

STATE OF ALASKA

DEPARTMENT OF NATURAL RESOURCES DIVISION MINING LAND & WATER

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January 14, 2010

Mr. Ken Taylor
Vice President, Environment
The Pebble Limited Partnership
3201 C Street, Suite 604
Anchorage, Alaska 99503

Certified Mail – Return Receipt Requested

Dear Mr. Taylor:

We appreciate the Pebble Limited Partnership (Pebble) coming forward with the information presented in your letter of November 6, 2009. In reviewing the information in the letter, we now understand what happened, and the reasons why water was taken from sites and sources outside those permitted under existing Temporary Water Use Authorizations (TWUPs). Fortunately due to the nature of your activities and the precautions taken, it does not appear that there was any environmental damage resulting from your activities. Regardless, taking the quantities of water used from these sites and sources without an authorization violates the Alaska Water Act and Water Management Regulations (AS 46.15.080 and 11 AAC 93.035). In addition, based on the information submitted, it appears that Pebble also placed water intake structures in streams without any review by the Alaska Department of Fish and Game (ADF&G), Division of Habitat, to determine if Fish Habitat Permits were required, which is a violation of AS 16.05.

These violations are also a breach of Section 2 of the terms of Pebble's Miscellaneous Land Use Permit for Hardrock Exploration and Reclamation, ADL 096118, which requires all operations under the permit to be conducted in conformance with applicable federal, state, and local laws and regulations. Accordingly, pursuant to AS 46.15.155 (i) and 38.05.850, the following permits are suspended effective immediately: TWUP A2006-142 through TWUP A2006-150, TWUP A2009-21, TWUP A2009-82 and TWUP A2009-83, and MLUP A096118. These permits are suspended until Pebble provides a detailed written plan that assures that all water sources used in drilling and other operations that require an authorization are properly permitted, and DNR, DMLW Water Resources and Mining Sections, and ADF&G, Division of Habitat, have approved of this plan. Additionally, the state expects Pebble to pay for its past violations.

It appears that if Pebble had applied for the sources or stream reaches actually used, TWUPs likely would have been issued. The quantity of water being used for the drilling program is a de minimus quantity when compared to the water available in the areas where drilling took place, and it is unlikely that any damage resulted because the appropriate measures were employed (e.g., screened intake) at the water intakes to protect fish and fish habitat. Nevertheless, the appropriate permits

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were never applied for or issued, and Pebble's activities violated state law and the terms of MLUP A096118. Those activities cannot be allowed to continue in the absence of safeguards to assure future water withdrawals are lawful.

Let me explain further the reasons for suspending the permits and what Pebble must do to lift the suspension. In reviewing the maps of the 2007, 2008 and 2009 Pebble Diamond Drill Holes and Water Sources, provided with Pebble's November 6th letter, it is apparent that it was not just during the 2009 drilling program that unpermitted water withdrawal sites and water sources were used. It appears that water has been taken from unpermitted sources and locations as many as 45 times over the past 3 years.

DNR processed Pebble's TWUP applications based on the information provided in those applications, which included the specific lakes and stream segments that Pebble was going to use as water sources for drilling. The regulation at 11 AAC 93.220(b) sets out the required information needed to process the application and Pebble's applications complied with this regulation. The TWUPs that were issued specifically identified the water sources and stream reaches authorized for water withdrawals. Pebble personnel's misunderstanding or confusion as to the geographic limitations of the individual TWUPs or how the TWUPs authorizations coordinated with the ADF&G Habitat Permits is not an acceptable excuse for withdrawing water from sources and locations not authorized under the TWUPs.

In order to lift the suspension placed on the permits and resume water withdrawals and exploration activities under the TWUPs and MLUP, Pebble must pay for its past violations, including penalties, and must also provide DMLW and ADF&G with a detailed written plan that ensures that such violations do not occur in the future. The written plan must ensure that in the future all water sources and stream reaches used in drilling and other operations are properly permitted, and Pebble must obtain approval of the plan from DMLW's Water Resources and Mining Sections, as well as ADF&G's Division of Habitat. This plan should include, but is not limited to:

- 1) provision for submission to DNR of appropriate maps prior to drilling, showing specific water sources and approximate take points within an authorized reach of a stream, for each drill hole, including identification of the specific TWUP that authorizes that water source;
- 2) a plan for coordination and training of field staff, geologists, engineers, drillers, and any other workers involved in the placement of intake hoses, and the connection of intake hoses to the drilling operation;
- 3) provision for GPS identification prior to and after the intake is in place and email submittal of this GPS information to identified contact persons with DNR's Water Resources Section and ADF&G's Division of Habitat; and
- 4) submittals to Water Resources Section staff and ADF&G Division of Habitat staff of photographic confirmation at each source and take point, prior to and after intake equipment has been placed and removed.

In addition, Pebble must appoint a field position (Compliance Officer) to be responsible for making sure that any water source being used has the appropriate TWUP authorization and ADF&G Habitat review or permit, checking locations of water sources and take points, and ensuring that all field

operations are in compliance with conditions and stipulations of the TWUPs, MLUP, and Fish Habitat Permits.

In determining the adequacy of the written plan, DNR and ADF&G Division of Habitat will consider whether the means and methods provided in the plan are adequate to assure the state agencies that this situation will never happen again. The suspension of the above referenced TWUPs and MLUP will not be lifted, and no applications for temporary water use or land use permits will be processed for this project, until Pebble's written plan for compliance is approved as provided herein.

Regarding the past violations, Pebble's actions are, at a minimum, a trespass against the state's property and resource interests. Although it does not appear that any environmental damage occurred as a result of these violations, the state's ownership and management interests in state resources were nevertheless damaged by Pebble's trespass, its failure to comply with state permitting and regulatory processes, and its unauthorized uses of state water. The state will settle its civil trespass claim for each past apparent violation for the amount of \$1,000 per violation, for a total settlement of approximately \$45,000. This amount will compensate the state for its lost permitting fees, the time necessary to investigate and address these violations, the transgressions against the state's ownership and management interests in state resources, the violations of the state's permitting authorities, and serve as a deterrent to future violations.

Again, while we appreciate Pebble's candor in coming forward with information concerning these violations, steps must be taken to protect the state and its resources and avoid future violations. A proposed settlement agreement in accordance with this letter is enclosed. I will be contacting you by phone in the next week to finalize this agreement for the parties' signatures.

Sincerely,



Dick Mylius, Director
Division of Mining, Land and Water

cc: John Shively, CEO, Pebble Partnership
Commissioner Tom Irwin
Commissioner Denby Lloyd
Attorney General Dan Sullivan
Kerry M. Howard, Director, ADF&G Habitat
Gary Prokosch, Chief, DNR, DMLW, Water Resources Section
Rick Fredericksen, Chief, DNR, DMLW, Mining Section
Tom Crafford, DNR Large Project Coordinator
Ed Fogels, Director, DNR Office of Project Management and Permitting