

OK
Outgoing
C007/0045

0004

From: Daron Haddock
To: John Gefferth; Karl Houskeeper
Date: 3/20/2008 4:33 PM
Subject: Fwd: Covol - file: C007/0045
Attachments: Covol - file: C007/0045

Please see the attached email from Mary Ann regarding the disposition of the Covol site and their ability to operate. Mary Ann was pretty clear that she would allow them to operate once they had posted a bond and provided a complete application, both of which we have. We do have Steve Alder trying to provide some more of the legal pieces to the puzzle, but as I see it Covol is authorized to operate. We should be able to give you a definite go or no go soon after Steve alder gets back in the office. Thanks.

From: Mary Ann Wright
To: Daron Haddock
CC: Angela Nance; Jo Ogea; Steve Alder
Date: 3/20/2008 3:44 PM
Subject: Covol - file: C007/0045
Attachments: 0002.pdf; 0003.pdf; 10202006ltrGallifromAlder.pdf

Daron:

RE: Ability of COVOL to process coal waste from permitted sites.

Attached is my letter to Covol, Keith Thompson, of 3/13/07. See the second to the last paragraph of the letter that, upon posting the surety amount of \$165,000, "would allow COVOL to process coal waste from existing permitted sites while COVOL completes the permitting process."

- 1) COVOL has submitted the required bond, and
- 2) COVOL has submitted an administratively complete application for review (personal comm. DRH 3/17/08).

Therefore, COVOL can process coal waste from existing permitted sites. This was anticipated as part of the settlement agreement.

Second attachment is COVOL's appeal to the Board and, third, a 10/20/06 Atty Gen letter to COVOL counsel regarding settlement. I do not have the documents referred to in the first paragraph of that letter, I don't believe that I received those.

As a side note: On 3/4/08 Steve Alder, AG, agreed to research where we left off in the matter of the Settlement Agreement and the formal withdrawal of the Board matter.

Please let me know if you have any questions. Thanks.

Mary Ann Wright

Associate Director, Mining
Utah Division of Oil, Gas and Mining
801-538-5306

Daron:

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Please let me know if you have any questions. Thanks.

Mary Ann Wright

Associate Director, Mining
Utah Division of Oil, Gas and Mining
801-538-5306

0002



State of Utah

**Department of
Natural Resources**

MICHAEL R. STYLER
Executive Director

**Division of
Oil, Gas & Mining**

JOHN R. BAZA
Division Director

JON M. HUNTSMAN, JR.
Governor

GARY R. HERBERT
Lieutenant Governor

March 13, 2007

OK
Outgoing
C/007/00415

Mr. Keith Thompson
COVOL Engineered Fuels LC
10653 S. River Front Parkway, Suite 300
South Jordan, Utah 84095
kthompson@headwaters.com

Subject: COVOL Application Outline of Dry-Coal Cleaning Facility/Requirement to Permit and Post Bond

Dear Mr. Thompson:

The Division of Oil, Gas & Mining (Division) has completed a review of the Permit Outline submitted by Covol Engineered Fuels LC (COVOL) in December 2006. In addition, we are responding to telephone requests from you and Mr. Bunderson about Covol accepting coal mine waste for processing, and not just for 'test runs' of 1000 cyds. Based on COVOL's plans to bring coal mine waste from other permitted sites, COVOL needs to firmly agree to proceed with permitting, and therefore to formally drop its appeal to the Board of Oil Gas & Mining. In addition, COVOL needs to post a bond for reclamation of the site in the amount of \$165,000.

The Division reviewed the application along with the environmental audit submitted by COVOL during discovery. The Division appreciates COVOL's efforts and believes the outline is very close to the permit requirements to which the Division previously agreed. The Division would like to ease the permitting process as much as possible and invites COVOL to discuss this matter in person, by phone, or by letter at any time.

While the permit outline is close, there are several items that still need to be addressed. The following comments correlate with the permit outline chapters:

I. Chapter 1

- 1) Permit and disturbed area map: include a table with acreages - permit area/disturbed area map.
- 2) Include map showing adjacent surface landowners.
- 3) Provide the MSHA Number.
- 4) Provide ownership and control information.

II. Chapter 2

- 1) Provide map showing different soil types.
- 2) Provide surface facilities map showing location of topsoil storage areas.
- 3) Address how topsoil will be stored and protected.
- 4) Address where any toxic or acid-forming materials that will be generated, will be placed and handled on site.

III. Chapter 3

- 1) Address any Threatened and Endangered species (wildlife or vegetation) on or adjacent to the permit area.

IV. Chapter 4

- 1) The application should include a copy of the Wellington City Agreement for reclaiming the site.
- 2) Since the land is an industrial site, the reclamation plan should be a clean-up plan of the site, i.e., removal of coal, wood, metal, non-coal waste material and where it will be disposed.
- 3) Discuss how the buildings will be left.
- 4) Provide the class III cultural survey on undisturbed area and class I cultural survey for the permit area (paper search). These reports must be in a confidential section of the application.
- 5) Provide a copy of the SPCC Plan.

V. Chapter 5

- 1) Provide a surface facility map showing all buildings (permanent structures), refuse piles, coal storage areas, non-coal waste storage areas, P.E stamped.
- 2) Engineering and Hydrology maps need P.E. certifications.
- 3) Provide hydrology map showing locations of sediment ponds, diversion ditches, silt fences etc.
- 4) All temporary and permanent coal mine waste and/or refuse and/or "by-products" pile storage areas need to be addressed. Show on map all refuse storage areas. Explain how is the material handled and disposed?

Page 3
Keith Thompson
March 13, 2007

VI. Chapter 6

N/A

VII. Chapter 7

- 1) Provide a table of water rights for the facility/water replacement plan.
- 2) Separate the disturbed area from the undisturbed area and show how water is controlled on the site. (OGM recommends a sedimentation pond to treat all drainage from the disturbed area). Show how structures are designed and for which design event.
- 3) Include the UPDES permit.
- 4) Identify all water sources on a map (seeps, springs)—quarterly water sampling program.

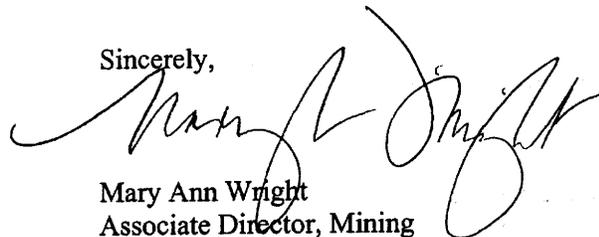
VIII. Chapter 8

- 1) Provide public liability insurance.
- 2) Provide reclamation cost estimate (if different from \$165,000) and post a bond.

Last week, I provided Trace Bunderson of your office with a reclamation cost estimate of \$165,000. This amount is based on an average cost estimate per acre from the mining program of \$5,000/acre. Immediately posting this amount as a bond, whether cash (CD, LOC, Treasury notes) or surety bond, would allow COVOL to process coal waste from existing permitted sites while COVOL completes the permitting process. Submittal of a completed mine permit application should follow within a reasonable time.

Please contact me at (801) 538-5306 to set up a meeting to review this and other permitting issues as soon as possible. Thank you for your patience and cooperation.

Sincerely,



Mary Ann Wright
Associate Director, Mining

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MAY 12 2006

SECRETARY, BOARD OF
OIL, GAS & MINING

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C/007/0045

Craig D. Galli (5072)
Matthew C. Droz (10741)
HOLLAND & HART LLP
60 E. South Temple, Suite 2000
Salt Lake City, Utah 84111-1031
Phone: (801) 799-5842
Fax: (801) 364-9124
Attorneys for Covol Engineered Fuels, LC

**BEFORE THE BOARD OF OIL, GAS, AND MINING
DEPARTMENT OF NATURAL RESOURCES
STATE OF UTAH**

In Re Memorandum Decision of the Division Of
Oil, Gas, and Mining to Permit Covol Engineered
Fuels, LC (COVOL) under the Surface Mining
Control and Reclamation Act, Carbon County, Utah

**REQUEST FOR AGENCY ACTION
OF COVOL ENGINEERED FUELS,
LC TO APPEAL MINE PERMIT
DETERMINATION**

Docket No.2006-009
Cause No. C/007/0045

Pursuant to Utah Admin. Code R641-105-100 and Utah Code Ann. § 63-46b-3(b),
Petitioner Covol Engineered Fuels, LC (COVOL), by and through its attorneys, Holland & Hart,
LLP, hereby submits its Request for Agency Action to Appeal Mine Permit Determination.

COVOL and the Division of Oil, Gas and Mining ("DOGM") previously entered into a
"Stipulation of the Parties Regarding Proceedings Before the Board of Oil, Gas and Mining,"
dated April 28, 2006 (the "Stipulation"), to govern these proceedings. That Stipulation provides
that this Appeal will be decided through formal adjudication, including discovery, pre-hearing
motions, and stipulated facts through a pre-hearing conference. *See* Stipulation ¶ 5.

Accordingly, COVOL reserves the right to provide the Utah Board of Oil Gas and Mining (the

“Board”) supporting documentation, including motions, affidavits, exhibits, briefs and memoranda, as part of its full briefing of the merits prior to the hearing which will not occur prior to July 26, 2006.

STATEMENT OF JURISDICTION

The Board has jurisdiction over this Request for Agency Action pursuant to Utah Code Ann. § 40-10-14 and Utah Admin. Code R645-300-200.

STATEMENT OF FACTS

1. COVOL has proposed to operate a 500,000 tpy (or more) capacity coal cleaning and blending facility in Wellington, Carbon County, Utah (the “Facility”). The Facility will utilize a dry air separation process in order to beneficiate off-specification coal product. The Facility will produce a customized coal fuel for its end-user customers based on specifications provided by the end user. *See* Letter from R. Keith Thompson, COVOL to Lowell P. Braxton (Jul. 13, 2004) (**Exh. A**). Construction of the Facility is scheduled to be completed within two or three months.

2. On September 13, 2004, DOGM issued preliminary findings concluding that the proposed operation “is not being done ‘in connection with’ a coal mine. As such it would not require permitting under the Utah coal regulatory program since it is not considered coal mining and reclamation operations.” *See* Letter from Mary Ann Wright transmitting “Preliminary Finding of Proposed Coal Beneficiating Air Processing Facility in Carbon County” (Sept. 13, 2004) (**Exh. B**).

3. COVOL subsequently entered into two coal processing agreements, one with PacifiCorp (**Exh. C**) and the other with Commonwealth Coal Services, Inc. (**Exh. D**). COVOL

previously provided both agreements to DOGM.¹

4. On March 17, 2006, DOGM issued COVOL a “Determination to Permit Under the Surface Mining Control and Reclamation Act” (the “Determination”) (**Exh. E**). The Determination reversed its earlier findings, concluding that the Facility constituted a “surface coal mining operation” within the meaning of Utah Code Ann. § 40-10-3(2).

5. On April 3, 2006, COVOL filed with the Board its “Notice of Administrative Appeal” pursuant to Utah Admin. Code R645-300-211.

STATEMENT OF BASIS FOR RELIEF SOUGHT

For the reasons stated below, COVOL respectfully requests a declaratory judgment by the Board that the coal mine permit and reclamation requirements of the Utah Coal Mining and Reclamation Act (the “Act”) do not apply to the Facility.

I. COVOL’S FACILITY DOES NOT CARRY OUT ACTIVITIES “IN CONNECTION WITH A SURFACE COAL MINE”

The Act provides that “No person shall engage in or **carry out surface coal mining operations** within the state unless that person has first obtained a permit issued by the division pursuant to an approved mining and reclamation program....” Utah Code Ann. § 40-10-9(1)

(emphasis added). The Act defines “Surface coal mining operations” to mean:

Activities conducted on the surface of lands **in connection with a surface coal mine**.... These activities include excavation for the purpose of obtaining coal, including such common methods as contour, strip, auger, mountaintop removal box cut, open pit, and area mining, the uses of explosives and blasting, and in situ distillation or retorting, leaching or other **chemical or physical processing, and the cleaning**, concentrating, or other processing or preparation, loading of coal for interstate commerce **at or near the mine site**.

¹ Please note that Exhibits C and D are protected from disclosure as Confidential Business Information pursuant to Utah Code Ann. §§ 40-8-8(c) & 63-2-304(2).

Id. § 40-10-3(20) (emphasis added).

The state regulations address the permit requirements applicable to “coal processing plants not located within the permit area of a mine,” requiring a mine permit of “any person who operates or intends to operate a coal processing plant outside the permit area of any coal mining and reclamation operation, other than such plants which are located at the site of ultimate coal use.” Utah Admin. Code R645-302-261.

While the Facility does clean coal in a manner that involves “chemical or physical processing,” the Facility does not engage in any activity “in connection with a surface coal mine.” Utah Code Ann. § 40-10-3(20). As DOGM noted in the Determination, “the Utah Act closely follows the [Surface Mine Control and Reclamation Act], and therefore, the Division looks to the federal law for the meaning of ‘in connection with a surface coal mine.’”

Determination at 3. As part of the preamble to the analogous federal regulations (30 C.F.R. § 785.21(a)), the Office of Surface Mining (“OSM”) has published the following factors which regulatory authorities consider in determining the applicability of the federal regulations:

1. Whether the facility receives a significant portion of its coal from a mine.
2. The economic relationship between the facility and a mine.
3. The functional relationship between the facility and the mine it services. Does the facility have a useful life independent of a mine?
4. Geographic proximity to a mine, although geographic proximity is not a determinative factor.
5. The degree of control a mine has over the processing operations.
6. Any other type of integration that exists between a facility and a mine.

See generally 53 Fed. Reg. 47,384, 47,385-86 (Nov. 22, 1988).

Based on these six factors, the Facility does not operate in connection with a surface mine. First, COVOL currently does not have contracts to receive any of its coal from a coal mine. Rather, COVOL plans to receive coal from (1) Commonwealth Coal Services, Inc.

("Commonwealth"), a broker which receives coal from multiple coal mines; (2) the division of PacifiCorp which acquires feedstock for power plants (not from the PacifiCorp division which owns and operates coal mines; and (3) from coal purchases on the open market.²

Second, COVOL has no economic relationship with any coal mine. Third, COVOL has no functional relationship with any coal mine, and services no coal mine. Rather, COVOL's entire business is to service end users. Fourth, the Facility is not located on or adjacent to any coal mine. Fifth, no coal mine has control over the processing operations or over any other aspect of the Facility. Sixth, no degree of integration exists between the Facility and any coal mine.

II. DOGM'S INTERPRETATION AND APPLICATION OF ITS RULES VIOLATES UTAH CODE ANN. § 40-10-6.5

The Determination relies heavily on DOGM's "discretion" to apply its rules on a case-by-case basis. *See* Determination at 4 (citing the preamble to the federal rules). However, the Utah Coal Mining and Reclamation Act prohibits DOGM from promulgating and/or administering rules which are more stringent than federal law:

(2) Except as provided in Subsection (3), no rule which the board adopts for the purpose of the state administering a program under the federal Surface Mining Control and Reclamation Act may be more stringent than the corresponding federal regulations which address the same circumstances. In adopting such rules, the board may incorporate by reference corresponding federal regulations.

(3) The board may adopt rules more stringent than corresponding federal regulations for the purpose described in Subsection (2), only if it makes a written finding after public comment and hearing, and based on evidence in the record, that the corresponding federal regulation is not adequate to protect public safety and the environment of the state. Those findings shall be accompanied by an opinion referring to and evaluating the public safety and environmental

² Even though COVOL has no current plans to purchase coal directly from a coal mine, such arm's length purchases would not constitute operating "in connection with a coal mine."

information and studies contained in the record which form the basis for the board's conclusion.

Utah Code Ann. § 40-10-6.5.

DOGM has both adopted rules and is interpreting/administering its rules in a manner which is more stringent than federal law. First, DOGM's rules require **all** coal processing plants, except those "located at the site of ultimate coal use," to be permitted. Utah Admin. Code R645-302-261. Thus, a coal processing plant located on the site of a power plant is exempt from coal mine permitting, while a stand alone facility, like COVOL's operation, is subject to the permitting and reclamation requirements.

In contrast, the corresponding federal rules more narrowly apply to a "person who operates or intends to operate a coal preparation plant in connection with a coal mine but outside the permit area for a specific mine." 30 C.F.R. § 785.21(a). Thus, under federal law, a facility may be located away from the site of ultimate coal use, but still be exempt provided it does not operate in connection with a coal mine.

DOGM cannot deny the fact that on its face, the specific state rules are more stringent than the corresponding federal rules even though the Board has never made a finding that "the corresponding federal regulation is not adequate to protect public safety and the environment of the state" with an accompanying "opinion referring to and evaluating the public safety and environmental information and studies contained in the record which form the basis for the board's conclusion." Utah Code Ann. § 40-10-6.5. Thus, the state rules governing the coal processing plants violate this requirement of the Utah legislature.

Second, DOGM has interpreted and is attempting to apply its rules in a manner that is more stringent than federal law (or any other state law governing coal mine permitting). Indeed,

COVOL has owned and/or operated synthetic fuel facilities in Virginia, West Virginia and Pennsylvania which did not require a coal mine permit and were exempt from reclamation requirements. DOGM cannot identify a single state or OSM office which has imposed coal mine permit and reclamation requirements on a coal processing plant which is located offsite of a coal mine and operated independently (i.e., not “in connection with”) a coal mine.

The regulatory history of the federal rules also demonstrates that DOGM’s rules and interpretation of those rules is more stringent than the corresponding federal rules. OSM’s 1988 rule amendments clarify that OSM “can no longer treat all facilities which handle coal as either ‘in connection with’ a mine or ‘in connection with’ an end user as it could when the definition of coal preparation was based on the separation of coal from its impurities.... OSM is only requiring regulatory authorities to extend their permit requirements as far into the stream of commerce as those activities over which mine operators and the coal handlers who directly serve them, such as coal processors, have or could have control of operations.” 53 Fed. Reg. at 47,385. OSM noted that facilities in Maryland, Virginia, Alabama and California conduct coal processing activities which are not controlled by coal mines and their agents. “[T]he Act was [not] intended to regulate the activities of such facilities.... [I]t is necessary to ensure that the performance standards ... and permitting requirements are applied only to facilities conducting coal preparation ‘in connection with’ a coal mine.” *Id.*

The reference to the federal statute in the above quote makes clear that OSM acknowledged the existence of a jurisdictional bar established by statute. Importantly, OSM recognized that its jurisdiction in the “stream of commerce” ended when the coal preparation occurred by or for the end user:

[OSM] continues to believe that regulation of facilities operated by or **for the end user** of coal at the point of such use is not required under SMCRA because, **by virtue of their association with the end user of the coal, such facilities are not operated “in connection with” a coal mine.**

Id. at 47,384 (emphasis added).

In contrast, the Determination makes clear that DOGM believes that the assertion of its jurisdiction is appropriate notwithstanding the undisputed fact that the coal preparation conducted by COVOL is “for the end user,” *id.* pursuant to the end user’s specifications. DOGM disregards the fact that COVOL’s activities fall on the end user side of the stream of commerce. In DOGM’s view, only the power plant itself apparently is exempt from its jurisdiction: “Covol is not an end user.... Covol sells coal to power plants. The power plant is the end user.... Covol is not located at the site of an end user.” Determination at 5.

DOGM’s assertion of jurisdiction over the entire stream of commerce except for the power plant and activities conducted on the power plant site far exceeds the scope of jurisdiction articulated by OSM with respect to the corresponding federal regulations. DOGM has done so without conducting the requisite rulemaking, thereby violating the prohibitions of Utah Code Ann. § 40-10-6.5.

III. NO PRACTICAL BASIS EXISTS TO JUSTIFY IMPOSITION OF THE COAL MINE PERMIT AND RECLAMATION REQUIREMENTS

DOGM cannot identify a single practical reason to justify the imposition of the coal mine permit and reclamation requirements. First, unlike a coal mining operation, COVOL’s operations will result in no surface or subsurface disturbance (other than construction of infrastructure and coal storage) or impacts to mitigate or remediate such disturbance. For the purpose of obtaining its local land use approvals, COVOL’s parent company Headwaters

Incorporated, committed to the City of Wellington to ensure that "Covol will removal all coal and residual material located on the property (excluding material used for improvements)." See Letter from Steven G. Stewart, Headwaters Incorporated to Karl Houskeeper, Mayor of Wellington (July 6, 2005) (Exh. F).

Accordingly, even if DOGM had the discretion under the law – which it does not – to impose on COVOL the coal mine permit and reclamation requirements, no possible practical justification exists for doing so. Moreover, any environmental impacts associated with operations of the Facility will be regulated by the Utah Department of Environmental Quality. Thus, there simply is no regulatory need for imposing DOGM mine permit and reclamation requirements.

CONCLUSION

Covol respectfully requests that the Board reverse the March 17, 2006 "Determination to Permit Under the Surface Mining Control and Reclamation Act" issued by DOGM for the reasons stated above.

DATED this 12th day of May 2006.

HOLLAND & HART LLP



Craig D. Galli
Matthew C. Droz

Attorneys for Covol Engineered Fuels, LC

CERTIFICATE OF SERVICE

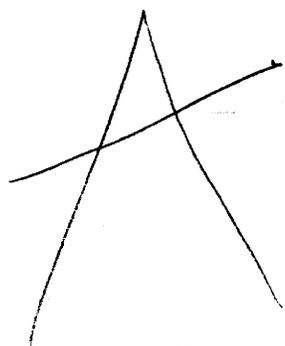
I hereby certify that a true and correct copy of the foregoing was served via hand delivery on the 12th day of May 2006 to the following:

Mr. James Peacock
UTAH BOARD OF OIL GAS & MINING
Department of Natural Resources
1594 West North Temple, Suite 1210
Salt Lake City, Utah 84114-5801

Steven F. Alder, Esq.
Utah Attorney General
1594 West North Temple, Suite 300
P.O. Box 140855
Salt Lake City, UT 84114



A handwritten signature in cursive script, appearing to read "S. F. Alder", is written over a horizontal line.





COVOL
ENGINEERED FUELS L.C.

A Division of Headwaters Incorporated

July 13, 2004

Lowell P. Braxton
Director
State of Utah
Division of Oil Gas and Mining
1594 West North Temple
Salt Lake City, Utah 84114

RE: Covol Engineered Fuels L.C., Coal Cleaning Project – Price, Utah

Dear Mr. Braxton:

Covol Engineered Fuels L.C. (Covol) is proposing to install and operate a 500,000 ton-per-year coal cleaning and blending facility in Carbon County. The facility will utilize a dry air separation process in order to beneficiate off-spec coal products. Feedstock for the facility will come from multiple local and other mining sources, and will not stem from any single mine and/or mining entity. In addition, it is anticipated that the finished, beneficiated product will be sold into the steam coal market. Of particular interest, this operation will create upwards of 15 new jobs in Carbon County.

Please find attached a description of Covol's proposed activities, as well as two (2) site plan drawings for your review.

Based upon previous rulings issued by the Division of Oil, Gas and Mining (Division), it is Covol's understanding that since the facility will not be directly associated with mining, as well as the fact that by-products from the operation will have beneficial use and/or waste will not remain on the site, the facility will not fall under the regulatory guidelines of the Division. Covol respectfully requests the Division's concurrence.

Sincerely,

R. Keith Thompson
Vice President

Attachments

Coal Cleaning Project
Covol Engineered Fuels LC
Price, Utah

Facility Description

The facility will clean and blend various coals. This facility will utilize patented equipment to beneficiate out-of-specification run-of-mine coal by reducing ash, pyritic sulfur and mercury through a dry air separation process. The facility is designed to process approximately 500,000 tons of run-of-mine coal per year.

Raw Material

High ash, high sulfur coal will be delivered to the facility via truck from several sources, including mines, in Carbon and Emery counties. Covol Engineered Fuel LC will purchase the coal directly from mining companies or enter into a tolling agreement to clean the out-of-specification coal. The various coals will be unloaded via a drive over truck dump and segregated into storage piles by radial stacker.

Coal Cleaning and Blending

The selected coal to be cleaned will be removed from the appropriate coal storage pile by front end loader and dumped into a receiving hopper. The coal will be conveyed to a vibrating screen and crusher unit. The screened and crushed coal is then conveyed to three (3) air jig cleaning units, according to size. The air jig units are complete with bag houses for particulate collection. This unit separates the ash and coal using pulsating air. The cleaned coal is then conveyed to a storage silo or several clean coal storage piles. This cleaned coal can then be blended to meet specifications for ash, sulfur, mercury content and BTU values. The beneficiated coal is then loaded into trucks via the drive under silo or loading hopper feed by a front end loader. The final product is shipped to a consumer, power plant, synfuel plant or coal load out terminal via truck. The by-product, ash and clay materials, are collected from the air jig units and conveyed to a storage pile for future use.

This coal cleaning and blending facility is designed to process non-compliant waste coals, producing a clean, customized fuel.

B



State of Utah

Department of
Natural Resources

ROBERT L. MORGAN
Executive Director

Division of
Oil, Gas & Mining

LOWELL P. BRAXTON
Division Director

OLENE S. WALKER
Governor

GAYLE F. McKEACHNIE
Lieutenant Governor

September 13, 2004

W. Layne Ashton, Corporate Manager
Covol Engineered Fuels, LC
10653 South Riverfront Parkway, Suite 300
South Jordan, Utah 84095

Re: Preliminary Finding, of Proposed Coal Beneficiating Air Processing Facility
in Carbon County – Covol Engineered Fuels, LC

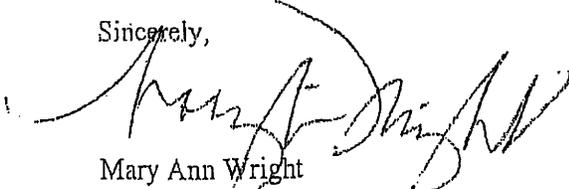
Dear Mr. Ashton:

Enclosed please find a memo outlining the Division's preliminary finding Concerning Covol's proposed operation in Carbon County, dated August 5, 2004. In order to finalize the finding, we request further information about the 'tolling fee' agreement with Pacificorp. Covol agreed to provide this information in our meeting of July 13, 2004.

Subject to a determination regarding the above noted information, and also subject to the result of an on site Division inspection, the initial determination is that mining activities will not be taking place at this site. Therefore, it does not appear at this time that this project will be subject to regulation under the Utah Coal Mining Act.

Please supply the needed information, and/or contact me if you have further questions at (801) 538-5306 or maryannwright@utah.gov.

Sincerely,


Mary Ann Wright
Associate Director, Mining

an
Enclosure
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August 5, 2004

TO: Mary Ann Wright, Associate Director, Mining

FROM: Pamela Grubaugh-Littig, Permit Supervisor
D. Wayne Hedberg, Permit Supervisor

RE: Preliminary Finding of Proposed Coal Beneficiating Air Processing Facility in Carbon County - Covol Engineered Fuels, LC

SYNOPSIS

On July 13, 2004, the Division received a proposal from Covol Engineered Fuels, LC (Covol), which discusses the installation of a 500,000-ton per year coal cleaning and blending facility in Carbon County. The facility will utilize a dry air separation process to beneficiate off-spec coal products. Feedstock for the facility will come from multiple local and other mining sources, and not from any single mine and/or mining entity. The "beneficiated" product will be sold into the steam coal market.

Based upon a previous finding in 1996, Covol feels that this activity would not fall under the purview of the Utah Coal Regulatory Program and has asked for the Division's concurrence. This memo is a preliminary finding and analysis of the proposal and provides findings, which will enable the Division to determine the permitting requirements for this type of facility.

During the meeting on July 13, 2004, Layne Ashton, Ronald Sherbak and Keith Thompson (Covol) as well as Jay Martin and Tom Paluso (Terra) met with Wayne Hedberg, Mary Ann Wright and Pamela Grubaugh-Littig (Oil, Gas, and Mining), the need to send more information about the PacifiCorp coal contract was noted. The preliminary discussion focused on PacifiCorp coal having a "tolling fee" for processing, which meant that Covol never bought the coal and PacifiCorp maintained ownership. The Division asked for more information on the contract to clarify the situation.

The Division also advised Covol that a preliminary finding would be issued, with a possible request for more information. Once the facility is operating, the Division would inspect the site and issue a final finding.

ANALYSIS

Under the Utah coal regulatory program it is necessary for anyone who engages in or carries out any coal mining and reclamation operations to first obtain a permit (R645-300-112.400). The question that must then be asked is, whether or not the Covol activity constitutes "coal mining and reclamation operations"?

This term is defined at R645-100-200 as follows:

"Coal Mining and Reclamation Operations" means (a) activities conducted on the surface of lands in connection with a surface coal mine or, subject to the requirements of Section 40-10-18 of the Act, surface coal mining and reclamation operations and surface impacts incident to an underground coal mine, the products of which enter commerce or the operations of which directly or indirectly affect interstate commerce. Such activities include all activities necessary and incidental to the reclamation of the operations, excavation for the purpose of obtaining coal, including such common methods as contour, strip, auger, mountaintop removal, box cut, open pit, and area mining; the use of explosives and blasting; in-situ distillation; or retorting, leaching, or other chemical or physical processing; and the cleaning, concentrating, or other processing or preparation of coal. Such activities also include the loading of coal for interstate commerce at or near the mine site. Provided, these activities do not include the extraction of coal incidental to the extraction of other minerals, where coal does not exceed 16-2/3 percent of the tonnage of minerals removed for purposes of commercial use or sale, or coal exploration subject to Section 40-10-8 of the Act; and, provided further, that excavation for the purpose of obtaining coal includes extraction of coal from coal refuse piles; and (b) the areas upon which the activities described under part (a) of this definition occur or where such activities disturb the natural land surface. These areas will also include any adjacent land the use of which is incidental to any such activities, all lands affected by the construction of new roads or the improvement or use of existing roads to gain access to the site of those activities and for haulage and excavation, workings, impoundments, dams, ventilation shafts, entryways, refuse banks, dumps, stockpiles, overburden piles, spoil banks, culm banks, tailings, holes or depressions, repair areas, storage areas, processing areas, shipping areas, and other areas upon which are sited structures, facilities, or other property or material on the surface, resulting from or incident to those activities.

Covol describe their activity as follows:

The facility will utilize Terra's patented equipment to beneficiate out-of-specification run-of-mine coal by reducing ash, pyretic sulfur and mercury through a dry air separation process. The facility is designed to process approximately 500,000 tons of run-of-mine coal per year. This facility will be located southeast of the Savage Terminal.

High ash, high sulfur coal will be trucked to the facility from several sources, including mines, in Carbon and Emery counties. Covol will purchase the coal directly from mining companies or enter into a tolling agreement to clean the out-of-specification coal. The various coals will be unloaded via a drive over truck dump and segregated into storage piles by radial stacker.

The selected coal to be cleaned will be removed from the appropriate coal storage pile by front end loader and dumped into a receiving hopper. The coal will be conveyed to a vibrating screen and crusher unit. The screened and crushed coal is then conveyed to three (3) air jig cleaning units, according to size. The air jig units are complete with bag houses for

particulate collection. This unit separates the ash and coal using pulsating air. The cleaned coal is then conveyed to a storage silo or several coal storage piles. This cleaned coal can be blended to meet specifications for ash, sulfur, mercury content and BTU values. The beneficiated coal is then loaded into trucks via the drive under silo or loading hopper feed by a front - end loader. The final product is shipped to a consumer, power plant, synfuel plant or coal load out terminal via truck. The by-product, ash and clay material, are collected from the air jig units and conveyed to a storage pile for future use.

This coal cleaning and blending facility is designed to process non-compliant waste coals that produces a customized coal fuel.

At first reading it would appear that Covol's proposed activity would fall under the chemical or physical processing of coal criteria found in the above definition and would require permitting. However, a closer look at the definition reveals that in order for the activity to be considered Coal Mining and Reclamation Operations it would have to be conducted "in connection with" a coal mine.

No definition of "in connection with" has been given since it is felt that each regulatory authority must have discretion in order to make valid decisions about the applicability of the performance standards of SMCRA in individual cases.

The preambles to Federal Rules 30 CFR parts 785 and 827 (November 22, 1988 Federal Register) provide important insight for how to determine if a processing plant is being operated in connection with a coal mine.

The following statements should be considered when determining whether a facility is operating "in connection with" a coal mine:

- 1) "OSM is only requiring regulatory authorities to extend their permit requirements as far into the stream of commerce as those activities over which mine operators and coal handlers who directly serve them, such as coal processors, have or could have control of operations."
- 2) The element of proximity is a valid consideration in determining whether a facility is regulated. (Activities at the site of a mine would be permitted.)
- 3) Coal preparation facilities which are being operated only in connection with another industrial facility, such as a power plant do not operate in connection with a mine and are not subject to regulation.
- 4) Does the facility have a useful life independent of the specific mine or mines which it serves?
- 5) Coal preparation facilities operated by retail sales dealers tend to be closely linked to end users and are generally not considered operating

in connection with a coal mine.

- 6) Functional or economical relationships with a mine should be considered when making an "in connection with" determination. (Does the facility receive a significant portion of their coal from a mine? Does the facility receive a significant portion of the output from a mine? Does the facility have an economic relationship with a mine?)

FINDINGS

- 1) Covol does not own, operate or control any coal mining operation.
- 2) Covol's facility is not located at the site of a mine.
- 3) The coal cleaning and blending facility produces a customized coal fuel that seems to be more closely associated to an industrial or end use than to mining.
- 4) Covol's facility would not service any specific mine but could receive its raw materials from various sources and operate independent of any given mine.
- 5) Covol would be acting similar to a retail sales dealer by purchasing "waste coal" from various entities and then marketing and selling their end product under the Covol name. However, in the case of PacifiCorp, the coal has a "tolling fee" for processing, which means that Covol never bought the coal and PacifiCorp maintained ownership. The Division will require further information about this "tolling fee" agreement prior to the final finding being issued.
- 6) There does not appear to be a functional or economic tie between Covol and any given mine. Covol indicates in the July 13, 2004 letter that their plant is not directly associated with mining. Covol's process is not necessary for any of the mines to continue operating. Covol might receive a significant amount of their source material from a particular mine, but would not be tied to that mine. The raw material could come from a variety of different sources.

Page 5
Air Processing Facility
August 5, 2004

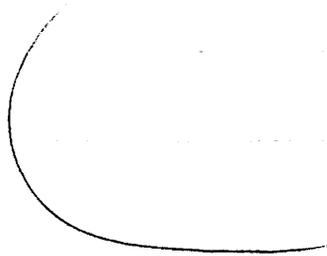
CONCLUSION

The proposed Covol activity is not being done "in connection with" a coal mine. As such, it would not require permitting under the Utah coal regulatory program since it is not considered coal mining and reclamation operations.

If the nature of Covol's activity changes, revised findings or other conclusions may be necessary. Should Covol become associated with a mine or involved in the ownership or control of a mining entity, or conduct mining activity such as extraction of coal from refuse piles, or excavation for the purpose of obtaining coal, they would certainly fall under the purview of the Coal Regulatory program.

The Division needs further information about the "tolling fee" agreement with PacifiCorp prior to issuing a final finding.

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**AGREEMENT TO PROCESS
HIGH ASH WASTE COAL INTO LOW ASH CLEAN COAL
TOLLING AGREEMENT**

The parties to this Tolling Agreement ("Agreement") to process high ash run of mine coal from PacifiCorp's Deer Creek mine ("Raw Coal") into low ash coal ("Clean Coal"), which is dated for reference purposes January 25, 2005, ("Effective Date") are: PACIFICORP, an Oregon corporation ("PacifiCorp"); and COVOL ENGINEERED FUELS LC a Utah corporation ("COVOL").

This is an Agreement by COVOL to process PacifiCorp's Raw Coal into Clean Coal as specified by PacifiCorp at COVOL's processing facility (the "Facility") located in Carbon County, Utah. Subject to the terms and conditions of this Agreement, COVOL agrees to process Raw Coal so provided, and PacifiCorp agrees to pay for such processing services as set forth below.

The parties agree as follows:

1. Term.

This Agreement shall be effective on the Effective Date and shall remain in effect until September 30, 2006, unless earlier terminated by PacifiCorp pursuant to Section 10 below. This Agreement may be extended at PacifiCorp's sole option for successive six (6) month periods through December 31, 2008. In the event PacifiCorp desires to extend the term of this Agreement for any additional six month period, PacifiCorp shall provide written notice to COVOL no later than thirty (30) days prior to the expiration of the current period in effect. For example, PacifiCorp shall provide an extension notice no later than September 1, 2006 if PacifiCorp desires to extend this agreement for a six month period beginning October 1, 2006 through March 31, 2007, and by March 1, 2007 if PacifiCorp has exercised the first extension option and desires to extend this Agreement for an additional six month period beginning April 1, 2007 through September 30, 2007.

2. Quantity.

PacifiCorp has approximately 140,000 tons of high ash Deer Creek coal stockpiled at Hunter Plant that PacifiCorp is willing to commit to the initial testing of this coal cleaning process subject to Section 10 below and any unanticipated needs at PacifiCorp's Utah generating plants. In addition, during the term of this Agreement, PacifiCorp at its discretion and based upon the availability of Raw Coal shall have the right to deliver to the Facility up to 25,000 tons of Raw Coal each calendar month. The parties shall agree to work with each other if the monthly quantities vary significantly from the ratable monthly volume of 25,000 tons of Raw Coal.

3. Raw Coal Delivery.

- (a) Throughout the Term, as provided for by the Raw Coal delivery provisions set forth below, PacifiCorp will deliver Raw Coal to the Facility for consignment to COVOL. Raw

Coal deliveries will be pursuant to schedules agreed to by COVOL and PacifiCorp and in accordance with the shipping requirements specified between the parties. The costs of unloading, storage, and subsequent loading at the Facility will be borne by COVOL and are included in the tolling fee. COVOL shall not use or process any Raw Coal provided by PacifiCorp hereunder for any purpose other than requested by PacifiCorp in accordance with the terms of this Agreement.

- (b) If PacifiCorp has Raw Coal stored at the Facility, PacifiCorp may use such Raw Coal to fulfill its supply obligations as determined by PacifiCorp.
- (c) Title to all inventories of Raw Coal will at all times remain vested in PacifiCorp and not COVOL, and COVOL shall use and process such Raw Coal in strict accordance with the provisions of this Agreement. Solely in order to protect PacifiCorp's property interest in all Raw Coal and Clean Coal to which this Agreement relates against any claim made in respect thereof by a creditor of COVOL or others claiming through COVOL, COVOL grants to PacifiCorp a security interest in all of COVOL's right, title and interest in Raw Coal delivered by PacifiCorp to the Facility, all work-in-process and all Clean Coal now or hereafter produced for PacifiCorp, wherever located, and all proceeds thereof (collectively, the Collateral), to secure performance of all obligations of COVOL to PacifiCorp, which security interest shall be prior to all other security interests in the Collateral. The parties agree that PacifiCorp shall have the right to file any financing statement as PacifiCorp in good faith determines are necessary or desirable to evidence COVOL's status as a consignee with respect to Raw Coal delivered by PacifiCorp and with respect to Clean Coal and work-in-process, and to evidence PacifiCorp's status as a secured party with respect to the Collateral.

4. Raw Coal Supply.

Tolling.

COVOL will operate its Facility to process Raw Coal delivered from PacifiCorp into Clean Coal in accordance with the coal quality requirements specified by PacifiCorp. Subject to COVOL meeting the quality requirements of Section 9(b), PacifiCorp will pay to COVOL a tolling fee for each ton of Raw Coal processed into a ton of Clean Coal.

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COVOL shall process the Raw Coal tonnage delivered by PacifiCorp for tolling under this Agreement.

5. Tolling Fee.

The tolling fee to be paid by PacifiCorp to COVOL [REDACTED] processed into Clean Coal tons through the Facility. The tolling fee includes all costs of coal unloading, coal handling, coal storage, coal processing and clean coal loaded into coal trucks provided by PacifiCorp per designated shipment schedules as determined by PacifiCorp. The tolling fee includes the cost of all Governmental Impositions in effect as of the Effective Date of this Agreement. "Governmental Impositions" means any local, state, or federal condition, rule, law or regulations or change which takes effect after the Effective Date of this Agreement which increases or decreases the cost of processing the Raw Coal into Clean Coal as described under this Agreement. [REDACTED]

6. Delivery, Loading and Scheduling.

- (a) The Facility located in Price, Utah shall be open to receive deliveries of Raw Coal five (5) days a week (Monday — Friday) from 7:00 a.m. until 4:00 p.m. The parties may mutually agree, from time to time, to modify such hours and days scheduled for delivery.
- (b) Processed Clean Coal shall be loaded into PacifiCorp's contracted coal trucks at the Facility five (5) days a week (Monday - Friday) from 7:00 a.m. until 4:00 p.m. The parties may mutually agree, from time to time, to modify such hours and days scheduled for loading. Unless otherwise agreed, all trucks shall be loaded by COVOL at the Facility in a timely manner. PacifiCorp's contracted trucking company's employees, drivers, etc. shall at all times comply with COVOL's personnel, safety rules, minimum insurance requirements and loading procedures which will be provided in writing to PacifiCorp.

7. Shipment Schedules.

Both parties shall provide estimated monthly shipment and processing schedules for both the Raw Coal as well as Clean Coal tonnage volumes. Shipment and processing schedules shall be sent according to Section 23 Notices, of this Agreement.

8. Coal Weighing.

The Deer Creek coal stockpiled at the Hunter Plant shall be weighed by certified platform scales at the Hunter Plant prior to delivery to the Facility. Raw Coal tons delivered to the Facility from the Deer Creek Mine shall be weighed by certified platform truck scales at the Huntington Plant. The scales shall be tested and certified annually. Clean Coal tons

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processed and loaded at the Facility shall be weighed by certified platform truck scales at the point of destination as determined by PacifiCorp i.e., Carbon, Hunter, Huntington plants and or Savage Coal Terminal. The scales shall be tested and certified annually. Tonnage of Raw Coal processed into Clean Coal shall be based on COVOL's belt scales. Processed Raw Coal shall never exceed the tonnage weights of Raw Coal delivered to the Facility.

9. Coal Quality.

(a) Raw Coal Quality.

The Raw Coal delivered hereunder shall be substantially free from impurities including tramp metal and mine debris and shall conform to the following specifications on an "as received" basis based on a monthly weighted average period. The typical specifications shall mean the weighted-average value of the appropriate quality component, on an as received basis, for all shipments during a calendar month. As used herein, the term "shipment" shall mean the aggregate of the truckloads that are loaded on any one-day. The typical quality of Raw Coal supplied to Covol hereunder shall be as follows:

Deer Creek
Raw Coal
Btu/lb.
Moisture
Ash
Sulfur

Range
As Received



The Raw Coal as received shall be sized to a nominal 2"x 0". PacifiCorp makes no other quality representations, warranties or assurances. Raw Coal delivered to the Facility shall be sampled manually at the Facility by a mutually agreed upon method. The samples representing each daily shipment shall be prepared at PacifiCorp's Central Fuels Lab ("CFL"). Three splits will be prepared, one of which will be analyzed for a short proximate analysis. Another split will be supplied to COVOL where it may be analyzed at an independent lab, and the remaining split will be retained by CFL in a sealed container for a period of sixty (60) days for possible use as a referee split if either party should dispute the results of the analysis. If it is determined that the referee split needs to be analyzed, such analysis shall be performed at a mutually agreed upon laboratory. The costs associated with analyzing the referee split shall be born equally by both parties. The costs associated with analyzing Raw Coal shall be borne by PacifiCorp. Each party shall be responsible for the costs of analysis of its' split. All analyses shall be performed in accordance with ASTM standards.

(b) Clean Coal Quality.

The Clean Coal processed hereunder shall be substantially free from impurities including tramp metal and mine debris and shall conform to the following specifications on an "as received" basis based on a monthly weighted average period. The typical specifications shall mean the weighted average value of the appropriate quality component, on an as

received basis, for all shipments during a calendar month. As used herein, the term "shipment" shall mean the aggregate of the truckloads that are loaded on any one-day. The typical quality of Clean Coal processed and supplied by COVOL hereunder shall be as follows:

<u>Deer Creek Clean Coal</u>	<u>Minimum As Received</u>	<u>Max As Received</u>
Btu/lb.	[REDACTED]	[REDACTED]
Moisture	[REDACTED]	[REDACTED]
Ash	[REDACTED]	[REDACTED]
Sulfur	[REDACTED]	[REDACTED]

The Clean Coal as received shall be sized to a nominal 2"x 0". COVOL makes no other quality representations, warranties or assurances. Clean Coal loaded from the Facility shall be sampled manually at the Facility by a mutually agreed upon method. The samples representing each daily shipment shall be prepared at PacifiCorp's Central Fuels Lab ("CFL"). Three splits will be prepared, one of which will be analyzed for a short proximate analysis. Another split will be supplied to COVOL, where it may be analyzed by an independent lab, and the remaining split will be retained by CFL in a sealed container for a period of sixty (60) days for possible use as a referee split if either party should dispute the results of the analysis. If it is determined that the referee split needs to be analyzed, such analysis shall be performed at a mutually agreed upon laboratory. The costs associated with analyzing the referee split shall be born equally by both parties. The costs associated with analyzing Clean Coal shall be borne by COVOL. Each party shall be responsible for the costs of analysis of its' split. All analyses shall be performed in accordance with ASTM standards.

10. Early Termination.

If at any time during the term of this Agreement, PacifiCorp determines (1) that the Clean Coal delivered from COVOL causes coal handling problems and or significant coal consumption problems which in PacifiCorp's sole judgement adversely impacts electric generation at any of its' plants or the plants' abilities to burn the Clean Coal; and or (2) the Clean Coal recovery process is no longer economically viable to PacifiCorp based upon PacifiCorp's sole judgment, COVOL shall be notified of the problem and be given the opportunity to correct the problem. If COVOL is unable to correct the problem then PacifiCorp shall have the right to terminate this Agreement within thirty (30) days after providing written notification to COVOL outlining the reason(s) for the termination.

11. Facility Maintenance and Insurance.

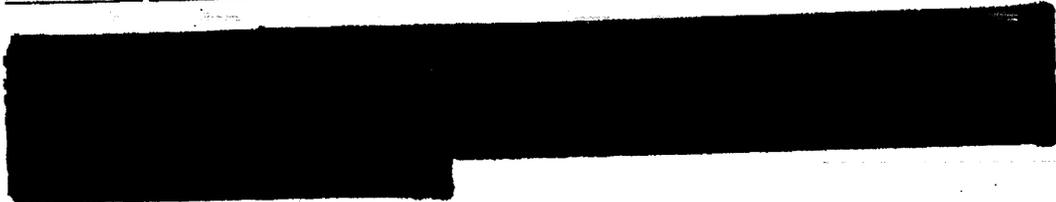
COVOL will maintain all risk casualty insurance in amounts sufficient to repair or replace any facilities damaged in an insured loss, and comprehensive general liability insurance covering liability for personal injury, death or property damage, with policy limits of not less than \$1,000,000 per occurrence and \$2,000,000 aggregate liability. All such policies shall name PacifiCorp as an insured, to the extent of it's insurable interests, shall provide that the insurer may not cancel or refuse to renew such policies without

providing PacifiCorp thirty (30) days prior written notice thereof and shall be in form and substance reasonably satisfactory to PacifiCorp. ..

PacifiCorp will certify to COVOL's insurance underwriter on request and from time to time the amount and provisions of its product liability insurance coverage applicable to products manufactured by COVOL. PacifiCorp agrees to cause COVOL to be named as an additional insured on such insurance, the additional premium, if any, to be paid by COVOL.

Headwaters Incorporated guarantees that any and all raw feedstock shall be returned to PacifiCorp, at no additional cost to PacifiCorp if COVOL is unable or unwilling to process the Raw Coal tons into Clean Coal tons.

12. Invoice and Payment.



13. Force Majeure.

A party's obligation under this Agreement shall be suspended in the event of a force majeure which could not reasonably have been avoided or which cannot reasonably be overcome by the exercise of due diligence by the party claiming the force majeure and which will prevent either party from performing its obligations under this Agreement. The term "force majeure", shall mean an act of God, lightening, storms, fire, flood, slide, explosion, strike, lockout, labor dispute, riot, insurrection, act of the public enemy, sabotage, embargo, blockage, war, breakdown of or damage to the coal mine, or equipment or facilities related to such mines, adverse geologic conditions which could not have been reasonably anticipated by a prudent miner, interruptions or breakdowns of the electrical power system serving COVOL or PacifiCorp facilities, the interruptions of scheduled transportation by reason of the occurrence which constitutes a force majeure under applicable transportation agreements, orders or acts of military or civil authority, and any other cause, whether or not of the same class or kind enumerated above, or otherwise which is not reasonably within the control of the party claiming the force majeure. Acts of civil authority, as that term is used herein, shall include any act or order of any court and any act or failure or refusal to act of any governmental agency or officer charged with the enforcement or administration of any applicable law, rule, regulation or lease, including the effective denial to either party of any necessary permit, license, lease, lease right or approval, which effectively prohibits the operation, in whole or in part, of the coal mines and equipment or facilities related thereto, or the facilities of any rail carrier, terminal or shipping company.

A party claiming force majeure shall promptly give the other party written notice of such force majeure and an estimate of the extent and duration thereof. Upon giving such

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notice, the obligation of the party claiming force majeure shall be suspended to the extent necessary by such force majeure and during the continuance of such force majeure or its effects and the party claiming the force majeure shall incur no liability by reason of its failure to perform the obligations so suspended, provided that the disabling effects of such force majeure shall be eliminated by the party claiming force majeure as soon as and to the extent reasonably possible. The obligation to eliminate the disabling effects of force majeure to the extent reasonably possible shall not be construed to impose an obligation to make significant capital expenditures, and the manner in which labor difficulties shall be handled shall be entirely within the discretion of the party concerned. Unless otherwise agreed and in lieu of any proration requirement under the Utah Uniform Commercial Code, neither party shall be entitled to any pro rata share of the available supply of coal. The parties shall use their best efforts to make up force majeure tons on a mutually agreeable schedule.

14. Limitation of Liability.

A party's liability for any cause of action arising out of this Agreement between the parties, whether or not arising out of negligence, is expressly limited to direct monetary damages. Notwithstanding any provision of the Agreement between the parties, PacifiCorp and COVOL shall in no event be liable to the other for special, consequential, exemplary or punitive damages, except as those damages relate to either party's obligation to indemnify the other against third-party claims.

15. Indemnification.

PacifiCorp shall not be liable for and COVOL agrees to indemnify and hold PacifiCorp and its affiliates, officers, directors, employees and agents harmless against any and all losses, expenses, claims or causes of action of every kind and character, directly or indirectly resulting from or arising out of the operation of the Facility or COVOL's acts or omissions under this Agreement on account of damage to and/or loss of any property or on account of injury to or death of any person or persons. COVOL shall defend each claim asserted and suit brought involving any matter as to which PacifiCorp is to be indemnified hereunder and shall pay all costs, expenses and attorneys' fees incidental thereto and all judgments resulting therefrom; and PacifiCorp shall have the right, at its option, to participate in the defense of each such suit or proceeding without relieving COVOL of any obligation hereunder.

COVOL shall not be liable for and PacifiCorp agrees to indemnify and hold COVOL and its affiliates, officers, directors, employees and agents harmless against any and all losses, expenses, claims or causes of action of every kind and character directly or indirectly resulting from or arising out of PacifiCorp's acts or omissions under this Agreement on account of damage to and/or loss of any property or on account of injury to or death of any person or persons. PacifiCorp shall defend each claim asserted and suit brought involving any matter as to which COVOL is to be indemnified hereunder and shall pay all costs, expenses and attorneys' fees incidental thereto and all judgments resulting therefrom; and COVOL shall have the right, at its option, to participate in the defense of each such suit or proceeding without relieving PacifiCorp of any obligation hereunder.

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16. Entire Agreement.

This Agreement constitutes the entire Agreement between PacifiCorp, and COVOL with respect to the subject matter hereof. Any statement, representation, understanding, term or condition, whether written or oral, not expressly set forth herein, forms no part of this Agreement and is not binding upon either party. This Agreement supersedes and replaces any prior Agreement or understanding between PacifiCorp and COVOL, whether written or oral, regarding the subject matter hereof, and any such Agreement or understanding is void and without further force or effect.

17. Applicable Law.

This Agreement shall be governed by and construed in accordance with the laws of the State of Utah.

18. Assignment.

This Agreement may not be assigned wholly or in part by any party without the written consent of the other parties, which consent shall not be unreasonably withheld.

19. Compliance with Laws:

COVOL agrees to operate the Facility and all unloading, loading and all other activities at the Facility in material compliance with all United States, state and local laws, including without limitation all laws relating to environmental protection, pollution or contamination.

PacifiCorp agrees not to deliver any raw feedstock materials that do not comply with all environmental laws.

20. Amendments.

This Agreement may not be amended, supplemented, or otherwise modified except by written instrument making reference hereto and signed by PacifiCorp and COVOL.

21. Confidentiality.

Except when required for regulatory reporting by law, by governmental or judicial order, or pursuant to regulatory audit request, the parties shall not reveal the terms of this Agreement and shall protect the confidentiality of the information developed in connection with this Agreement; provided, however, that neither party will be precluded from revealing such information in obtaining or attempting to obtain financing or in filing reports and information with the Security and Exchange Commission, or the appropriate governmental authorities, or making public information required thereby, or when advised by legal counsel that such disclosure is required. When required, the parties may

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also submit information to consultants and contractors performing work related to this Agreement who agree in writing to protect the confidentiality of such information.

22. Documentation and Audit Rights.

PacifiCorp and COVOL shall maintain all records and accounts pertaining to quantities, quality analyses and source of all coal supplied under this Agreement for a period lasting through the term of this Agreement and for two (2) years thereafter. PacifiCorp and COVOL shall have the right, at no additional expenses to either party, to audit, copy and inspect such records and accounts at any reasonable time upon reasonable notice during the term of the Agreement and for two (2) years thereafter.

23. Notices

Any required Notice to be given to either party shall be given by U.S. mail, electronic mail (telex) and/or overnight delivery express service as follows:

If to PacifiCorp:

PacifiCorp
201 South Main St. Suite 2100
Attn: General Manager - Fuels
Salt Lake City, Utah 84111
Telephone: (801) 220-4608
Fax: (801) 220-4578

If to Covol Engineered Fuels LC:

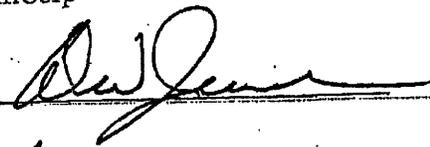
Covol Engineered Fuels LC.
10653 S. Riverfront Parkway Suite 300
Attn: Keith Thompson, Manager
South Jordan, Utah 84095
Telephone: 801-984-9400
Fax: 801-984-9460

24. Attorneys Fees.

In the event litigation involving or relating to this Agreement is commenced by any party, the prevailing party in such litigation shall be entitled to recover from the other parties its reasonable attorneys fees and costs incurred in connection with such litigation and any appeal therefrom.

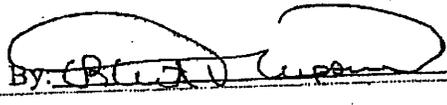
IN WITNESS WHEREOF, the parties have executed this Agreement by their respective, duly authorized representatives effective as of the date first written above.

PacifiCorp

By: 

Its: Assistant Vice President

Covol Engineered Fuels LC

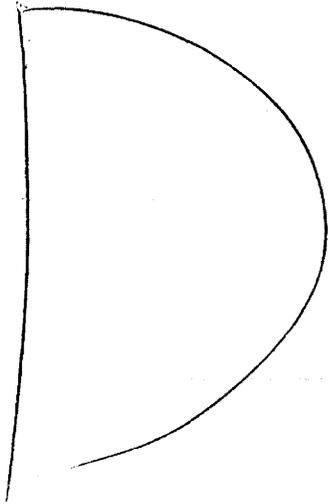
By: 

Its: Vice President

Headwaters Incorporated
(For Purposes of Paragraph 11)

By: 

Its: President HES



**AGREEMENT TO PROCESS
HIGH ASH WASTE COAL INTO LOW ASH CLEAN COAL
TOLLING AGREEMENT**

The parties to this Tolling Agreement (this "Agreement") to process high ash run of mine coal ("Raw Coal") into low ash coal ("Clean Coal"), which is dated July 19, 2005 (the "Effective Date") are: Commonwealth Coal Services, Inc., a Virginia corporation ("COMMONWEALTH"); and Covol Engineered Fuels, LC, a Utah limited liability company ("COVOL").

This is an Agreement by COVOL to process COMMONWEALTH's Raw Coal into Clean Coal at COVOL's processing facility (the "Facility") located in Carbon County, Utah. Subject to the terms and conditions of this Agreement, COVOL agrees to process Raw Coal so provided, and COMMONWEALTH agrees to pay for such processing services as set forth below.

The parties agree as follows:

1. Term.

This Agreement shall be effective on the Effective Date and shall remain in effect until one year after the date on which COVOL first processes COMMONWEALTH'S coal through the Facility. This Agreement will be extended for successive one (1) year periods through September 30, 2010 unless either party provides written notice of termination to the other no later than thirty (30) days prior to the expiration of the current period in effect.

2. Quantity.

COMMONWEALTH at its discretion and based upon the availability of Raw Coal shall have the right to deliver to the Facility up to 25,000 tons of Raw Coal each calendar month. The parties shall agree to work with each other if the monthly quantities vary significantly from the ratable monthly volume of 25,000 tons of Raw Coal.

3. Raw Coal Delivery.

- (a) Throughout the Term, as provided for by the Raw Coal delivery provisions set forth below, COMMONWEALTH will deliver Raw Coal to the Facility for consignment to COVOL. Raw Coal deliveries will be pursuant to schedules agreed to by COVOL and COMMONWEALTH and in accordance with the shipping requirements specified between the parties. COVOL shall not use or process any Raw Coal provided by COMMONWEALTH hereunder for any purpose other than requested by COMMONWEALTH in accordance with the terms of this Agreement.
- (b) Title to all inventories of Raw Coal will at all times remain vested in COMMONWEALTH and not COVOL, and COVOL shall use and process such Raw Coal in strict accordance with the provisions of this Agreement.

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- (c) COMMONWEALTH shall have title to all waste and refuse material that is a by-product of the cleaning process of the Raw Coal. COMMONWEALTH shall process, recycle or dispose of the same in accordance with all applicable laws. The costs of unloading, storage, and subsequent loading refuse material at the Facility will be borne by COVOL and are included in the tolling fee. Covol shall have the right of first refusal to the waste and refuse material at no charge in which case title to the waste and refuse material will pass to Covol.

4. Raw Coal Supply.

Tolling.

COVOL will operate its Facility to process Raw Coal delivered from COMMONWEALTH into Clean Coal in accordance with the coal quality requirements specified by COMMONWEALTH. Subject to COVOL meeting the quality requirements of Section 9(b), COMMONWEALTH will pay to COVOL a tolling fee for each ton of Raw Coal processed into Clean Coal. COVOL shall process the Raw Coal tonnage delivered by COMMONWEALTH for tolling under this Agreement.

5. Tolling Fee.

The tolling fee to be paid by COMMONWEALTH to COVOL is [REDACTED] processed into Clean Coal tons through the Facility [REDACTED]

[REDACTED] The tolling fee includes all costs of coal unloading, coal handling, coal storage, coal processing, and clean coal and processed by-product loaded into coal trucks provided by COMMONWEALTH per designated shipment schedules as determined by COMMONWEALTH. In the event that the recovery percentage rate of Clean Coal as compared to the Raw Coal delivered to the Facility for the purpose of processing is determined [REDACTED]

6. Delivery, Loading and Scheduling.

- (a) The Facility located in Wellington, Utah shall be open to receive deliveries of Raw Coal five (5) days a week (Monday — Friday) from 7:00 a.m. until 4:00 p.m. The parties may mutually agree, from time to time, to modify such hours and days scheduled for delivery.
- (b) Processed Clean Coal shall be loaded into COMMONWEALTH's contracted coal trucks at the Facility five (5) days a week (Monday - Friday) from 7:00 a.m. until 4:00 p.m. The parties may mutually agree, from time to time, to modify such hours and days scheduled for loading. Unless otherwise agreed, all trucks shall be loaded by COVOL at the Facility in a timely manner. COMMONWEALTH's contracted trucking COMMONWEALTH's employees, drivers, etc. shall at all times comply with COVOL's

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personnel, safety rules, minimum insurance requirements and loading procedures which will be provided in writing to COMMONWEALTH.

7. Shipment Schedules.

Both parties shall provide estimated monthly shipment and processing schedules for both the Raw Coal as well as Clean Coal tonnage volumes. Shipment and processing schedules shall be sent according to Section 23 Notices, of this Agreement.

8. Coal Weighing.

Raw Coal tons delivered to the Facility shall be weighed by certified platform truck scales at the Coal Cleaning Facility. The scales shall be tested and certified annually. Clean Coal tons processed and loaded at the Facility shall be weighed by certified platform truck scales at the Coal Cleaning Facility. Recovery rate of Raw Coal processed into Clean Coal shall be based on COVOL's belt scales. Processed Raw Coal shall never exceed the tonnage weights of Raw Coal delivered to the Facility.

9. Coal Quality.

(a) Raw Coal Quality.

The Raw Coal delivered hereunder shall be substantially free from impurities including tramp metal and mine debris and shall conform to the following specifications on an "as received" basis based on a monthly weighted average period. The specifications shall mean the weighted-average value of the appropriate quality component, on an as received basis, for all shipments during a calendar month. As used herein, the term "shipment" shall mean the aggregate of the truckloads that are loaded on any one-day. The quality of Raw Coal supplied to Covol hereunder shall be as follows:

MINE	Range	
<u>Raw Coal</u>	<u>As Received</u>	
Btu/lb.	[REDACTED]	Moisture
[REDACTED]	[REDACTED]	
Ash	[REDACTED]	
Sulfur	[REDACTED]	

The Raw Coal as received shall be sized to a nominal 2"x 0". COMMONWEALTH makes no other quality representations, warranties or assurances. Raw Coal delivered to the Facility shall be sampled manually at the Facility by a mutually agreed upon method. The samples representing each daily shipment shall be prepared and analyzed at mutually agreed upon independent lab ("Lab"). Three splits will be prepared, one of which will be analyzed for a short proximate analysis. Another split will be supplied to COVOL, and the remaining split will be sent to COMMONWEALTH. If it is determined that a referee split needs to be analyzed, such analysis shall be performed at a mutually agreed upon laboratory. Each party shall be responsible for all costs to analyze its own split. The costs

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associated with analyzing the referee split shall be born equally by the parties. All analyses shall be performed in accordance with ASTM standards.

(b) Clean Coal Quality.

The Clean Coal processed hereunder shall conform to the following specifications on an "as received" basis based on a monthly weighted average period. The specifications shall mean the weighted average value of the appropriate quality component, on an as received basis, for all shipments during a calendar month. As used herein, the term "shipment" shall mean the aggregate of the truckloads that are loaded on any one-day. The quality of Clean Coal processed and supplied by COVOL hereunder shall be as follows:

<u>MINE</u> <u>Clean Coal</u> Btu/lb.	<u>Minimum</u> <u>As Received</u>	<u>Max</u> <u>As Received</u>
Moisture	[REDACTED]	[REDACTED]
Ash	[REDACTED]	[REDACTED]
Sulfur	[REDACTED]	[REDACTED]

The Clean Coal as received shall be sized to a nominal 2"x 0". COVOL makes no other quality representations, warranties or assurances. Clean Coal loaded from the Facility shall be sampled manually at the Facility by a mutually agreed upon method. The samples representing each daily shipment shall be prepared at the Lab. Three splits will be prepared, one of which will be analyzed for a short proximate analysis. Another split will be supplied to COVOL, and the remaining split will be sent to COMMONWEALTH. If it is determined that a referee split needs to be analyzed, such analysis shall be performed at a mutually agreed upon laboratory. Each party shall be responsible for all costs to analyze its own split. The costs associated with analyzing the referee split shall be born equally by the parties. All analyses shall be performed in accordance with ASTM standards.

10 Early Termination.

If at any time during the term of this Agreement, COMMONWEALTH determines (1) that the Clean Coal delivered from COVOL causes coal handling problems and or significant coal consumption problems which in COMMONWEALTH's judgment adversely impacts the ability to burn the Clean Coal; and or (2) the Clean Coal recovery process is less than 30%, COVOL shall be notified of the problem and be given the opportunity to correct the problem. If COVOL is unable to correct the problem then COMMONWEALTH shall have the right to terminate this Agreement within thirty (30) days after providing written notification to COVOL outlining the reason(s) for the termination

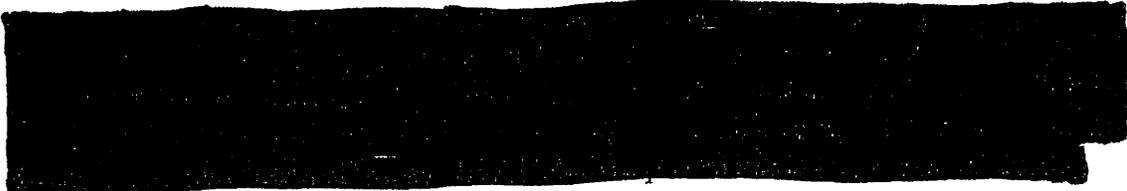
11. Insurance.

COVOL will maintain commercially reasonable insurance levels for liability and damage.

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COVOL will certify to COMMONWEALTH'S insurance underwriter on request and from time to time the amount and provisions of its product liability insurance coverage applicable to products manufactured by COVOL. COVOL agrees to cause COMMONWEALTH to be named as an additional insured on such insurance.

12. Invoice and Payment.



13. Force Majeure.

A party's obligation under this Agreement shall be suspended in the event of a force majeure which could not reasonably have been avoided or which cannot reasonably be overcome by the exercise of due diligence by the party claiming the force majeure and which will prevent either party from performing its obligations under this Agreement. The term "force majeure", shall mean an act of God, lightning, storms, fire, flood, slide, explosion, strike, lockout, labor dispute, riot, insurrection, act of the public enemy, sabotage, embargo, blockage, war, breakdown of or damage to the coal mine, or equipment or facilities use to store or process COMMONWEALTH'S coals, adverse geologic conditions which could not have been reasonably anticipated by a prudent miner, interruptions or breakdowns of the electrical power system serving COVOL or COMMONWEALTH facilities, the interruptions of scheduled transportation by reason of the occurrence which constitutes a force majeure under applicable transportation agreements, orders or acts of military or civil authority, and any other cause, whether or not of the same class or kind enumerated above, or otherwise which is not reasonably within the control of the party claiming the force majeure. Acts of civil authority, as that term is used herein, shall include any act or order of any court and any act or failure or refusal to act of any governmental agency or officer charged with the enforcement or administration of any applicable law, rule, regulation or lease, including the effective denial to either party of any necessary permit, license, lease, lease right or approval, which effectively prohibits the operation, in whole or in part, of the coal mines and equipment or facilities used to store or process COMMONWEALTH'S coal, or the facilities of any rail carrier, terminal or shipping company serving COMMONWEALTH.

A party claiming force majeure shall promptly give the other party written notice of such force majeure and an estimate of the extent and duration thereof. Upon giving such notice, the obligation of the party claiming force majeure shall be suspended to the extent necessary by such force majeure and during the continuance of such force majeure or its effects and the party claiming the force majeure shall incur no liability by reason of its failure to perform the obligations so suspended, provided that the disabling effects of such force majeure shall be eliminated by the party claiming force majeure as soon as and to the extent reasonably possible. The obligation to eliminate the disabling effects of

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force majeure to the extent reasonably possible shall not be construed to impose an obligation to make significant capital expenditures, and the manner in which labor difficulties shall be handled shall be entirely within the discretion of the party concerned. Unless otherwise agreed and in lieu of any proration requirement under the Utah Uniform Commercial Code, neither party shall be entitled to any pro rata share of the available supply of coal. The parties shall use their best efforts to make up force majeure tons on a mutually agreeable schedule.

14. Limitation of Liability.

A party's liability for any cause of action arising out of this Agreement between the parties, whether or not arising out of negligence, is expressly limited to direct monetary damages, which in COVOL's case shall be limited to the cost of returning any Raw Coal and/or Clean Coal to COMMONWEALTH. NOTWITHSTANDING ANYTHING TO THE CONTRARY HEREIN, EXCEPT FOR THIRD-PARTY DAMAGES ARISING AS A RESULT OF INDEMNITY UNDER SECTION 15 BELOW, NEITHER PARTY SHALL BE LIABLE TO THE OTHER FOR SPECIAL, CONSEQUENTIAL, EXEMPLARY OR PUNITIVE DAMAGES.

15. Indemnification.

COMMONWEALTH shall not be liable for and COVOL agrees to indemnify and hold COMMONWEALTH and its affiliates, officers, directors, employees and agents harmless against any and all losses, expenses, claims or causes of action of every kind and character, directly or indirectly resulting from or arising out of the operation of the Facility or COVOL's negligent acts or omissions under this Agreement on account of damage to and/or loss of any property or on account of injury to or death of any person or persons. COVOL shall defend each claim asserted and suit brought involving any matter as to which COMMONWEALTH is to be indemnified hereunder and shall pay all costs, expenses and attorneys' fees incidental thereto and all judgments resulting therefrom; and COMMONWEALTH shall have the right, at its option, to participate in the defense of each such suit or proceeding without relieving COVOL of any obligation hereunder.

COVOL shall not be liable for and COMMONWEALTH agrees to indemnify and hold COVOL and its affiliates, officers, directors, employees and agents harmless against any and all losses, expenses, claims or causes of action of every kind and character directly or indirectly resulting from or arising out of COMMONWEALTH's negligent acts or omissions under this Agreement on account of damage to and/or loss of any property or on account of injury to or death of any person or persons. COMMONWEALTH shall defend each claim asserted and suit brought involving any matter as to which COVOL is to be indemnified hereunder and shall pay all costs, expenses and attorneys' fees incidental thereto and all judgments resulting therefrom; and COVOL shall have the right, at its option, to participate in the defense of each such suit or proceeding without relieving COMMONWEALTH of any obligation hereunder.

16. Entire Agreement.

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This Agreement constitutes the entire Agreement between COMMONWEALTH, and COVOL with respect to the subject matter hereof. Any statement, representation, understanding, term or condition, whether written or oral, not expressly set forth herein, forms no part of this Agreement and is not binding upon either party. This Agreement supersedes and replaces any prior Agreement or understanding between COMMONWEALTH and COVOL, whether written or oral, regarding the subject matter hereof, and any such Agreement or understanding is void and without further force or effect.

17. Applicable Law.

This Agreement shall be governed by and construed in accordance with the laws of the State of Utah.

18. Assignment.

This Agreement may not be assigned wholly or in part by any party without the written consent of the other parties, which consent shall not be unreasonably withheld.

19. Compliance with Laws:

COVOL agrees to operate the Facility and all unloading, loading and all other activities at the Facility in material compliance with all federal, state and local laws.

COMMONWEALTH agrees not to deliver any raw feedstock materials that do not comply with all environmental laws.

20. Amendments.

This Agreement may not be amended, supplemented, or otherwise modified except by written instrument making reference hereto and signed by COMMONWEALTH and COVOL.

21. Confidentiality.

The parties agree that this Agreement shall be governed by the Confidentiality Agreement executed by the parties on _____, 200_ (the Confidentiality Agreement"), and each and every term of the Confidentiality Agreement are incorporated herein by reference as fully as if repeated verbatim in the Agreement.

22. Documentation and Audit Rights.

COMMONWEALTH and COVOL shall maintain all records and accounts pertaining to quantities, quality analyses and source of all coal supplied under this Agreement for a period lasting through the term of this Agreement and for two (2) years thereafter. COMMONWEALTH and COVOL shall have the right, at no additional expenses to

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either party, to audit, copy and inspect such records and accounts at any reasonable time upon reasonable notice during the term of the Agreement and for two (2) years thereafter.

23. Notices

Any required Notice to be given to either party shall be given by U.S. mail, electronic mail (telefax) and/or overnight delivery express service as follows:

If to COMMONWEALTH:

Commonwealth Coal Services, Inc.
5413 Patterson Ave., Suite 200
Attn: Wallace Taylor
Richmond, Virginia 23226
Telephone: 804-282-9833
Fax: 804-282-9836

If to COVOL:

Covol Engineered Fuels, LC
10653 S. Riverfront Parkway Suite 300
Attn: Keith Thompson
South Jordan, Utah 84095
Telephone: 801-984-9400
Fax: 801-984-9460

24. Attorneys Fees.

In the event litigation involving or relating to this Agreement is commenced by any party, the prevailing party in such litigation shall be entitled to recover from the other parties its reasonable attorneys fees and costs incurred in connection with such litigation and any appeal therefrom.

IN WITNESS WHEREOF, the parties have executed this Agreement by their respective, duly authorized representatives effective as of the date first written above.

Commonwealth Coal Services, Inc.



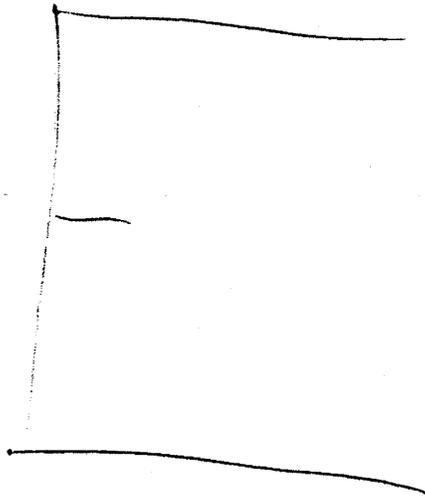
Robert H. Scott
President

Covol Engineered Fuels, LC



R. Keith Thompson
Vice President

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State of Utah

Department of
Natural Resources

MICHAEL R. STYLER
Executive Director

Division of
Oil, Gas & Mining

JOHN R. BAZA
Division Director

JON M. HUNTSMAN, JR.
Governor

GARY R. HERBERT
Lieutenant Governor

March 17, 2006

Keith Thompson, Vice President
Covol Engineered Fuels, LC
10653 South River Front Parkway, Suite 300
South Jordan, Utah 84095

Subject: Determination to Permit Under the Surface Mining Control and
Reclamation Act, C/007/0046. Outgoing File

Dear Mr. Thompson:

As we discussed on last December 20, 2005, the Division of Oil, Gas and Mining ("OGM") has made a determination that the Surface Mining Control and Reclamation Act applies to the Wellington Utah Headwaters Energy Services coal processing facility. Enclosed, please find a copy of the OGM Finding that Covol/Headwaters must obtain a permit. I suggest that we meet in the near future to set the timeline for posting a bond and submitting an operation and reclamation plan. Please contact Pamela Grubaugh-Littig at (801) 538-5268 or pamgrubaughlittig@utah.gov.

Pursuant to Utah Code Ann. § 40-10-14 and Utah Administrative Code R645-300-200, an appeal may be made to OGM's Finding. Should you choose to appeal to the Board of Oil, Gas and Mining, please contact Ms. Julie Carter, Secretary to the Board, at juliecarter@utah.gov or at (801) 538-5277 for further instruction on the Board appeal process.

Sincerely,

Mary Ann Wright
Associate Director, Mining

Enclosure: Analysis memo
O:\007046.DTE\Mr Thompson.doc



State of Utah

**Department of
Natural Resources**

MICHAEL R. STYLER
Executive Director

**Division of
Oil, Gas & Mining**

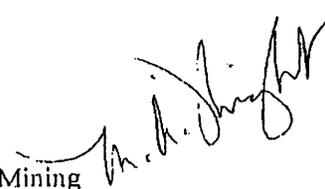
JOHN R. BAZA
Division Director

JON M. HUNTSMAN, JR.
Governor

GARY R. HERBERT
Lieutenant Governor

March 16, 2006

TO: File

FROM: Mary Ann Wright, Associate Director, Mining 

RE: Covol Engineered Fuels, L.C., Wellington, Utah

INTRODUCTION

Covol Engineered Fuels, L.C. ("Covol") plans to operate a coal processing plant in Carbon County, Utah. Covol will receive coal from coal mines and coal handlers and send the coal through a dry air separation process to separate the coal from its impurities. Covol is currently under contract to process coal from two coal handlers and return the beneficiated coal to the handler. Covol intends to expand its business portfolio to purchase waste pile coal, add a chemical additive to the coal and reap the benefit of a federal tax credit for Synfuel production, and possibly sell NOx emission credits under the Clean Air Act. The Division of Oil, Gas & Mining ("Division") finds, based upon several inspections of the Covol plant and information provided by Covol, that Covol will engage in "coal mining and reclamation operations" and will therefore need to obtain a permit from the Division, in accordance with the Coal Mining and Reclamation Act, Utah Code Ann. § 40-10-1 et seq. ("Act") and the implementing regulations, Utah Administrative Code R645-100 et seq.

FACTS

On July 13, 2004, Covol sent the Division a proposal to install a 500,000 ton-per-year coal cleaning and blending facility in Carbon County, Utah. In its original proposal, Covol stated that it plans to:

utilize patented equipment to beneficiate out-of-specification run-of-mine coal by reducing ash, pyretic sulfur and mercury through a dry air separation process. . . . High ash, high sulfur coal will be delivered to a facility via truck from several sources, including mines, in Carbon and Emery counties. . . . The selected coal to be cleaned will be removed from the appropriate coal storage pile by front end loader and dumped into a receiving hopper. The coal will be conveyed to a vibrating screen and crusher unit. The screened and crushed coal is then conveyed to three (3) air jig cleaning units, according to size. The air jig units are complete with bag houses for particulate collection.

This unit separates the ash and coal using pulsating air. The cleaned coal is then conveyed to a storage silo or several clean coal storage piles. This cleaned coal can be blended to meet specifications for ash, sulfur, mercury content and BTU values. The beneficiated coal is then loaded into trucks via the drive under silo or loading hopper feed by a front-end loader.

Letter from R. Keith Thompson, Vice President, Covol, to Lowell P. Braxton, Director, Division of Oil, Gas & Mining (July 13, 2004). This process will produce a waste pile, which Covol intends to store for future use as "road base or fill" or return it to the mine of origin waste stockpile.

Furthermore, Covol intends to add a chemical additive to the cleaned coal, which it claims reduces NOx emissions. By adding a chemical additive, Covol intends to market the coal as a Synfuel product and take advantage of a federal tax credit for production of Synfuel. Covol also intends to market its NOx credits under the Clean Air Act. As of December 2005, Covol had taken no concrete steps toward realizing these business plans.

Currently Covol is storing 27,080 tons of coal from PacifiCorp's Deer Creek Mine. Covol has contracted with PacifiCorp to process approximately 25,000 tons of raw coal each month for a period of one year. Under this contract, PacifiCorp will retain ownership of the coal and Covol will receive a tolling fee for the processing. PacifiCorp retains the right to terminate the agreement based upon PacifiCorp's sole judgment that the "process is no longer economically viable to PacifiCorp." PacifiCorp has also entered another tolling agreement with Commonwealth Coal Services, Inc. ("Commonwealth") with similar provisions to the PacifiCorp Tolling Agreement.

To date, Covol has only contracted to process coal from PacifiCorp and Commonwealth. While it intends to expand its business portfolio, there is no indication if or when that would happen.

ANALYSIS

Covol will operate a "surface coal mining operation" because it will crush, screen, and separate the coal from its impurities, operate "in connection with" a coal mine, and because it is not located at the site of ultimate use. Therefore, Covol must obtain a permit from the Division. In Utah, it is unlawful to engage in "surface coal mining operations" without a permit from the Division. Utah Code Ann. § 40-10-9(1) (2004 & Supp. 2005). "Surface coal mining operations" means:

(a) Activities conducted on the surface of lands in connection with a surface coal mine . . . These activities include . . . in situ distillation or retorting, leaching or other chemical or physical processing . . .

(b) The area upon which the activities occur or where the activities disturb

the natural land surface. These areas shall also include any adjacent land the use of which is incidental to the activities, . . . or other property or materials on the surface from or incident to the activities.

Id. § 40-10-3(20). Based upon this definition, a person engages in "surface coal mining operations" if (A) the activity falls within one of the listed activities, and (B) the facility operates "in connection with a surface coal mine."

A. Covol's Activity Will Fall Within the Definition of "Surface Coal Mining Operation" Because it Will Engage in a "Chemical or Physical Processing" of Coal.

"Surface coal mining operations" includes "in situ distillation or retorting, leaching or other chemical or physical processing" of coal. Neither the Act, nor the implementing rules define "chemical or physical processing." Because the Utah Act closely patterns the federal Surface Mining Control and Reclamation Act ("SMCRA"), 30 U.S.C.A. § 1201 et seq., the Division looks to federal law, regulations, and interpretations to decipher the meaning of "chemical or physical processing." SMCRA does not provide a definition for "chemical or physical processing." However, the Office of Surface Mining Reclamation and Enforcement ("OSM"), the federal regulatory agency, has interpreted "chemical or physical processing" to include both those activities which separate coal from its impurities, and those activities "which do not separate coal from its impurities but which otherwise engage in physical or chemical processing (i.e.: crushing, screening, and sizing facilities)." Permanent Regulatory Programs; Definitions; Requirements for Permits for Special Categories of Mining; Coal Preparation Plants; Performance Standards, 52 Fed. Reg. 17,724, 17,725 (May 11, 1987)

Covol will crush, screen, and use a dry air separation process to separate the coal from its impurities. This activity falls within the definition of "chemical or physical processing" of coal, and therefore, Covol must obtain a permit if it also operates "in connection with" a coal mine.

B. Covol Will Operate "In Connection with a Surface Coal Mine."

Neither the Coal Mining and Reclamation Act nor the Utah Administrative Code defines "in connection with a surface coal mine." As noted above, the Utah Act closely follows SMCRA, and therefore, the Division looks to the federal law for the meaning of "in connection with" a coal mine. Neither Congress nor the OSM has defined "in connection with" a coal mine. However, the phrase has generated extensive discussion from the mining community because it is unclear from the language whether off-site facilities were categorically excluded from regulation.

To clarify that off-site facilities operating "in connection with" a coal mine are to be regulated, OSM and the Utah Board of Oil, Gas & Mining ("Board") adopted regulations requiring "any person who operates a coal preparation plant in

connection with a coal mine but outside the permit area for a specific mine" to obtain a permit. 30 C.F.R. § 785.21. See Utah Admin. Code R645-302-260. OSM refused to define "in connection with" because it believed that "[a]ny attempt to further define this phrase in a regulation would unduly restrict the discretion that regulatory authorities must have in order to make valid decisions about the applicability of the performance standards of SMCRA in individual cases." Permanent Regulatory Program; Coal Preparation Plants Not Located Within the Permit Area of a Mine, 53 Fed. Reg. 47,384, 47,385 (Nov. 22, 1988). Instead, OSM provided a non-exhaustive list of factors that would be appropriate to consider in making a determination of "in connection with" a coal mine. Those factors are:

1. Whether the facility receives a significant portion of its coal from a mine.
2. The economic relationship between the facility and a mine.
3. The functional relationship between the facility and the mine it services. Does the facility have a useful life independent of a mine?
4. Geographic proximity to a mine, although geographic proximity is not a determinative factor.
5. The degree of control a mine has over the processing operations.
6. Any other type of integration that exists between a facility and a mine.

Surface Coal Mining and Reclamation Operations; Permanent Regulatory Program; Support Facilities and Coal Preparation Plants, 48 Fed. Reg. at 20,393; Permanent Regulatory Program; Coal Preparation Plants Not Located Within the Permit Area of a Mine, 53 Fed. Reg. at 47,385-89. Also, a facility will not be considered "in connection with" a coal mine if such facility is located at the "site of ultimate coal use," unless the facility is also located at the site of the mine. Utah Admin. Code R645-302-260. See also PacifiCorp v. Office of Surface Mining Reclamation and Enforcement, 143 IBLA 237, 252 (1998) (holding coal processing plant located adjacent to power plant and delivering coal to power plant via conveyor belt did not operate "in connection with" coal mine because it was located at site of ultimate coal use and not located at site of mine). While the statute and the regulations refer to "mine" singularly, neither OSM nor the Division interprets the language to limit application to activities in connection with only one mine. Permanent Regulatory Program; Coal Preparation Plants Not Located Within the Permit Area of a Mine, 53 Fed. Reg. at 47,388. Regardless of the number of mines a facility is operating "in connection with," if the Division finds, based upon the above-listed factors and any other factors it deems pertinent, that a facility is both engaged in the "chemical or physical processing" of coal and operating "in connection with" a coal mine, the Division will require permitting.

Furthermore, even though a facility receives coal from a coal handler instead of directly from a mine does not mean that a facility is not operating "in connection with" a coal mine. A facility cannot exempt itself from regulation by merely purchasing coal through a middleman. Instead, the Division will consider this factor in looking at the facility as a whole in determining whether the facility is operating "in connection with" a coal mine.

Upon reviewing Covol's operations, the Division finds:

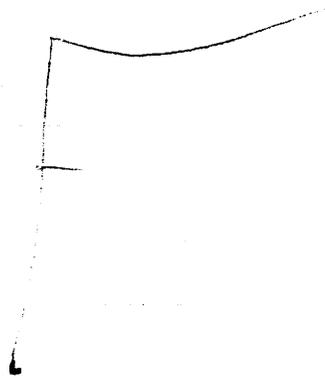
1. Covol's plant is located outside the permit area of any specific mine.
2. Covol is not an end user. Covol is currently building a plant that would clean coal and has indicated its intention to create a Synfuel product by applying a chemical additive. Labeling the treated coal as "Synfuel" is only relevant in determining whether Covol will reap the benefits of a federal tax credit and is not relevant to determining whether Covol is an end user. Covol sells coal to power plants. The power plant is the end user.
3. Covol is not located at the site of an end user.
4. Covol intends to buy and sell coal on the open market in the future. Regardless of where Covol sells its coal, it intends to purchase coal from either a coal mine, coal handler, or a waste pile, all of which are regulated by the Division. Covol will be just one step further in the process of marketing coal taken from a coal mine.
5. Covol only has plans to receive coal from either the Deer Creek Mine or the Hidden Splendor Mine, both of which are located in the same valley as Covol.
6. Covol will serve a necessary function of the coal mine operations by processing out-of-specification coal that might otherwise be treated as waste.
7. Currently, Covol is economically dependent upon its contracts with the coal mines. Covol has indicated that it plans to broaden its business plan to include NOx emission credit trading, and Synfuel tax credits. However, selling NOx emission credits and benefiting from a Synfuel tax credit depends upon Covol processing coal purchased from either a coal mine or a waste pile, both of which are regulated by the Division under the Utah Coal Mining and Reclamation Act and SMCRA.
8. Under the PacifiCorp and Commonwealth Tolling Agreements, Covol does not have the authority to sell the processed coal on the open market. Covol is contractually obligated to return the coal to the coal handler.

9. Covol will serve as an intermediary between several coal mines located in Utah and end-users. It currently has plans to purchase all of its coal from coal mines for sale to various power plants.

Based upon the above facts as made known to OGM, the Division finds that Covol will operate "in connection with" a coal mine. While the fact that Covol intends to buy and sell coal on the open market might weigh against permitting, the fact that Covol will also serve as a mere processing plant for several coal mines or handlers weighs in favor of permitting. Even if Covol's business plan were fully developed as it is proposed, the Division would still require permitting because some of its business would be "in connection with" a coal mine. Covol cannot escape regulation by conducting some types of business that would not be regulated where it also conducts business "in connection with" a coal mine. Covol has strategically placed itself close to five coal mines. Covol intends to clean out-of-specification coal for use by an end-user and may create a Synfuel by applying a chemical additive. It is and will continue to be functionally and economically integrated with various Utah coal mines and thus, the Division concludes that Covol will operate "in connection with" a coal mine.

CONCLUSION

Covol will engage in "coal mining and reclamation operations" because (1) by crushing, screening, and running the coal through an air separation device, Covol will be engaging in the "physical processing" of coal; and (2) Covol will operate "in connection with" a coal mine because it is functionally and economically dependent upon coal mines and because it is not located at the "site of ultimate coal use." Therefore, Covol must obtain a permit from the Division.





Adding Value to Energy™

Hand Delivered

July 6, 2005

Mayor Karl Houskeeper
City Counsel
City of Wellington, Utah

RE: Letter of Assurance

Dear Mayor Houskeeper and Council Members:

This Letter of Assurance is provided in connection with the proposed activities of our subsidiary, Covol Engineered Fuels, LC ("Covol"), at 1865 W. Ridge Road, Wellington, Utah 84542.

As you know, Covol owns 30 acres at the above location and intends to construct and operate a coal-cleaning facility. More specifically, Covol will contract to have coal shipped to the facility where it will be processed and returned to the coal owners or other buyers.

The coal-cleaning process will generate residual material suitable for beneficial uses such as structural fill. Covol intends to use some of this material for its own purposes with the remaining residual material either returned to the original coal owners or sold to third parties.

Headwaters Incorporated supports Covol's desire to be a long-term resident of Wellington and a positive contributor to the local economy. As such, Headwaters hereby provides you with assurance that it will lend its financial support and cause Covol to manage the coal and residual material located at the facility in accordance with applicable laws. Further, upon termination of its operations, Headwaters will ensure that Covol will remove all coal and residual material located on the property (excluding material used for improvements).

Sincerely,

HEADWATERS INCORPORATED



Steven G. Stewart
Chief Financial Officer

Cc: Keith Thompson,
General Manager, Covol Engineered Fuels LC

10653 S. River Front Parkway
Suite 300
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October 20, 2006

Mr. Craig D. Galli
Holland & Hart, LLP
60 E. South Temple, #2000
Salt Lake City, Utah 84111-1031

Re: *Settlement Negotiations Between Covol Engineered Fuels, LC and the
Division of Oil, Gas & Mining*

Dear Craig:

Thank you for your hospitality and the use of your offices for taking depositions and the meeting on Monday, October 16, 2006. I also want to thank you for opening the door to possible settlement. I think it is the right thing for both parties and I am very hopeful that this path will be fruitful. Attached is a proposed Stipulation and Joint Motion for Continuance and a proposed Order. Please let me know if they are sufficient and workable.

In an effort to clarify the Division's expectations and understanding of the agreement reached in the October 16 meeting, the following is an outline of the steps that the Division understands will be taken by both parties over the next few months. This is a summary based on my recollection and notes. As we both acknowledged prior to the discussions, these discussions and the steps set forth below are for settlement purposes only and will not be admissible if this matter proceeds to hearing.

1. Covol will complete an environmental compliance assessment report of the Covol site and share the same with the Division.
2. Covol will also consult with an environmental consultant who will provide a rough outline of an expected permit. As part of the rough outline prepared by Covol's consultant, the Division understands that the Covol site will have an industrial/commercial post-mining land use that would not require Covol to reclaim the parking lot and road, the plan will ensure removal of coal and coal by-products consistent with the post-mining land use, and Covol will provide a surety for the estimated costs of reclamation of the site.

3. The Division agrees to structure a permitting process that will take advantage of the background data already gathered by the environmental compliance assessment, nearby permitted sites, and other publicly available sources.
4. You indicated that Covol could provide a brief outline of a proposed permit application within the next four to six weeks. Once Covol provides the brief outline, the Division will review it to ensure that it will contain the essential elements, keeping in mind Covol's post-mining land use and the background information already available.
6. Once both parties have had an opportunity to review the outline, Covol and the Division expect to be able to enter into a formal settlement agreement and jointly seek dismissal of the case before the Board. If a settlement cannot be agreed upon, the hearing will be rescheduled.

Please let me know if there is something I have missed.

Thank you again,

Steven F. Alder



Attorney for Division of Oil, Gas &
Mining