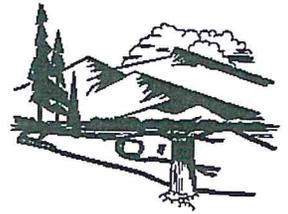




Department of Environmental Quality

To protect, conserve and enhance the quality of Wyoming's environment for the benefit of current and future generations.

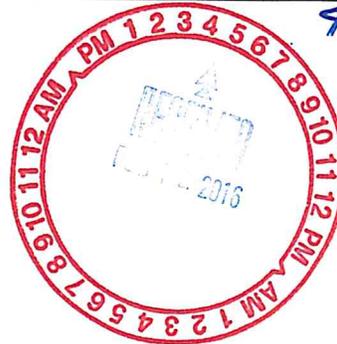


Matthew H. Mead, Governor



Todd Parfitt, Director

February 12, 2016



4:29 pm

Hand Delivered

Jeffrey Fleischman
Chief, Denver Field Division
150 East B St. RM 1018
Casper, WY 82601

RE: Ten Day Notice related to Alpha Natural Resources, Inc., Alpha Coal West, Inc.

Dear Mr. Fleischman,

On January 21, 2016, you sent the Wyoming Department of Environmental Quality (DEQ) a ten-day notice (TDN) related to the Wyoming operations of Alpha Natural Resources, Inc., and Alpha Coal West, Inc. (collectively Alpha). In that correspondence you stated that the Office of Surface Mining Reclamation and Enforcement (OSMRE)

has reason to believe that Alpha Coal may be in violation of Wyoming Land Quality Division Coal Rules and Regulations found at Chapter 12, Section 2(b) (Bonding and Insurance Procedures) because it may have allowed the bond amount to fall below the amount necessary to assure that the operator will faithfully perform all requirements of the Wyoming Environmental Quality Act and will comply with all rules and regulations and any provisions of the approved permit.

(TDN at 1-2).

In response, DEQ will show that it has taken a number of appropriate actions authorized under Wyoming's program to correct the violation alleged by OSMRE. All of these actions were taken after informing and consulting with OSMRE and its attorneys. DEQ's actions have ensured that the public has not incurred one dollar in reclamation liability for Alpha's operations in Wyoming. At the same time, not one miner has been put out of work as a result of DEQ's actions. Reclamation continues at both mines on schedule and there has been no harm to the environment, public health, or public safety. Nor will there be any harm because of Alpha's ongoing bankruptcy as DEQ retains the right to take all appropriate enforcement action against the company. Wyoming received substantial

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additional security for Alpha's reclamation obligations in the bankruptcy proceedings and a commitment that upon exiting the bankruptcy Alpha will post substitute bonds sufficient to cover the full amount of its reclamation obligations in Wyoming. These substantial steps towards full compliance are appropriate "other actions" and establish "good cause," and therefore, OSMRE should find that no further action on the TDN is necessary or appropriate.

BACKGROUND

In November of 2014, DEQ renewed Alpha's self-bonds for the Belle Ayr and Eagle Butte mines based on the audited 2013 fiscal year-end financial statements. DEQ also required Alpha to submit its audited 2014 fiscal year-end financial statements upon their completion. Alpha provided those financial statements to DEQ on March 12, 2015.

After reviewing those statements, DEQ sent Alpha a letter on April 20, 2015, notifying the company that it may no longer satisfy the financial solvency requirements set forth in Chapter 11 of DEQ's rules. DEQ requested that Alpha provide additional information within 30 days. The following day Alpha requested a copy of the Land Quality Division's calculations related to Alpha's continuing eligibility for self-bonding, and DEQ provided those calculations the same day.

On May 13, 2015, Alpha provided DEQ with unaudited financial statements for the first quarter of 2015. Two days later, representatives from Alpha met with staff from DEQ's Land Quality Division to discuss DEQ's interpretation of the rules related to self-bonding. On May 20, 2015, Alpha provided DEQ with additional information related to its current financial condition. Representatives from Alpha and DEQ held a telephone conference on May 21, 2015, to discuss again Alpha's eligibility for self-bonding.

On May 26, 2015, DEQ notified Alpha by letter that after carefully reviewing all of the information Alpha had provided DEQ determined that Alpha Coal West, Inc., and Alpha Natural Resources, Inc., no longer qualify under the self-bonding program. DEQ required Alpha to substitute its existing self-bonds with corporate sureties licensed to do business in the State of Wyoming, cash, governmental securities, federally insured certificates of deposit, or irrevocable letters of credit within 90 days pursuant to Chapter 11, Sections 5(a) and (b) of the Land Quality Division rules for surface coal mining operations.

On June 9, 2015, Alpha sent a letter to Director Parfitt requesting an informal conference with him pursuant to Wyo. Stat. Ann. § 35-11-110 for the purpose of reviewing the May 26, 2015 substitution demand. Alpha then filed a Petition for Review of Agency

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Action challenging the substitution demand on June 24, 2015, in the District Court for the Sixth Judicial District in Campbell County, Wyoming. Shortly after Alpha filed its appeal, Director Parfitt granted Alpha's request for an informal conference. In light of the fact that the informal conference could negate the appeal in state court, Alpha requested that the court stay the appeal until the conclusion of the informal conference. DEQ did not oppose this request to allow the administrative proceedings to reach their natural conclusion before litigating the same issues raised in the appeal. The court granted the stay on July 29, 2015.

On August 3, 2015, Alpha filed a voluntary petition for relief under chapter 11 of title 11 of the United States Code in the United States Bankruptcy Court for the Eastern District of Virginia. Prior to Alpha's filing in the bankruptcy court, over the summer of 2015, DEQ staff attempted to reach out to OSMRE staff on multiple occasions for guidance on self-bonding in general and Alpha in particular. These attempts to work collaboratively with OSMRE were generally unsuccessful, and on August 27, 2015, OSMRE staff informed Kimber Wichmann from the Land Quality Division that in light of the litigation between Wyoming and Alpha in the bankruptcy proceedings OSMRE could not supply any guidance to DEQ regarding self-bonding issues.

In spite of the bankruptcy proceedings, DEQ attempted to schedule the informal conference Alpha had requested. Because Alpha had not attempted to schedule the informal conference for over a month, Director Parfitt wrote counsel for Alpha on August 25, 2015, to set the date for the informal conference. Due to scheduling conflicts for both Director Parfitt and Alpha, the informal conference was not set immediately.

Soon after Alpha filed its petition with the bankruptcy court, DEQ and Alpha began negotiations to address the pending substitution demand, although the demand had been temporarily stayed by the state court in Wyoming. The result of these discussions was a proposed stipulation and order to be filed with the bankruptcy court. During the negotiations, DEQ informed OSMRE of the status of its negotiations with Alpha, and provided drafts of the proposed stipulation and order to OSMRE and its attorneys. Counsel for OSMRE suggested revisions to the document, and these suggestions were generally incorporated into the final agreement between DEQ and Alpha.

After significant negotiations, Alpha filed a motion with the bankruptcy court requesting that the court enter the stipulation and order concerning reclamation bonding for Alpha's surface coal mining operations in Wyoming. As set forth in that motion, Alpha and DEQ strongly disagreed whether the automatic stay barred DEQ from enforcing the substitution demand. *See In re Alpha Nat. Res., Inc.*, Doc. 379 at ¶ 15 (Bankr. D. Va. 2015). To settle this serious dispute and put Alpha on a path towards compliance, DEQ and the State of Wyoming stipulated to the entry of the order pursuant to the authority vested in

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the administrator of the Land Quality Division in Wyo. Stat. Ann. § 35-11-701(c). Although it had ample opportunity to do so, OSMRE did not object to Alpha's motion.

The order provides that for the duration of the bankruptcy proceedings, Alpha may satisfy its bonding requirements in Wyoming without complying with the substitution demand. *In re Alpha Nat. Res.*, Doc. 628 at ¶ 1. In addition to its claim for the full amount of Alpha's reclamation obligation should it become due as specified in the order, Wyoming was granted a superpriority claim for \$61 million dollars. Wyoming was precluded from seeking additional collateral or revoking, terminating, refusing to grant, amending, or taking any other adverse action with respect to Alpha's mining permits on account of Alpha's failure to comply with the substitution demand. *Id.* at ¶ 2. And any proceedings relating to the substitution demand or Alpha's self-bonding status were stayed by the order of the bankruptcy court, including the still pending informal conference. *Id.* Alpha was ordered to comply with all its reclamation obligations, and Wyoming was authorized to take any necessary regulatory action to ensure that these obligations are met. *Id.* at ¶¶ 3-4. Upon confirmation of the plan of reorganization Alpha, or the successor to its Wyoming mining operations, must satisfy Wyoming's bonding requirements, or DEQ will immediately issue an appropriate notice of violation and order.

Thus, Alpha remains liable under the existing self-bond, indemnity, and corporate guarantee agreements, as further secured by the settlement agreement, for the entirety of its reclamation obligations in Wyoming. Consequently, WDEQ has not "allowed the bond amount to fall below the amount necessary" to ensure Alpha's compliance as alleged in the TDN. Any notion that Alpha continues to mine without a bond or with a bond that is limited to the \$61 million superpriority claim is incorrect.

Because the bankruptcy court stayed all proceedings related to Alpha's self-bonding status, DEQ cancelled the informal conference, and Alpha and DEQ informed the state court of the stay.

Subsequently, Alpha reached a similar agreement with the State of West Virginia and the West Virginia Department of Environmental Protection. *See In re Alpha Nat. Res.*, Doc. 1049. Although styled in part as a consent order and lacking a similar stay provision, West Virginia, like Wyoming, accepted additional security from Alpha in the bankruptcy proceedings to temporarily satisfy Alpha's bonding obligations in that state and placed Alpha on a similar path towards compliance.

Several environmental groups challenged that order on the grounds that it violated West Virginia law. In resolving the challenge, the bankruptcy court issued a ruling of significant applicability to the TDN issued to Wyoming. There the court found:

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... DEP did not violate West Virginia law when it entered into the West Virginia Settlement. West Virginia law clearly permitted DEP to negotiate a compromise and enter into a consent agreement following initiation of the enforcement action. See W. Va. Code. R. § 38-2-20.40.j (authorizing DEP to enter into a settlement “at any point in the enforcement process following the issuance of a notice of violation, a cessation order, or a show cause order”).

Id. Doc. 1332 at 15. In addition, the bankruptcy court found:

[T]hat the West Virginia Settlement represents a fair and equitable deal for all parties, and is well above the lowest point of reasonableness. Absent the West Virginia settlement, the Debtors and the state of West Virginia would have become embroiled in time consuming, expensive, and distracting litigation over whether West Virginia’s substitution demand violated the automatic stay. The Debtors have admitted that this litigation would be “hotly contested.” The Debtor’s likelihood of success in such litigation is hardly assured, given the regulatory and police power exception to the automatic stay. *See* 11 U.S.C. § 362(b)(4). If the Debtors were to lose the litigation with West Virginia, they would be required to immediately post over \$244 million in substitute bonds in order to continue mining in West Virginia. Given the Debtor’s limited liquidity, this could be a substantial hurdle that could impair the Debtor’s reorganization efforts. The West Virginia Settlement avoids such a result and allows the Debtors to gradually transition away from the self-bonding program while still upholding their reclamation obligations to the state of West Virginia. The Court is convinced that this agreement will best preserve the value of the Debtor’s bankruptcy estates, maximize the return to creditors, help preserve jobs, and give the Debtor’s the opportunity to reorganize their business affairs. Indeed, the Environmental Parties do not dispute that this settlement results in a substantial benefit to the Debtors and to the State of West Virginia.

Id. at 13. The settlement of the “hotly contested” dispute between Wyoming and Alpha is similarly fair, equitable, reasonable, and authorized by Wyoming law.

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OSMRE'S LIMITED AUTHORITY

The Surface Mining Reclamation and Control Act of 1977 (SMCRA), struck “a balance between protection of the environment and agricultural productivity and the Nation’s need for coal as an essential source of energy.” 30 U.S.C. § 1202(f). In enacting SMCRA, Congress found it “essential to the national interest to insure the existence of an expanding and economically healthy underground coal mining industry,” and also provided that “the primary governmental responsibility for developing, authorizing, issuing, and enforcing regulations for surface mining and reclamation operations . . . should rest with the States.” 30 U.S.C. § 1201(f). To achieve this goal, the statute established “a program of cooperative federalism that allows the States, within limits established by federal minimum standards, to enact and administer their own regulatory programs, structured to meet their own particular needs.” *Hodel v. Va. Surface Mining & Reclamation Ass’n*, 452 U.S. 264, 289 (1981).

SMCRA adopted a two-step approach. First, the Secretary of the Interior was required to implement a federal regulatory program setting minimum standards for surface coal-mining operations within six months of August 3, 1977. 30 U.S.C. § 1252(e). Second, the states were authorized to propose and receive approval for their own individual programs. 30 U.S.C. § 1253. The Secretary introduced an initial regulatory program on December 17, 1977. 42 Fed. Reg. 62639. Wyoming received approval to implement its own program effective November 26, 1980. 30 C.F.R. § 950.10.

States with approved regulatory programs exercise exclusive jurisdiction over surface coal-mining operations, while the Secretary exercises exclusive jurisdiction in States with federal plans. 30 U.S.C. §§ 1253(a), 1254(a). A State with an approved program maintains exclusive authority except in certain limited situations, such as if the State fails to enforce its program. 30 U.S.C. § 1271. As the Fourth Circuit has noted, “SMCRA provides for *either* State regulation of surface coal mining within its borders *or* federal regulation, but not both.” *Bragg v. West Virginia Coal Ass’n*, 248 F.3d 275, 289 (4th Cir. 2001) (emphasis in original). “Under this arrangement, . . . the Secretary retains a limited and ordered federal oversight role to ensure that the minimum requirements of SMCRA are being satisfied[.]” *Pennsylvania Fed’n of Sportsmen’s Clubs, Inc. v. Hess*, 297 F.3d 310, 317 (3d Cir. 2002) (internal citation omitted).

OSMRE’s oversight authority is authorized and limited by 30 U.S.C. § 1271. Subsection (a) of that statute addresses individual violations by a specific permittee, and authorizes OSMRE to issue a notice to a state regulatory authority if it “has reason to believe that any person is in violation of any requirement of this chapter or any permit condition required by this chapter.” 30 U.S.C. § 1271(a)(1). Once such a notice is issued,

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the state regulatory authority has ten days “to take appropriate action to cause said violation to be corrected or to show good cause for such failure[.]” *Id.*

Appropriate action under 30 U.S.C. § 1271(a)(1) includes any “enforcement or *other action* authorized under the State program to cause the violation to be corrected.” 30 C.F.R. § 842.11(b)(1)(ii)(B)(3) (emphasis added). This provision of OSMRE’s regulations

focuses on the goal of the Act itself—to see that violations are corrected. In doing so, the rule allows state discretion in how best to accomplish that goal—but only if those means are authorized under the state program. OSM is not permitting a “free bite,” but is simply saying that the federal government will not substitute its judgment and second-guess the states on a case-by-case basis, unless the state action is arbitrary, capricious or an abuse of discretion under its program.

53 Fed. Reg. 26733, 26734 (July 14, 1988) (emphasis added).

When it proposed this regulation, OSMRE recognized a distinction between enforcement and other actions to correct a possible violation. “[E]nforcement would include, but would not be limited to, the issuance of an NOV to the operator” and an “other action” could include a permit revision or a proceeding to forfeit a bond, but noting that these “examples are not meant to be an exhaustive list of acceptable responses.” 52 Fed. Reg. 34050 34051 (Sept. 9, 1987). It added:

By this rule, OSMRE would reject the concept that appropriate action to cause a violation to be corrected would only include responses showing that at the time of the State response either the condition constituting the possible violation of the Act no longer exists or the State has issued an NOV or cessation order.... Direct OSMRE enforcement against an operation would not be utilized ... when the State is acting reasonably to correct a possible violation. Under the proposed rule, *appropriate action would mean that certain conditions may continue in the short term, but ultimately the violation of the State program will be resolved.*

Id. (emphasis added). In the final rulemaking OSMRE went even further, and stated that “actual abatement of a violation is not the standard for determining whether a state response is appropriate,” provided the state response would “lead to abatement within a reasonable time.” 53 Fed. Reg. at 26734.

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“Good cause” for failing to correct a violation includes circumstances in which “[u]nder the State program, the possible violation does not exist.” 30 C.F.R. § 842.11(b)(1)(ii)(B)(4)(i). It also includes circumstances in which “State regulatory authority is precluded by an administrative or judicial order from an administrative body or court of competent jurisdiction from acting on the possible violation, ... where the temporary relief standards of section ... 526(c) of the Act have been met[.]” 30 C.F.R. § 842.11(b)(1)(ii)(B)(4)(iv).

OSMRE considers appropriate action to cause a violation to be corrected or good cause for failure to do so to be “an action or response by a State regulatory authority that is not arbitrary, capricious, or an abuse of discretion under the state program. 30 C.F.R. § 842.11 (b)(1)(ii)(B)(2). OSMRE internally defines “arbitrary, capricious, or an abuse of discretion” as essentially irrationality or the failure to follow correct procedures or applicable law. OSMRE Directive INE-35 § 3.b. (Jan. 31, 2011). “In general, OSM[RE] will make a finding of appropriate action or good cause if the [regulatory authority] presents a rational basis for its decision, even if OSM[RE] might have decided it differently.” *Id.* at § 4.d.

DEQ’S APPROPRIATE ACTIONS

At every stage of its interactions with Alpha DEQ took appropriate action to investigate and respond to Alpha’s declining financial condition.

First, DEQ’s 2014 renewal of Alpha’s self-bonds were based on the only available audited financial statements in conformity with Chapter 11, Section 4(a)(ii) of its regulations. That section provides that in considering a renewal application, the Administrator “may request financial statements for the most recently completed fiscal year together with an independent certified public accountant’s audit opinion or review opinion of the financial statements with no adverse opinion. Additional unaudited information may be requested by the Administrator.”

When additional information became available in April 2015 which indicated that Alpha may no longer qualify for self-bonding, DEQ requested additional information to aid in its review of Alpha’s continued eligibility. When that information failed to demonstrate Alpha continued to be eligible, DEQ issued a substitution demand in conformity with Chapter 11, Section 5 of its regulations. In response, Alpha exercised its rights under state law to request an informal conference and to file a petition for review in state court of the substitution demand.

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Before any further action on the substitution demand was required by Chapter 11, Section 5, Alpha filed for relief in the bankruptcy court. That action created a serious dispute between Alpha and DEQ about whether DEQ could take any further action related to the substitution demand. In light of this dispute, DEQ chose to exercise its authority under Wyo. Stat. Ann. § 35-11-701 to negotiate a settlement that would ultimately eliminate the violation. That statute provides that if “the director or the administrators have cause to believe that any persons are violating any provision of this act or any rule, regulation, standard, permit, license, or variance issued pursuant hereto, ... the director through the appropriate administrator, shall cause a prompt investigation to be made.” Wyo. Stat. Ann. § 35-11-701(a). If, as a result of DEQ’s investigation, it appears that a violation exists, “the administrator of the proper division may, by conference, conciliation, and persuasion, endeavor promptly to eliminate the source or cause of the violation.” Wyo. Stat. Ann. § 35-11-701(c). This authorization to enter into settlements is similar to West Virginia’s settlement authority which the bankruptcy court found to be a lawful source of its authority to enter into a substantially similar settlement agreement.

DEQ’s decision to enter into the settlement agreement was appropriate other action and not arbitrary, capricious, or an abuse of discretion. The settlement is as eminently reasonable, equitable, and lawful as the bankruptcy court found the West Virginia settlement agreement. In fact, the decision of the bankruptcy court likely establishes that DEQ’s settlement is per se appropriate other action. The agreement settled a “hotly contested” dispute in a way that provided additional interim security to Wyoming, and set Alpha on a path to comply with its bonding obligations at the conclusion of the bankruptcy proceedings. Absent the settlement, Alpha would be immediately required to post the full amount of its reclamation bond obligation, which it is obviously unable to do during the pendency of the bankruptcy. Instead, the settlement allows Alpha to transition away from its self-bonds over the limited duration of the bankruptcy to the benefit of the company, the state, and the public. This is exactly the situation envisioned by OSM when it drafted its regulations to allow for certain conditions in the short term, so that the violation will ultimately be resolved within a reasonable time.

Having cleared the low bar of rationality and lawfulness, OSMRE is not permitted to second-guess the wisdom of DEQ’s settlement agreement. While OSMRE might have chosen not to settle or to settle on other terms, the fact that Wyoming has an approved program means that DEQ has exclusive jurisdiction to make these decisions.

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THE BANKRUPTCY STAY PROVIDES GOOD CAUSE

In addition to being appropriate other action, the stay issued by the bankruptcy court provides good cause for DEQ's decision not to take further enforcement action at this time. The stay entered by the bankruptcy court satisfies the temporary relief standards of section 526(c) of SMCRA. As a result, no further action on the TDN is warranted.

OSMRE regulations allow for the possibility that certain administrative and judicial actions can prevent enforcement actions by state regulatory authorities. *See* 30 C.F.R. § 842.11(b)(1)(ii)(B)(4)(iv). While the bankruptcy order does not purport to determine whether or not the violation exists, it does satisfy the temporary relief standard set forth in Section 526(c) of SMCRA. 30 U.S.C. § 1276(c). That section governs temporary injunctions of Secretarial acts so long as the following three standards are met:

- (1) all parties to the proceedings have been notified and given an opportunity to be heard on a request for temporary relief;
- (2) the person requesting such relief shows that there is a substantial likelihood that he will prevail on the merits of the final determination of the proceeding; and
- (3) such relief will not adversely affect the public health or safety or cause significant imminent environmental harm to land, air, or water resources.

These standards were met when the bankruptcy court entered the stay. Alpha's bankruptcy filing was widely reported both locally in Wyoming and across the nation. Similarly, when Alpha and DEQ reached a settlement subject to approval by the bankruptcy court, that fact was also widely reported. *See, e.g., Alpha Natural Resources and Wyoming regulators announce self-bonding deal in bankruptcy case*, Casper Star Tribune (Sept. 8, 2015). After the settlement was announced, the bankruptcy court held a hearing on Alpha's motion for entry of the stipulation and order on September 28, 2015. No one, including OSMRE, objected to the entry of the stay during that hearing.

In its motion to the bankruptcy court, Alpha demonstrated a substantial likelihood of success on the merits of the final determination that the automatic stay precludes DEQ from enforcing the substitution demand. It is worth recalling here, that at the urging of OSMRE, Alpha did not seek relief under Section 105 of the bankruptcy code irrespective of whether the automatic stay applied. As evidenced by the bankruptcy court's favorable view of the West Virginia settlement, a request for stay pursuant to the court's equitable powers would in all likelihood have been granted whether DEQ objected or not. Finally,

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the fact that DEQ consented to the entry of the stay is inconsequential to the objective likelihood of success demonstrated by Alpha.

In turn, there can be no dispute that the stay will not adversely affect the public health or safety or cause any imminent environmental harm. To the contrary, the order ensures that reclamation will continue unabated for the duration of the bankruptcy proceeding and that DEQ will have full enforcement power over Alpha's mining operations.

Because any interested person had an opportunity to be heard before the bankruptcy court entered the stay, it was substantially likely that Alpha would obtain the stay, and no harm results to the public or the environment, DEQ's compliance with the stay constitutes good cause not to take additional enforcement action against Alpha. This is true regardless of whether the stay prohibits OSMRE from taking action inconsistent with the bankruptcy court's order. Issuance of the TDN or other further action by OSMRE related to Alpha's self-bonding status arguably qualifies as an administrative "proceeding" precluded by the plain language of the court's order. In either event, the order from a court of competent jurisdiction precludes DEQ from taking any further enforcement action against Alpha based on its self-bonding status. That is good cause.

CONCLUSION

The dramatic decline in Alpha's financial condition within a short period of time culminating in bankruptcy proceedings created a series of challenges for both DEQ and OSMRE. These events highlight certain systemic problems with self-bonding, but had to be addressed individually and in a timely manner. DEQ, as the entity with exclusive jurisdiction over the matter, exercised its considerable discretion to enter a settlement that protects the public, the environment and sets a firm timetable for Alpha's transition away from self-bonds. This resolution was lawful, reasonable, and meets the goal of SMCRA to see that violations are corrected. OSMRE has no basis for second guessing DEQ's judgment, and even if it did, the court's order justifies DEQ's decision not to take further action.

Accordingly, DEQ requests that OSMRE respond to this response to the TDN by finding that DEQ took appropriate other action and has good cause for deciding not to take further enforcement action against Alpha as a result of its self-bonding status.

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Please let me know if you have questions or concerns about anything in this response. Again, we believe that both parties would benefit from a meeting to discuss the issues raised in the TDN and this response before OSMRE responds. DEQ hereby renews its request to meet at a time that is mutually convenient for OSMRE and DEQ.

Sincerely,



Kyle Wendtland
Administrator, Land Quality Division

cc: Matthew H. Mead
Michael Enzi
John Barrasso
Cynthia Lummis
Peter K. Michael
Janice M. Schnieder
Drew McCallister
Carl Black
Patrick Crank
Todd Parfitt