silica 2.5 dust in the air which affect our health and probably animal health. In other localities near frac sand facilities, veterinarians have noticed increased fertility problems including a significant lower conception rate and higher rate of stillborn and weak calves. There have been similar reports by farmers near mine sites in Chippewa County. Coincidence?

I'm also seeing a tremendous increase in the number of homes for sale around these sites and at greatly reduced prices. Some people have given up and just walked away from their home to move elsewhere.

Now I am seeing the approval of another reclamation permit for a 1300+ acre frac sand mine, processing plant, and trans-load station. This permit has been granted to a company with a known history of disregarding DNR regulations that protect our groundwater from contamination.

I have also read a good bit of The Chippewa County Code of Ordinances.

The Chippewa County Code of Ordinances Chapter 30, Sec. 106 lines 741-744 states:

"Sec. 30-106. Permit denial. An application for a nonmetallic mining reclamation permit shall be denied if any of the factors specified in Wis. Admin. Code NR § 135.22 exist.

NR 135.22 Denial of application for reclamation permit, clearly states, "An application to issue a nonmetallic mining reclamation permit *shall* be denied if

(c) 1. The applicant, or its agent, principal or predecessor has, during the course of nonmetallic mining in Wisconsin within 10 years of the permit application or modification request being considered shown a pattern of serious violations of this chapter or of federal, state or local environmental laws related to nonmetallic mining reclamation."

Northern Sands, LLC has more than 20 DNR violations of inappropriate exploratory borehole abandonments in Chippewa County. Leaving holes open can create a direct conduit for entry of contaminants to waters of the state and is a *serious* violation of ch. 281, Wisconsin Statutes and ch. NR812, Wis. Adm. Code. (Just

ask anyone who has to drink water from an aquifer that has had liquid manure dumped down a hole into it).

The proposed post−mining land use given in 3.0 of the Howard Township Properties Nonmetallic Mine Reclamation Plan "include a combination of commercial and passive recreational uses....Approximately eighty-five percent of the site will be reclaimed as prairie grasslands: approximately fifteen percent of the area will be reclaimed as woodland." The Chippewa County Land Conservation and Forest Management staff can explain better than I can that prairie grasslands are not the same as productive agricultural cropland that sustain food, fiber, and renewable energy production. (See goal 2 from Chippewa County's Comprehensive Plan as quoted above.)

NR 135 also states, "The proposed post−mining land use shall be consistent with local land use plans." In addition, State law Sec. 66.1001. Wis. Stats. requires that local land use-related decisions be consistent with the goals and objectives of that community's comprehensive plan. I am not seeing how taking more and more productive cropland and forest away to return it to native prairie "maintains the capacity of the land to support productive forests and agricultural working lands to sustain food, fiber, and renewable energy production".

I would also like to question why Chippewa County is not requiring an independent expert or consultant to do the monitoring and reporting of this mine site with reimbursement costs paid back to the county by Northern Sands. This permit allows Northern Sands to do their own checking and reporting. Their history has shown how well they have done that in the past. On multiple occasions, their actions and reports have been fabricated and falsely reported to both the Howard Town Board and the Wisconsin DNR. Having county personnel or even state personnel checking to make sure the monitoring and reporting is being done accurately is just adding to the taxpayers' burden. With Northern Sands history, they will need close oversight and this cost should fall back onto Northern Sands—not the taxpayers.

An agency-designated consultant with recognized experience in the areas of financial assurance and reclamation should also be required to evaluate any financial assurance given by Northern Sands with the costs incurred paid by Northern Sands. Reclamation Surety Bonds for other mining

endeavors have proved inadequate in the past. Repeatedly, the Surety Bonds have been for inadequate amounts. They may cover the cost of reclamation as outlined, but usually fail to cover any problems that may occur—especially the cost of re-working an area where reclamation failed and the cost of pollution clean-up. Also, there is a history of Surety Bond issuers failing when it comes time for the actual reclamation. In some instances there has been a close tie between the surety bond company and the mine owner.

In conclusion, I would like to repeat my question of how the Chippewa County envisions its future and how its actions in permitting these frac sand mines support this vision.

Thank you.

Johnne added some additional comments regarding her research. She says she has other materials she would be willing to share if there is someone concerned about the financial aspects of reclamation.

in researching the problems associated with Reclamation Surety Bonds, I have found:

a Most reliable Surety Bond companies do not do surety bonds for reclamation. The nature of what surety bonds do and what reclamation is make them incompatible. A Surety bond is for a set period of time,while reclamation will not be completed until some unknown date in the future.

b The companies that do provide Surety Bonds for reclamation are often not reliable. Past history has shown that they

will provide a bond for a set period of time both initially and with each renewal, but refuse renewal when actual reclamation is near at which time they may disappear, dissolve, or declare bankruptcy.

c The Bureau of Land Management no longer considers Surety Bonds an adequate source of financial assurance for reclamation of mines permitted by them.

d Most Surety Bonds are for inadequate amounts. They only consider the cost of reclamation if everything goes well. They do not cover the cost of any reclamation failure. Reclamation failures have in the past bankrupted many companies providing the bond. This is one of the major reasons why many local, state and federal governments no longer consider surety bonds an adequate form of financial assurance for reclamation.

I will give website information to different documentation describing the problems with reclamation surety bonds from state regulators', surety bond industry's, mining association, and lawyers' points of view. A few key points, I will list below.

According to David Ganje of Ganje Law Offices in Rapid City (practicing in the area of natural resources, environmental and commercial law) in http://www.lexenergy.net/south-dakotas-first-in-situ-leach-uranium-mining-project/

"My concern with any large natural resource project is the risk of socializing the expense of any possible environmental cleanup as a cost paid by the taxpayer. "Superfund" is a federal environmental law under which the government supervises cleanup of contaminated mining and industrial sites. The polluter is financially responsible for the cleanup. However about 30 percent of Superfund sites are orphaned sites where no responsible party is available to pay for cleanup. Without adequate financial assurance terms in place by a mine operator to pay for a possible cleanup, the taxpayer may have to step in to pay.

A mine operator's financial capacity comes into play in the matter of abandoned mines, orphaned mines, spills, costs of water reclamation,

decontamination and closure or decommissioning of a mine. Many mine operators address financial assurance requirement by using surety bonds. A surety bond is an insurance company's guarantee of an applicant's performance under a permit. An applicant must prove adequate financial resources for reclamation, spills and final closure. Nevertheless several mining operations in the US have been closed with unresolved environmental and groundwater issues exceeding the costs of the financial assurances posted for the operation."

According to Kellan McLemore, Staff Attorney, Midwest Environmental Advocates, "There is already a history in Wisconsin of mining companies bailing on their reclamation commitments prior to completion of reclamation."

According to "Mine Reclamation Bonding – from Dilemma to Crisis to Reinvention: What's a State Regulator to Do?" Presented by Gregory E. Conrad Executive Director Interstate Mining Compact Commission Before the Energy and

Mineral Law Foundation Winter Workshop on Energy Law February 11, 2014 http://www.imcc.isa.us/EMLF%20Bonding%20Presentation%20Final.pdf

"traditional surety bonds, or similar instruments, were never designed for long-term reclamation obligations like water treatment but instead were focused on shorter term and very defined obligations that had a high certainty for eventual release following the completion of reclamation (generally based on success of revegetation of the site). Ordinarily, bonding underwriters will not provide a surety bond if it is determined that a site will have long-term pollutional discharges since the bond will likely never be released – an outcome that a bonding company will do its best to avoid. This is largely because reclamation bonds, unlike insurance, are intended to function primarily as credit transactions or accommodations in which the surety anticipates no loss."

And

"Over the course of the past 35 years since the enactment of the Surface Mining Control and Reclamation Act of 1977 (SMCRA)[2], bonding (or financial assurance)[3] programs related to the reclamation of coal mining operations have undergone a series of adjustments that reflect the changing nature of both the coal and surety industries. Some changes have involved small refinements; others represent new, innovative approaches that were not on anyone's radar screen in the early days of SMCRA's implementation. In many respects, the bonding program under SMCRA has served as a microcosm of the larger financial and economic challenges faced by the country as a whole, beginning with the "bonding dilemma" of the mid-90's when bankrupt surety companies and under-funded bond pools caused great concern, to the "bonding crisis" of the early 2000's as the surety and insurance industries responded to the significant losses associated with 9/11 and catastrophic weather events, to the "bonding challenges" that we face today as a result of corporate restructuring and unanticipated environmental conditions and priorities, especially related to water quality and long-term treatment scenarios. ... There are a variety of

other issues that the states are currently working through in the bonding arena and many of these were discussed at three recent workshops that IMCC hosted for state regulatory authorities. Beyond those mentioned above, states are also focused on bond forfeitures, especially those associated with bankruptcies and the potential for alternative enforcement; tracking letters of credit as a result of bank mergers and closures; difficulties associated with updating and increasing bond amounts; the expense associated with full cost bonding; insufficient funds following bond forfeitures; and the increasing complexity of administering a bonding program, especially with regard to risk analysis."

Gregory Conrad states, "Representing as I do the states that regulate the mining industry, my views are admittedly from the perspective of a state government agency, whose primary interest is to ensure that the state will have sufficient funds to complete the reclamation should the operator default and to thereby protect the citizens and taxpayers of the state from being saddled with unfunded liabilities. It is this same interest that has motivated several federal government agencies to develop or propose robust financial

assurance programs where mineral extraction is concerned, including the Bureau of Land Management[9], the U.S. Forest Service and the U.S. Environmental Protection Agency."

According to RECLAMATION BONDS FROM THE SURETY PERSPECTIVE Presented By William T. Gorton III, Esq., (https://www.bestlawyers.com/Downloads/Articles/2267_1.pdf)

"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. ... Until the recent surge in coal prices, numerous companies with large coal mine environmental obligations have been dissolved or become bankrupt in the last ten 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." ... 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 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.

According to http://corporate.findlaw.com/business-operations/mining-and-the-vanishing-surety-bond-market.html

Financial Distress in the Surety Industry

"In the congressional hearings during the summer of 2002, the president of the Surety Association of America (SAA), Lynn Schubert, testified that a report released by SAA in May 2002 provides evidence of the potentially devastating conditions facing the surety bond industry.... These problems have been accompanied by a shrinking supply of surety companies due to mergers, bankruptcies, and unilateral decisions by surety providers to leave the business. According to one source, the availability of surety is constrained due to the presence of fewer surety companies than in the past. Reportedly, five of the twelve largest surety providers were acquired or exited the business between 1998 and 2001. The

impacts of the recent events on surety providers similarly have affected the reinsurance market. In order to limit financial exposure, surety companies historically have entered into agreements with reinsurance providers. For example, a surety company may contractually agree to be liable for a percentage or predetermined amount of the bond liability with any additional amounts covered by the reinsurer. If the bond is forfeited, the reinsurer is typically liable for the agreed upon dollar amount to the surety provider and not to the beneficiary of the bond. ... the unique circumstances related to the extractive industry have curtailed dramatically the availability of sureties for mining companies now as compared to the 1990s. In particular, the mining industry's ability to obtain financial guarantees is directly affected by the duration of the surety commitment, the downturn in the market for minerals, recent regulatory changes, and the changing surety industry.

First, in contrast to most non-mining projects, the obligations related to mining reclamation often are of indefinite duration and can extend for decades or longer. Regulators increasingly have responded to this long-term exposure to risk by a

wariness to release any portion of a surety as reclamation is performed. Delay in bond release provides further evidence to surety companies that the duration of risk is highly uncertain, and thus makes them less willing to provide new or increased surety to the mining industry."

http://faculty.lawrence.edu/gerardd/wp-content/uploads/sites/9/2014/02/22-RP-Gerard-bonding.pdf

Abstract:

It is becoming a standard practice for governments to require mining operations to post reclamation bonds. Yet, there have been few theoretical treatments examining the rationale for bonding mechanisms, and even fewer empirical treatments of the effectiveness of bonding. This paper addresses some of these holes in the literature. It begins by examining the rationale underlying reclamation bonds, and discusses the strengths and weaknesses of bonding as a tool for enforcing reclamation requirements. The role of bonding mechanisms is to help enforce standards, not necessarily yield efficient

outcomes, and these mechanisms are best viewed as a complement to — not a substitute for — liability rules. The paper also examines the effectiveness of bonding by drawing on evidence from hardrock mining on public lands in the western United States.

Problems with bonding mechanisms.

There are several problems associated with bonding mechanisms that limit their applicability (Shogren et al., 1993). First and foremost, bonding is not free — the firm, the regulator, and the surety each incur transaction costs. These transaction costs increase as uncertainty increases or as contracting becomes more complex, as complex contracts are costly to write, interpret, and enforce. For instance, a contract that specifies that “reasonable efforts must be taken to reclaim the site” would be likely to be much more difficult to enforce than one that specified bright-line rules for reclaiming drill holes, roads, processing facilities, and the like. As

contracting becomes more costly, the effectiveness of the bonding mechanism decreases. Uncertainty is also a primary impediment to the smooth operations of liability rules. Therefore, it is unlikely that the bonding mechanism will be an effective substitute for liability rules. A second problem is that bonds can impose liquidity constraints on firms. Cash, treasury bonds, certificates of deposit, and other liquid assets are often acceptable forms of collateral, but these instruments can tie up a firm's operating capital. This liquidity constraint becomes more binding as the deposit amount increases. One way to mitigate the liquidity constraint is by involving a third party, for instance, a surety. For a fee, a surety agrees to cover the amount of the bond if the agent fails to fulfill its obligation, which also transfers a portion of the default risk from the public to the surety provider (there is not necessarily a transfer of funds that the landowner holds in trust; instead, the surety assumes a legal obligation to provide funds if the firm reneges on its agreement). The use of a surety reduces, but does not eliminate, liquidity constraints. The firm must pay an annual premium, and the bond amount is also a liability on the firm's balance sheet that adversely affects

the firm's credit. Although collateral reduces the firm's moral hazard, it also introduces moral hazard on the side of the regulator. A wealth-maximizing regulator may have the incentive to retain the bond whether or not reclamation is performed. This is a potentially serious defect of the bonding mechanism. If, however, the operating permit specifies reclamation requirements that can be verified by a third-party at a low cost, the firm should be able to successfully challenge the regulator's decision. Moreover, it would be difficult for a state with a poor reputation to attract capital to its jurisdiction, and surety pro- viders would be less likely to underwrite contracts for operations within that state.

Based on past history of mining reclamation and the problems state and federal agencies have reported with surety bonds, I question whether Chippewa County has the staff resources to conduct adequate review of financial assurance issues? NRC (Nuclear Regulatory Commission) officials told us that their staff resources are limited and that they lack the financial expertise to

evaluate compliance with investment restrictions. . .The federal watchdog agency General Accountability Office (GAO) expressed concern over the BLM and NRC's ability to determine the costs of reclamation. At the very least, I would like to suggest that Chippewa County follows the advice of David Ganje of Ganje Law Offices in Rapid City (practicing in the area of natural resources, environmental and commercial law).

Whether the financial assurance is in the form of a surety bond, escrow account or any other form, the agency with designated authority over an applicant's financial assurance requirements shall evaluate in writing all financial assurance documentation using an agency-designated non-party (Consultant) with recognized experience in the areas of financial assurance. This designation shall be a condition of any permit or license. The costs incurred by the agency in contracting with the Consultant shall be paid by the applicant.

If any of this information can be used by anyone else in the battle against frac sand mines, please feel free to use it. I also have a copy of a 2005 Consent Order and Agreement showing that a regulated surety company had $500,000 less cash available than the $4.3M in reclamation guarantees it had written for a mine operator where the surety company was closely affiliated with the mine operator. This is not a normal reason for surety bond failures but it does show that this does happen.

Hope this is useful.

Johnne Smalley

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Welcome to the Frac Sand Sentinel, a newsletter highlighting resource links, news media accounts, blog posts, correspondence, observations and opinions gathered regarding local actions on, and impacts of, the developing frac sand mining and processing industries.

CHECK OUT THE WEBSITE: WWW.CCC-WIS.COM for additional information