NATURAL RESOURCES INDUSTRY: LIQUIDITY, OPERATIONAL AND COMPLIANCE CHALLENGES

April 1, 2020
Webinar Format

▪ All Lines Muted
▪ Please Use Chat Function to Submit Questions
▪ Webinar Will Be Recorded
▪ Slides Will Be Shared With All Participants
Overview

Michael A. Zody, Chair Environment, Energy and Natural Resources Practice Group
Overview and Theme/Goal

- Bring our collective experience to bear on the crisis facing our natural resources clients.
- Our team has lived through tough times in the industry, nothing quite like this, but we wanted to quickly get a dialogue going and be a resource to assist on the hard issues.
- Q&A at the end, but I may pose questions as we move through material.
Presenters

Mike Zody
Overview and Theme/Goal

Rew Goodenow
Liquidity Issues and Options, Pre CV-19 Relief Package Options

Ross Keogh
CV-19 Relief Package Options, CARES Act

Craig Johnson
Supply Chain and Receivables

Bruce White
Reorganizations/Bankruptcy, Voluntary and Involuntary, with New Provisions in CARES Act

Kevin Johnson
Insurance Key Reminders
Presenters

Rew Goodenow
Bonding, Reclamation, Temporary Care and Maintenance

Kevin Johnson
Essential/Critical Infrastructure

Jacob A. Santini
Enforcement and Compliance Relief, and Permitting Challenges

Mike Zody
Q&A
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Things are changing rapidly. We are working extremely hard to keep up with all that is happening. This webinar is based on available information as of March 31, 2020, but everyone must understand that this webinar is not a substitute for legal advice. If there are questions about the information contained in the presentation and how it applies to your business, then you should contact your legal counsel. This presentation is not intended and will not serve as a substitute for legal counsel on these issues. Given the complexity and rapidly changing landscape, you must consult with your legal counsel on these issues.
Liquidity Issues and Options, Pre CV-19 Relief Package Options

Rew R. Goodenow
Liquidity Issues

- Increasing existing lines of credit, revolvers, flooring lines and commercial facilities
- Review existing credit agreements and statements to determine terms, availability of credit
- Determine whether the full amount of the line can be borrowed (cash flow revolver) or is limited to amounts not previously advanced, or to the security (asset based line)
- Are the loan covenants currently satisfied; is there a duty to refresh; has an event occurred that would limit the availability (material adverse effect)
Liquidity Issues

- Common covenants: leverage ratio, material business change, cross defaults, cash flow
- New liquidity sources, commercial credit, CARES Act, private equity, asset sales, joint ventures
CARES Act – The four legs of the table

- $2.2 trillion in spending
- Direct taxpayer subsidies ($1,200 payments), and unemployment support
- $500 billion in Treasury directed intervention funds
- $349 billion through SBA 7(a) loan program for Paycheck Protection Program (PPP) loan
- Various tax changes and appropriations
PPP Loan Framework

- Available to cover 8 Weeks of Payroll Costs, interest, rent and utilities from February 15, 2020 through June 30, 2020.
- If maintain workforce at not less than 75% of compensation level loan can be forgiven
- All current SBA 7(a) Lenders can make PPP Loans starting April 3, 2020 (Friday)
- Loan principal is capped at 2.5 of monthly payroll costs or $10 million
- 500 employees or less (generally)
Eligibility Generally

- Broadens Eligible Business types:
  - Businesses
  - 501(c)(3)s
  - Veteran’s Organizations
  - Tribal Business Concerns
  - Self-Employed Individuals
  - Sole Proprietorships
  - Sector 72 Business

- No Revenue Limits-Just Employee Base limits
Payroll Costs

- Payroll Cost includes:
  - Salary, Wages, commissions and similar compensation
  - Gratuities
  - Employee Benefits (Health Care, Retirement, and Leave)
  - Severance Benefits
  - State and Local Tax
  - Independent contractor costs can also be included
Payroll Costs

Payroll Cost excludes:

- Any employee’s compensation which is in excess of $100,000 annually ($8,333.33/month)
- Compensation to Employees residing outside the U.S.
- Sick Leave Benefits under the Response Act
Allowable Uses Of Loan Proceeds

- Payroll Costs (Described Previously)
- Interest
- Rent
- Utilities
Loan Terms

- No Personal Guaranties
- Non-Recourse-unless use proceeds for impermissible purpose
- No Collateral
- No Credit Elsewhere Requirement
- No SBA Fees
- No Prepayment Fee
Terms Applicable to Portion of Loan Not forgiven

- Maximum 10-year term (amortized)
- Maximum of 4% interest
- 6 months and up to 1 year of deferred interest and principal payments
  - Deferral guidance to come
Lists of Top SBA Lenders

- **UTAH**: https://www.sbalenders.com/top-sba-lenders-utah/
- **IDAHO**: https://www.sbalenders.com/top-sba-lenders-idaho/
- **NEVADA**: https://www.sbalenders.com/top-sba-lenders-nevada/
- **MONTANA**: https://www.sbalenders.com/top-sba-lenders-montana/
Loan Forgiveness

- Can’t exceed principal balance of loan
- Subject to reduction forgiveness amount equal to amount of principal expended on:
  - Payroll Costs for Covered Period
  - Interest of Mortgage Obligation (incurred before 2-15, 2020)
  - Covered Rent (enforceable before 2-15, 2020)
  - Covered Utilities
- Amounts forgiven not subject to income tax
- Forgiveness is applied for with Lender
Reduction of Loan Forgiveness

- Reduction in Number of Employees (proportional) as a function of FTEs during one of two periods:
  - Average number of FTEs for February 15, 2019 to June 30, 2019; or
  - Average number of FTEs for period from January 1, 2020 to February 15, 2020.

- Reduction in Compensation

- De minimis exceptions may be coming in the form of regulations
Other Subsidies and Programs in CARES Act

- SBA will pay principal and interest on your existing 504 or 7(a) loan (except a PPP Loan)
- Required Minimum Distribution Relief
- Employee Benefits Opportunity- Employer Student Loan Payments
- Disaster Relief Payments
- 6.2% Social Security Tax Loan
- Bonus Depreciation and Business Interest
- Modification of NOLs Rules
- Payroll Tax Refundable Tax Credit
SBA Payment of Your 504 or 7(A) Loan

- The SBA will make 6 months of Payments on your behalf
  - Excludes EIDL and PPP Loans
  - Starts with next payment due date for 6 months
    - If loan is already deferred starts at end of deferment
- Also applies to loans made within 6 months of enactment of CARES Act
- Available to all 7(a) and 504 Borrowers as impact is presumed.
- $17 billion expected subsidy
Required Minimum Distribution Relief (Age 70.5)

- Allows taxpayers to not take RMDs prior to January 1, 2021.
- Avoids retirees locking in losses.
- Boosts economy by leaving money in markets.
- $100k loans from retirement plans also available.
Tax Free Payments on Student Loans

- Allows employers to make payments on an employee’s student loan or to make payment to an employee that the employee uses to make a payment on the student loan.
- Tax free to Employee.
- Could reduce salary (so long as not more than 25% - PPP loan issues) and still pay the employee the same after tax amount.
Disaster Relief Payments

- The March 13, 2020 national emergency declaration triggered 26 USC § 139

- Qualified disaster payments to individuals are now exempt from gross income

- The provision is extremely broad, allowing employers to reimburse employees for “reasonable” expenses associated with the pandemic.

- Example include: costs to set up and maintain a home office, medical expenses, housing, increased childcare expenses, expenses to maintain social distancing, alternative commuting, expenses associated with working from home.
Social Security Tax Loan (6.2%)

- May make social security tax payment 50% on December 31, 2021 and 50% on December 31, 2022.
- Precludes PPP forgiveness.
Bonus Depreciation & Business Interest

- Improvement Property generally depreciated over 39 year useful life (straight line)
- Allows amendment of tax returns to claim refund back to 2018 and use 15 year depreciation for Improvement Property.
- Deductible business interest raised from 30 to 50%.
Modified NOL Rules

- Allows 5-year carryback beginning after December 31, 2017.
- Implicates 35% corporate tax bracket years.
- Deferral of 80% income limitation from 2017 through 2021.
- Section 965 (generally foreign income) income not eligible.
Payroll Tax Credit

- Credit is not available if you have a PPP loan

- Available in two circumstances:
  - Organizations suffering a partial or full shutdown (by Shutdown Order).
  - Organizations whose gross receipts decline more than 50% as compared to same quarter last year. Tax credit ends in quarter gross receipts exceed 80%.

- Credit Amount
  - Fewer than 100 employees: all wages paid in quarter subject to gross receipts decline, or all wages paid during shutdown order.
  - 100 or more employees: only wages paid to employees that were not providing service eligible for credit.
Payroll Tax Credit

- Credit is immediately refundable as an overpayment of Employment Taxes.
- Limited to $5,000 credit per employee ($10,000 in wages).
- Healthcare expenses are qualified wages.
- Nonprofits may also utilize.
Watch for the Next Federal Packages

- Phase 4 Relief: major infrastructure investment?
- Relief for larger businesses?
- Tougher political battle
- Continue to work closely with trade associations
Producer Challenges Responding to Wide-Spread Financial Stress

R. Craig Johnson
COVID 19 – Dual Viruses

- Biological Virus – the Virus itself
  - Wide-spread governmental actions including:
    - Stay at home
    - Shuttering of businesses (esp. service business)
    - Government determines winners/losers (i.e., essential/non-essential)

- Economic Virus – the consequence
  - Business closures and high unemployment
  - Liquidity squeezes
  - Supply chain disruptions
  - CARE Act and other government bailouts/incentives
Mid to Long-Term Economic Disruptions

- Effects will last for months if not years
- Fundamental shifts in economy
Aggravates Already Slowing Industrial Demand

- 60 day, 6 month and 1 year zinc charts and copper charts show downward trending
Dual Squeeze on the Producers

- Suppliers and customers in cash squeeze liquidity situation
- Both then squeeze the producer to preserve liquidity
  - Suppliers want cash quicker
  - Customers want longer pay cycle
- (Financial institutions are a third squeeze, dealt with separately)
Response Plan for Producers

- Immediate forming response team of purchasing, management, finance, sales and legal
  - Tasked with immediate analysis of suppliers and customers
    - Long term contracts and payable issues
    - Cancellation and force majeure possibilities (note – economic force majeure not valid unless agreed)
    - What is essential and what can be deferred (capex, etc.)
    - Financial viability of suppliers and customers – establish a watch list for those at high risk
Response Plan for Producers

- Renegotiate contracts as soon as possible
  - Purchasing discounts in exchange for more rapid payment
  - Accelerate payments of accounts receivable for discounts (don’t get into mismatch of over committing to discounts on the sales side, if not balanced by discounts on purchasing side)
  - Understand Article 2 of the Uniform Commercial Code issues, including anticipatory repudiation and right to adequate assurance of performance.
Shore up Bank Lines of Credit and Revolving Credit Arrangements
Supply Chain Reliability

- During stress times, low cost suppliers often appear – often inferior or counterfeit products – Don’t Be Tempted!
- Block chain tracking and verification (See Guardtime Blockchain)
Start Working on Restructuring/Bankruptcy Plan Now

- Don’t wait too long – need cash to come out of restructuring/bankruptcy successfully
- Results in forced cancellation of some arrangements, stretching out others.
- Acts as leverage on suppliers and customers if carefully used.
5 Steps to Deal with Virus

<table>
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<tr>
<th>THE BIOLOGICAL VIRUS</th>
<th>THE ECONOMIC VIRUS</th>
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<tbody>
<tr>
<td>1. Wash hands frequently</td>
<td>1. Wash your budget frequently</td>
</tr>
<tr>
<td>2. Practice Respiratory Hygiene</td>
<td>2. Practice Fiscal Discipline</td>
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<tr>
<td>3. Avoid touching eyes, nose, mouth</td>
<td>3. Avoid making rash or involuntary decisions</td>
</tr>
<tr>
<td>4. Maintain Social Distance</td>
<td>4. Maintain disciplined relations with suppliers and customers</td>
</tr>
<tr>
<td>5. Seek Medical Attention Early</td>
<td>5. Seek professional assistance early</td>
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Workouts and Restructurings in the Energy and Mining Sectors

Bruce H. White
Introduction and Scope

The energy and mining sectors are highly distressed and virtually all commodities are at or near historic lows, with no sign of price recoveries in sight.

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Workouts and Restructuring Step-by-Step

Directors and Officers can’t sit back and do nothing - they have a duty of care to act.
Restructuring Step-by-Step

- **Be proactive.** If you wait until you have run cash-dry, it may be too late.
  - Directors and officers have a fiduciary duty of care. Don’t stick your head in the sand.
  - Directors and officers have duties in the “zone of insolvency”, which can deepen insolvency claims.

- **Get the right professionals involved early.** The right professionals can, and often do, make the difference between a successful reorganization and a failed effort.

- **Get an objective analysis.** A realistic assessment of the project’s worth and potential for reorganization can save you from throwing good money after bad.
Restructuring Step-by-Step

Professionals

The right team can make all of the difference:

- **Financial Advisors** – Solid financial advisors are key to keeping the reorganization on track, restructuring practices, and providing expert testimony on valuation, feasibility, reporting, and other key issues.

- **Restructuring Attorneys** – Chapter 11 practitioners are a specialized group, but it helps to have a group within a firm that is already anchored in and familiar with the industry.

- **Investment Bankers** – Credible investment bankers/sales professionals are the key to running sales and marketing processes and providing expert testimony to get sales approved.

- **Ordinary Course Professionals** – The debtor will need to continue employing existing or new counsel to provide permitting, litigation, operational, compliance, and other advice to the debtor.
Restructuring Step-by-Step

What alternatives do you have?

A. Workouts and forbearance agreements;
B. State court receivership;
C. Federal receivership;
D. Assignment for the benefit of creditors; and
E. Bankruptcy reorganizations.
Restructuring Step-by-Step

The Players:

**Before Bankruptcy:**

- Secured creditors
- Bondholders/indenture trustee (secured or unsecured)
- General unsecured creditors, including operating companies, materials and equipment suppliers, independent contractors, and utilities
- Regulators
- Employees and labor unions
- Taxing authorities

*While in Bankruptcy, all of the above plus:*

- United States Trustee
- Bankruptcy judge
- Creditors’ committee(s)
Tools for Effective Reorganization

Reorganization Options:

1. Workouts

   A. **Raise Money** – difficult in this environment

   B. **Purchase or sale of secured debt** – purchase of the secured debt by a friendly party, who then succeeds to all the rights of the secured creditor and may then foreclose

   C. **Tender or Exchange Offer** – exchange of secured debt for cash out at a discount or a write-down of existing debt (usually) with some equity stake

2. Bankruptcy Reorganization
Prior Bankruptcy Scheme

- **Chapter 7** – liquidation (out of business)

- **Chapter 11** – reorganization; expensive and lengthy; creditors have to be paid in full or prior owners lose their ownership.

- **Chapter 13** – pay as much as possible over 3-5 years, then get a fresh start.
Small Business Reorganization Act of 2019

Added Subchapter V to Chapter 11:

- Small business debtor remains in possession and control of its business.
- No creditors committee; instead, a trustee to assist the debtor.
- Small business owners retain ownership if creditors are paid disposable income for 3-5 years.
- U.S. Trustee fees waived.
- Time periods reduced, including plan in 90 days.
CARES Act

• Raises eligibility for Subchapter V from $2.7 million in secured and unsecured debt to $7.5 million in non-coronavirus debt.

• Changes sunset in one (1) year.
Restructuring Step-by-Step

Keys to a Successful Reorganization:

1. Cash flow and financing;
2. Value; and
3. Relationship with secured creditor.
Develop a Workable Business Plan
Tools for Effective Reorganization

Bankruptcy Basics: Asset Sales Under Bankruptcy Code Section 363

Section 363 provides for a court-approved sale of some or all of the debtor’s assets.

Key Issues:

- Partial Sale
- Sale “Free and clear” (Section 363(f))
- Competitive bidding (or not)
- Stalking horse, break-up fee, and bid protections
- Sale of tenant-in-common interests (TICS) (Section 363(h))
Tools for Effective Reorganization

Bankruptcy Basics: How do I get out?

There are three ways to exit a Chapter 11 bankruptcy case:

1. Plan of reorganization/liquidation;

2. Asset sale followed by a dismissal; and

3. Dismissal/conversion to Chapter 7 (i.e., failure).
Take-Aways

1. **Be proactive** – In order to maximize the chances of success, act early while the entity has the capacity for reorganization and has good relationships with creditors.

2. **Get the right professionals involved early** – It is very difficult to assess the capacity for a project’s reorganization without the assistance of professionals who are experienced in turnarounds. The right professionals can make the difference between a successful reorganization and a failed effort.

3. **The right company or project can be reorganized, others cannot** – Get the right professionals to assess the project’s capacity for reorganization. “Lightning strike” problems are more likely solvable, while systemic problems are usually not fixable.
Insurance Key Reminders

Kevin W. Johnson
Coverage Limits

- Who is covered
  - Affiliates
  - Additional Insureds

- What is covered
  - Exclusions
  - Representations regarding covered parties
Policy Limits

- Occurrence and Aggregate limits
- Deductibles and SIR
- Subcaps
- Excess layers
Notice Requirements

- Have you had triggering events?
- Timely notice is critical
Bonding, Reclamation, Temporary Care and Maintenance

Rew R. Goodenow
Bonding Pressures

- Alert to the BLM and state authorities of liquidity issue and need for consultation
- 43 CFR 3809 regulations – the bond stays in place
- To whom does the bond belong: financial instrument, cash, LOC, surety
- Surety decertified or bond cancelled
- Temporary care and maintenance
- Reclamation
Essential/Critical Infrastructure

Kevin W. Johnson
Federal Guidance

- On March 13, 2020, President Trump declared a national emergency as a result of the novel coronavirus pandemic.

- Since then, the Cybersecurity and Infrastructure Security Agency ("CISA") has issued guidelines regarding what CISA considers as critical infrastructure workforce. The latest guidance was issued on March 28, 2020, and includes the following 16 areas:
Federal Guidance

- Chemical
- Commercial Facilities
- Communications
- Critical Manufacturing
- Dams
- Defense Industrial Base
- Emergency Services
- Energy
- Financial
- Food and Agriculture
- Government Facilities
- Information Technology
- Healthcare and Public Health
- Nuclear Reactors, Materials and Waste
- Transportation Systems
- Water
Federal Guidance

- Subcategories within these areas have changed over time.

- The CISA emphasizes that its information is for guidance only; any orders are state ordered and managed and federally supported.

- The Centers for Disease Control also has published guidelines for protecting the health and safety of critical infrastructure workforce.
  - Encourage sick workers to stay at home
  - Identify where and how workers might be exposed to COVID-19 at work
Federal Guidance

- Maintain healthy business operations
- Identify a workplace coordinator who will be responsible for monitoring working conditions
- Implement flexible sick leave and supportive policies and practices
- Review access to essential functions at the jobsite and how such functions are delivered at the jobsite
- Determine how operations will continue if absenteeism spikes
- Establish policies and procedures for social distancing
  - Six feet of distancing, subject to health and safety laws such as OSHA and MSHA
  - Avoid large gatherings
Federal Guidance

- Maintain a healthy work environment
  - Consider improving the engineering controls using the building ventilation system
  - Enforce respiratory etiquette and hand hygiene
  - Routine environmental cleaning
  - Enhanced cleansing and disinfection

- Establish travel policies to protect against the spread of COVID-19

As with the CISA guidance, the CDC information is for guidance only and is to be implemented at the state and local level
State Response

- In response to the CISA and CDC guidance, many states and municipalities have issued executive and health orders, including Arizona, California, Idaho, Montana, Nevada and Utah.

- The executive and health orders generally follow the structure of the CISA guidance, tailored to fit the requirements of the specific state or municipality
  - Non-Essential Businesses
    - Gym and fitness centers
    - Cinemas
    - Dine-in restaurants and bars
    - Barber shops
State Response

- Essential Businesses
  - Pharmacies
  - Gas stations
  - Grocery Stores
  - Hardware stores
  - Critical trades

- Critical Infrastructure
  - Generally follow CISA guidance, with local nuances
  - Many state orders have procedures for business to petition to be included as essential businesses or critical infrastructure
The executive and health orders generally reference the CDC guidance for essential businesses and critical infrastructure.

In certain states, the response is not as aggressive or lacks the force of law, so cities and counties have adopted orders that are more aggressive than those at the state level, such as Salt Lake City, Salt Lake County, Summit County and Wasatch County in Utah.
Recommended Actions

- Review state and municipal orders to determine whether a business fits within an essential business or critical infrastructure
- If a business is not considered an essential business or critical infrastructure, determine whether to petition to be considered as such
- In the absence of a state or municipal order, follow the CISA guidelines
- Develop a health and safety policy that follows the CDC guidance
Enforcement and Compliance Relief

Fundamental Issue: Once an operator overcomes the hurdle of continuing operations in light of the extraordinary circumstances, there is a reality that compliance with certain conditions will be impracticable

EPA’s Response: Temporary Enforcement Policy

- Released March 26, 2020
- Available at: https://www.epa.gov/enforcement/enforcement-policy-guidance-publications
EPA’s Temporary Enforcement Policy

**Enforcement Discretion.** EPA will withhold violations or civil penalties if a source can show that it made efforts to minimize the impacts and duration of non-compliance due to Covid-19.

**General Conditions**

“Make every effort to comply” with environmental obligations.
EPA’s Temporary Enforcement Policy

General Conditions (continued)

Where Compliance “is not reasonably practicable”

1. Act responsibly *under the circumstances* to minimize the effect and duration of noncompliance
2. Identify the specific nature and dates of the noncompliance
3. Identify how Covid-19 was the cause, the actions taken in response
   - Actions include the best efforts to comply and steps taken to come into compliance at the earliest opportunity
4. Return to compliance as soon as possible
5. Document actions 1 through 4
EPA’s Temporary Enforcement Policy

Reporting under Specific Circumstances

- **Compliance monitoring and reporting** – report non-compliance as provided in existing permits, regulations or statutes (e.g., T-V deviation reporting)
  - If no applicable reporting requirement exists – maintain the information internally

- **Acute Risk or Imminent Threat to Human Health or the Environment** – contact EPA and implementing State/Tribal authority

- **Excess Emissions (air/wastewater)** – notify implementing authority (EPA/State/Tribe) “as quickly as possible”

- **Hazardous Waste Generator Status** – if unable to transfer waste off-site, continue to properly label and store; EPA will use discretion to not treat as treatment, storage, or disposal facilities
Recertifications: MSHA will work with operations regarding annual refresher training and other certifications; extension of due dates through the duration of the emergency declaration

- Does not apply to new miner training
Pipeline & Hazardous Materials Safety Admin.

Emergency Policy available at:

Enforcement Discretion. Applies to potential violations under 40 CFR Part 190 – 199.
State Responses

Follow EPA’s lead (less formally)

- Utah Department of Environmental Quality – “will work with regulated communities on a case-by-case basis to determine reasonable exemptions to environmental rules”

- Waiving requirements for “wet” signatures and hand-delivery
Permitting Issues

- Agencies are working through public meetings and hearings issues, moving online but may require emergency orders.
- General slowdown in processing as agencies adjust to online methods and facilities face consultant travel restrictions.
- Requests by contractors for certifications that work is essential, such as field work like cultural surveys.
- Navigating social distancing issues.
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Thank You

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Thank You