

**RAILROAD COMMISSION OF TEXAS
HEARINGS DIVISION**

**SURFACE MINING DOCKET NO. C18-0002-SC-00-D
APPLICATION BY SAN MIGUEL ELECTRIC COOPERATIVE INC.
FOR ACCEPTANCE OF SELF-BOND WITH THIRD-PARTY GUARANTEE
PERMIT NO. 60, F, G AND H AREA LIGNITE MINE
McMULLEN COUNTY, TEXAS**

ORDER ACCEPTING RECLAMATION PERFORMANCE BOND

Statement of the Case

San Miguel Electric Cooperative, Inc. (SMECI), P. O. Box 280, Jourdanton, Texas 78026, has applied to the Railroad Commission of Texas (Commission) for acceptance of a self-bond with third-party guarantee and indemnity agreement for its Permit No. 60 for its F, G and H Area Lignite Mine located in McMullen County. The permit area is located approximately sixteen miles south of Jourdanton, Texas east of SH 16 and is southwest and adjacent to the Permit No. 11G area along FM 791. The proffered bond is in the amount of \$30,000,000. The application is made pursuant to the Texas Surface Coal Mining and Reclamation Act, TEX. NAT. RES. CODE ANN. CH. 134 (Vernon Supp. 2017), and the "Coal Mining Regulations," Tex. Railroad Comm'n, 16 TEX. ADMIN. CODE CH. 12 (Thomson West 2017).

As a condition for conducting surface mining activities, the Act requires the applicant to file a performance bond in acceptable form and in an amount sufficient to assure the completion of the approved reclamation plan if the work had to be performed at the direction of the Commission in the event of forfeiture. Tex. Nat. Res. Code §134.123 and §12.308 of the Commission Regulations provide the form of acceptable performance bonds.

Based upon Staff's analysis of reclamation costs, and the information and bond submitted by SMECI, the Commission finds that the bond and the guarantee and indemnity agreement submitted are acceptable in form and amount; the Commission also finds that the documents meet the requirements for bond acceptance. The Staff and the applicant, the only parties to the proceeding, have waived the preparation and circulation of a proposal for decision. Based on the application as supplemented, Staff's review of the application, the legal review, and financial review by Commission Staff, the Commission finds that the proffered bond may be accepted and the permit issued as Permit No. 60.

FINDINGS OF FACT

Based on the evidence in the record, the following Findings of Fact are made:

1. San Miguel Electric Cooperative, Inc. (SMECI), P. O. Box 280, Jourdanton, Texas 78026, applied to the Railroad Commission of Texas (Commission) for acceptance of a self-bond with third-party guarantee and indemnity agreement for its Permit No. 60 for its F, G and H Area Lignite Mine located in McMullen County by letter dated April 3, 2017. SMECI filed additional information on August 23, 2017. The application is made pursuant to the Texas Surface Coal Mining and Reclamation Act, TEX. NAT. RES. CODE ANN. CH. 134 (Vernon Supp. 2017), and the "Coal Mining Regulations," Tex. Railroad Comm'n, 16 TEX. ADMIN. CODE CH. 12 (Thomson West 2017) (Regulations).
2. By letter dated October 16, 2017, the Director, SMRD, transferred the application and original bond instruments to the Hearings Division, along with copies of legal and financial review memoranda from the Commission's Office of General Counsel and Financial Services Division.
3. In companion Docket No. C14-0020-SC-00-A, the Commission approved the application for a new permit for the F, G and H Area Lignite Mine. In Finding of Fact No. 55 of the order of approval, the Commission determined that a reclamation performance bond in a minimum amount of \$27,897,396 is required based on Staff's estimate of reclamation costs provided in Appendix II of its Technical Analysis filed in that docket. In the subject docket, SMECI requests acceptance of a bond in the amount of \$30 million. The proffered bond exceeds the amount required for the reclamation performance bonding.
4. The bond submitted by letter dated April 3, 2017 by SMECI is a self-bond with third-party guarantee and indemnity agreement. The third-party guarantor is National Rural Utilities Cooperative Finance Corporation (CFC), the guarantor of its approved bonds for Permit Nos. 11G and 52A for the adjacent San Miguel Lignite Mine.

5. The self-bond submitted is on a Commission form for self-bond. The bond is accompanied by the third-party guarantee and indemnity agreement also on a Commission form.
6. The bond submitted will provide bonding for operations as shown on the approved bond maps contained within the approved permit.
7. SMECI and CFC are business entities. SMECI is a corporation organized under the laws of the State of Texas for the purpose of engaging in rural electrification, and CFC is a District of Columbia cooperative association that provides financing for rural utility cooperatives and companies. Certified copies of the Articles of Incorporation, as amended, for SMECI (Item 10) and a Certificate of Good Standing issued by the District of Columbia for CFC (Item 17) are included in the bond documents.
8. The self-bond submitted by SMECI is signed by SMECI's General Manager, Mike Kezar, who is authorized to execute the bond on behalf of San Miguel [Incumbency Certificate dated March 22, 2017 and certified copy of Board Resolution dated February 17, 2017 (Item 10)]. The third-party guarantee and indemnity agreement is signed on behalf of the third-party guarantor CFC by Ann Shankroff and Paula Kramp, Assistant Secretary-Treasurers of CFC, who are duly authorized to execute the guarantee and indemnity agreement on behalf of CFC [certified copy of Corporate Resolution dated February 9, 2017 (Item 19)]. The third-party guarantee and indemnity agreement is signed on behalf of principal-permittee SMECI by SMECI's General Manager, Mike Kezar, who is authorized to execute the guarantee and indemnity agreement on behalf of SMECI. Corporate authorizations for San Miguel and CFC along with affidavits have been submitted to certify that the documents and agreements are valid under all state and federal laws [Affidavit of Mike Kezar (Item 6) Affidavit of Ann Shankroff (Item 19)]. The third-party guarantee and indemnity agreement contains the required undertaking by CFC to complete the reclamation plan for lands in default or to forfeit to the Commission an

amount necessary to complete the approved reclamation plan, not to exceed the bond amount. The requirements of §12.309(j)(5) have been met.

9. The self-bond and third-party guarantee and indemnity agreement provide that SMECI and CFC will comply with the requirements of the Texas Surface Coal Mining and Reclamation Act and applicable Commission Regulations.
10. The Commission regulation at 16 TEX. ADMIN. CODE §12.309(j)(3) provides that the Commission may accept a self-bond from the applicant and the applicant's third-party guarantor when the applicant meets the self-bonding requirements for a business entity set out in 16 TEX. ADMIN. CODE §12.309(j)(2)(A), (B), and (D) and when the third-party guarantor meets the requirements for a business entity set out in 16 TEX. ADMIN. CODE §12.309(j)(2)(A), (B), (C), and (D).
11. The applicant, SMECI, has met the requirements of 16 TEX. ADMIN. CODE §12.309(j)(2)(A), (B), and (D).
 - (a). SMECI has designated a suitable agent to receive service of process in Texas, Derrick L. Brummett, 6200 FM 3387, Christine, Texas (Item 7) [§12.309(j)(2)(A)].
 - (b). SMECI has been in continuous operation for a period of not less than 5 years immediately preceding the date of application and has not been subject to bankruptcy proceedings during that time (Item 7) [§12.309(j)(2)(B)].
 - (c). SMECI submitted required audited financial statements for the fiscal year ending December 31, 2016 (Item 9) in the application. By letter dated March 16, 2018, SMECI submitted audited financial statements for the fiscal year ending December 31, 2017. The auditors' statements contain no adverse opinions. By letter dated March 16, 2018, SMECI indicated that its unaudited financial statement for the first quarter of the current fiscal year are not yet available but will be provided to the

Commission as soon as they are complete. SMECI's income statement and balance sheets (Form 12a) for the months ending January 21, 2018 and February 28, 2018 were provided in the aforementioned March 2018 submittal [§12.309(j)(2)(D)].

12. CFC as third-party guarantor has met the requirements of 16 TEX. ADMIN. CODE §12.309(j)(2)(A), (B), (C), and (D).
 - (a). CFC has designated a suitable agent to receive service of process in Texas, Jeff Kilpatrick, 274 Ranch Ridge Drive, Spicewood, Texas (Item 13).
 - (b). CFC has been in continuous operation for a period of not less than 5 years immediately preceding the date of application and has not been subject to bankruptcy proceedings during that time (Item 13).
 - (c). Financial information has been submitted in sufficient detail to show that the requirements of §12.309(j)(2)(C)(i) and §12.309(j)(2)(D) have been met.
 - (1) CFC meets the financial criterion that it must have an investment grade rating for its most recent bond issuance of "A" or higher from Moody's Investors Service or Standard and Poor's Corporation (Item 16).
 - (2) SMECI has submitted CFC's audited financial statement for the most current fiscal year ended May 31, 2016 (Item 16; Form 10-K). The auditors' statement contains no adverse opinion. CFC's Form 10-Q for the quarterly periods ending August 31, 2017 and November 30, 2017 were submitted by letter dated March 16, 2018. SMECI indicated that CFC's unaudited financial statement for the most recently completed quarter of the current fiscal year are not yet available but will be provided to the Commission as soon as they are complete.

13. The terms of the third-party guarantee contain the provisions required for a third-party guarantee by 16 TEX. ADMIN. CODE §12.309(j)(3)(A). The guarantee provides that if SMECI fails to complete the reclamation plan, the guarantor shall do so or the guarantor shall be liable under the indemnity agreement to provide funds to the Commission sufficient to complete the reclamation plan not to exceed the bond amount. The guarantee shall remain in force unless CFC sends notice of cancellation as required by 16 TEX. ADMIN. CODE §12.309(j)(3)(B) and such cancellation is accepted by the Commission. The third-party guarantee guarantees all obligations of SMECI under the bond that includes providing replacement bonding as required.

14. The Regulations at 16 TEX. ADMIN. CODE §12.309(j)(4)(B) provide that for the Commission to accept a self-bond with third-party guarantee pursuant to qualification by 16 TEX. ADMIN. CODE §12.309(j)(2)(A), (B), (C)(i), and (D), the total amount of the guarantor's present and proposed self-bonds and guaranteed self-bonds for surface coal mining and reclamation operations shall not exceed 25% of the guarantor's tangible net worth in the United States [§12.309(j)(4)(B)]. Pursuant to §12.309(j)(1)(I), tangible net worth is equal to net worth minus intangibles such as goodwill and rights to patents or royalties.¹ Net worth is equal to total assets minus total liabilities [§12.309(j)(1)(F)]. CFC's total asset calculation for its fiscal year ending May 31, 2017 includes \$40,346,000 of "other assets" that are nonqualified 457(b) deferred compensation plans to highly compensated employees; the amounts deferred by employees are invested by the company. In their review, OGC and Financial Services excluded the \$40,346,000 of "other assets" from CFC'S total asset calculation based on the contention that deferred compensation amounts are more characteristic of a deferred liability than an asset to the corporation. CFC's tangible net worth amounts to \$1,058,459,000 without including "other assets" identified in its audited financial statement. With the self-bonds accepted for SMECI's existing Permit Nos. 11G and 52A and the proffered bond, CFC will have guaranteed self-bonds in a total amount

¹ CFC does not list any intangible assets for its fiscal year ending May 31, 2017 (Form 10-K, FYE May 31, 2017 at p. 72).

of \$130,000,000 [the \$30,000,000 bond requested for acceptance, the \$70,000,000 bond for Permit No. 11G (Order dated March 22, 2011) and the \$30,000,000 bond for Permit No. 52A (Order dated March 22, 2011)]. This amount is approximately 12.28% of \$1,058,459,000 CFC's tangible net worth in the U.S. based upon the audited statements of its fiscal year ending May 31, 2017. CFC meets the requirement of 16 TEX. ADMIN. CODE §12.309(j)(4)(B).

15. Acceptance of the self-bond with third-party guarantee and indemnity agreement in the amount of \$30,000,000 will allow SMECI to begin conducting surface coal mining and reclamation operations during the term of the permit.
16. The bond contains a clause replacing existing bond coverage and assuming existing liabilities.
17. No public notice other than notice of proposed action by the Commission in open meeting is required. Open meeting notice has been provided.

CONCLUSIONS OF LAW

Based on the above Findings of Fact, the following Conclusions of Law are made:

1. Required notice has been provided.
2. The Railroad Commission of Texas has the authority to determine the sufficiency of the value and form of reclamation performance bonds and to accept or deny reclamation performance bonds pursuant to the Texas Surface Coal Mining and Reclamation Act, TEX. NAT. RES. CODE Ch. 134 (Vernon Supp. 2017).
3. The reclamation performance self-bond, guarantee, and indemnity agreement meet the financial criteria of §12.309(j)(2)(A), (B), (C)(i), and (D) of the Regulations for a self-bond with third-party guarantee.
4. The reclamation performance bond with third party guarantee and indemnity agreement submitted by SMECI and executed by San Miguel and by CFC meet the requirements of the Texas Surface Coal Mining and Reclamation Act, TEX. NAT. RES. CODE Ch. 134 (Vernon Supp. 2008) and the Coal Mining Regulations of the Railroad Commission of Texas, 16 TEX. ADMIN. CODE Ch. 12, for value, form, and financial criteria for a self-bond with third-party guarantor.

IT IS THEREFORE ORDERED BY THE RAILROAD COMMISSION OF TEXAS that the above Findings of Fact and Conclusions of Law are adopted;

IT IS FURTHER ORDERED that the self-bond and the third-party guarantee and indemnity agreement in the amount of \$30,000,000 are accepted for reclamation performance bonding for the permit area, and Permit No. 60 is hereby issued;

IT IS FURTHER ORDERED that the Commission may vary the total bond amount as affected land acreage is increased or decreased or where the cost of reclamation changes; and

IT IS FURTHER ORDERED by the Commission that this order shall not be final and effective until 25 days after the Commission's Order is signed, unless the time for filing a motion for rehearing has been extended under Tex. Gov't Code §2001.142, by agreement under Tex. Gov't Code §2001.147, or by written Commission Order issued pursuant to Tex. Gov't Code §2001.146(e). If a timely motion for rehearing is filed by any party at interest, this order shall not become final and effective until such motion is overruled, or if such motion is granted, this order shall be subject to further action by the Commission. Pursuant to Tex. Gov't Code §2001.146(e), the time allotted for Commission action on a motion for rehearing in this case is 100 days from the date the Commission Order is signed.

SIGNED this 24th day of April, 2018.

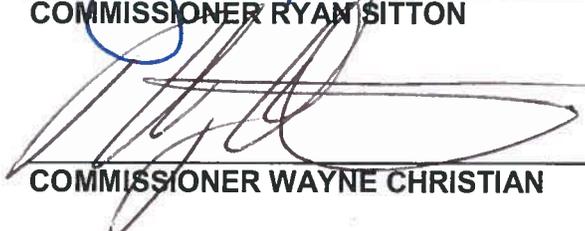
RAILROAD COMMISSION OF TEXAS



CHAIRMAN CHRISTI CRADDICK



COMMISSIONER RYAN SITTON



COMMISSIONER WAYNE CHRISTIAN

ATTEST:



Secretary, Railroad Commission of Texas

