Gila Resources Information Project
Promoting Healthy Communities by Protecting Our Environment Since 1998

February 3, 2017

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Via e-mail: Fernando.martinez@state.nm.us; michelle.hunter@state.nm.us

RE: Modification - Mining and Minerals Division Permit Nos. GR009RE, GR010RE, GR002RE, New Mexico Environment Department Discharge Permit Nos. 1340, 1341, and 1403

Dear Mr. Martinez and Ms. Hunter:

Thank you for setting up the January 20 conference call and WebEx presentation with Freeport-McMoRan Inc. (FMI) staff regarding the substitution of Freeport Minerals Corporation (FMC) for FMI as the Third Party Guarantor of its Grant County mines as outlined in FMI's modification applications dated December 13, 2016.

We appreciate your efforts to provide the FMC Financial Soundness Test (FST) results for 2015 and Q1, Q2, and Q3 of 2016. This information was very helpful for GRIP to evaluate the potential risks of Third Party Guarantees issued by FMC.

As outlined below, we remain very concerned about this modification application:

1) **The Certificate of Guarantor's Compliance (Exhibit A-1) is likely to underestimate FMC's environmental liabilities.**

- The guarantees listed in section 1b. of the *pro forma* for Freeport Minerals Corporation as guarantor are for FMC's U.S mines located in Arizona. As explained by GRIP's technical consultant, mining engineer Jim Kuipers, "corporate guarantees comprise 100% of the financial assurance for those sites and [FMI] has not provided any amount in any form of real financial assurance for those liabilities. The amounts are typically for minimal surface reclamation and limited post-reclamation obligations estimated to range from 2 – 30 years. Arizona water quality regulations allow for determination of groundwater impacts to be delayed until closure of the mine – this means the requirement for source controls and ground and/or surface water remediation post-mining has not been determined and therefore not included in the current Arizona financial assurance obligations."[1]

- The *pro forma* information provided does not include $300 million in liabilities resulting from a settlement agreement with the Department of Justice for cleanup of 94 abandoned uranium mines on the Navajo Nation. [2] As confirmed by FMI in the January 20 conference call, these liabilities fall on FMC, but are not reflected in the Financial Soundness Test information currently available.
- Liabilities in section 1b increased by $171 million from Q2 to Q3 2016. Are there additional liabilities that are not reported and how will these affect the FST results?

2) Freeport Minerals Corporation, a wholly owned subsidiary of FMI, is subject to potential impacts to the financial health of the larger corporation, including bankruptcy.

In the January 20 conference call, FMI staff did not provide any evidence of how FMC would be immune from the impacts of the financial health of its parent company, FMI. Moody's acknowledged the strong financial connection between FMI and FMC when it downgraded FMC in January 2016 to B1 from Baa3 reflecting "the fact that this debt is at the operating company level and benefits from a downstream guarantee from [FMI]." This rating occurred concurrently with Moody's downgrade of FMC's parent FMI. [3]

Jim Kuipers recommends in the attached memorandum that "MMD should undertake to evaluate and provide an explanation as to why the acceptance of a guarantee of a subsidiary corporation would not be subject to forfeiture in the event of the failure of the owner. This also suggests that if MMD accepts FMC as a

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[1] Letter from GRIP to MMD and NMED, October 12, 2016 RE: Third-Party Guarantee for Freeport-McMoRan Chino, Tyrone and Continental Mining Facilities, Mining and Minerals Division Permit Nos. GR009RE, GR010RE, GR002RE, New Mexico Environment Department Discharge Permit Nos. 1340, 1341, and 1403

[2] *Phoenix Business Journal* "Freeport-McMoRan, Obama administration strike $600M deal to clean up abandoned Navajo Nation uranium mines" January 18, 2017 http://www.bizjournals.com/phoenix/news/2017/01/18/freeport-mcmoran-obama-administration-strike-600m.html

[3] Moody's downgrades FCX's ratings, assigns B1 CFR; outlook negative. January 27, 2016. https://www.moodys.com/research/Moodys-downgrades-FCXs-ratings-assigns-B1-CFR-outlook-negative-- PR_343032

guarantor, it will need to also monitor the financial ability of [FMI] as well as FMC, and if [FMI]'s financial situation further erodes to ensure measures are proactively taken to consider impacts to FMC as a guarantor."

3) **It is highly probable that a decreasing copper price climate at any time in the future 1-2 years would likely result in FMC failing the FST, and MMD having to seek alternative forms of FA.**

Jim Kuipers has conducted sensitivity analyses that demonstrate how the Financial Soundness Test results are influenced by copper price, total obligated guarantees, net working capital, and combined sensitivity (see attached memo). Mr. Kuipers expert opinion is that if copper prices were to decline again, the state of New Mexico may find itself in a similar predicament in the next year or two and will need to require replacement of the Third Party Guarantee.

4) **Acceptance of a $104 million Third Party Guarantee puts at financial and environmental risk the state of New Mexico and communities surrounding FMI's Grant County mines.**

As described above, acceptance of $104 million Third Party Guarantee issued by Freeport Minerals Corporation is not in the public's best interest as it puts the State of New Mexico in a position of significant environmental and financial risk. FMI's policy of "maximizing the guarantees across the portfolio" as explained by FMI staff in the January 20 conference call represents a corporate goal of shifting risk to the public sector. Bankruptcy of FMI and FMC would force the state of New Mexico to cover $104 million in clean up costs or reduce the extent of reclamation work if funding could not be obtained.

5) **MMD should require that the Third Party Guarantee for FMI's Grant County mines is eliminated.**

It is clear that the only way to eliminate financial and environmental risk to the state of New Mexico and local communities is to phase out the Third Party Guarantee for FMI's Grant County mines.

Thank you for your consideration of our comments on this critical issue.

Sincerely,

Allyson E. Siwik

Allyson Siwik
Executive Director

Cc: Jim Kuipers, Kuipers & Associates

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January 31, 2017

To: Allyson Siwik, Gila Resources Information Project (GRIP)

From: Jim Kuipers P.E., Kuipers and Associates

Re: **Comments re Freeport Minerals Corp Third Party Guarantee for Chino, Tyrone, Cobre**

The following comments are based on the financial information provided to GRIP by MMD concerning Freeport Minerals Corp.

- As a subsidiary of Freeport McMoran Inc (FCX), Freeport Minerals Corp (FMC) is subject to potential impacts to the economic health of the larger corporation, including bankruptcy. Despite assurances from FCX/FMC representatives otherwise, we believe the possibility exists that if FCX were to become insolvent it is possible that FMC would likewise be subject to either sale or potentially abandonment. FCX/FMCs premise would appear to be based on economic suppositions rather than legal facts and precedents. MMD should undertake to evaluate and provide an explanation as to why the acceptance of a guarantee of a subsidiary corporation would not be subject to forfeiture in the event of the failure of the owner. This also suggests that if MMD accepts FMC as a guarantor, it will need to also monitor the financial ability of FCX as well as FMC, and if FCX's financial situation further erodes to ensure measures are proactively taken to consider impacts to FMC as a guarantor.

- Review of the FMC financial information and MMD financial soundness test (FST) requirements (see Table 1) suggest that the company's financial health is strongly tied to copper production and thus the price of copper itself. A sensitivity analysis should be performed relative to FMC's financial performance and copper price and used by MMD to consider taking pro-active measures to consider impacts to FMC as a guarantor.

- Total Obligated Guarantees – We have run a sensitivity analysis on FMC's total obligated guarantees to determine the level of guarantees that would cause FMC to fail the FST. FMC has acknowledged they are liable for the costs of the recent uranium remediation settlement, and as we have pointed out in the past, the costs represented for financial assurance in Arizona are highly deficient in comparison to those administered in NM by MMD. Additionally, FMC could become liable for additional costs relative to EPA's 108b rule. As shown in Table 1, Sensitivity Case #1, if all other factors were to remain the same as the 3rdQ 2016 and the corporate guarantees amount was to rise from the present level of $619.9M to $1,200M, or approximately double, FMC would fail the FST (part b.ii.).

- Net Working Capital – We also ran a sensitivity analysis on FMC net working capital to determine how the availability of working capital, which could be tied indirectly to the copper price, might affect FMC's ability to pass the FST. As shown in Table 1, Sensitivity Case #2, if all other factors were to remain the same as the 3rd Q 2016 and FMC's working capital was to decrease from $6.9B to $3.6B, FMC would likewise fail the FST (also part b.ii.).

- Combined Sensitivity. A sensitivity analysis was also done on the combined effect of increasing obligated guarantees and decreasing working capital. As shown in Table 1, Sensitivity Case #3, if all other factors were to remain the same as the 3rd Q 2016 and FMC's total obligated guarantees were to rise by $900M and their net working capital was to decrease to $5.3B, FMC would likewise fail the FST (also part b.ii.). Based on the consideration of these sensitivity analysis we believe it is highly probable that a decreasing copper price climate at any time in the future 1-2 years would likely result in FMC failing the FST, and the NM MMD having to seek alternative forms of FA.

We admit that other than requiring replacement of the third-party guarantee with an acceptable form of financial assurance, there may be no "pro-active" measures available to MMD, and that MMD is not in a legal position to require replacement until failure of the FST, in which event the company would not be able to provide a replacement guarantee, particularly if the failure of the FST is accompanied by bankruptcy. For that reason, we would suggest that at the least MMD respond in a timely manner, and that the State of New Mexico use this untenable situation as a reason to revise the NM Mining Act to not allow for the use of corporate, third party, or any other form of non-tangible financial assurance.

Finally, while FCX/FMC may desire to "maximize" its Third-Party Guarantees, the approach similarly maximizes the liability of public taxpayers, and in the event of a future slump in metals prices sets the stage for almost certain failure of the FST as well as potential bankruptcy. This approach would appear to be both contrary to the intention of the financial assurance provisions of the NM Mining Act as well as public interests overall, and in many respects is contrary to good corporate governance. A more reasonable and long-term approach would seek to eliminate all liabilities or debts over time and minimize the use of third-party guarantees.

Table 1 - Freeport Minerals Corp Financial Test Results

Balance Sheet	4Q2015	1Q2016	2Q2016	3Q2016	Sensitivity Case #1	Sensitivity Case #2	Sensitivity Case #2
Total Obligated Guarantees							
NM TPGs - Chino, Tyrone, Cobre	$203.1	$104.3	$104.3	$104.3	$104.3	$104.3	$104.3
TPGs - Other in U.S.	$321.2	$345.0	$345.0	$515.6	$515.6	$515.6	$515.6
Total	$524.3	$449.3	$449.3	$619.9	$1,200.0	$619.9	$900.0
Total Assets	$28,300	$28,120	$27,055	$27,287	$27,287	$27,287	$27,287
Total Assets in the U.S.	$12,283	$12,069	$11,476	$11,973	$11,973	$11,973	$11,973
Total Liabilities	$9,730	$9,690	$9,604	$9,324	$9,324	$9,324	$9,324
Net Income	$120	-$81	$601	$1,045	$1,045	$1,045	$1,045
Depreciation, Depletion and Amortization (DDA)	$1,358	$1,225	$1,280	$1,251	$1,251	$1,251	$1,251
Current Assets	$4,891	$4,939	$8,696	$9,292	$9,292	$9,292	$9,292
Current Liabilities	$1,546	$1,463	$2,202	$2,376	$2,376	$2,376	$2,376
Net Working Capital	$3,345	$3,476	$6,494	$6,918	$6,918	$3,600.0	$5,300.0
Net Worth	$18,570	$18,431	$17,451	$17,963	$17,963	$17,963	$17,963
Total Intangible Assets	$317	$312	$308	$308	$308	$308	$308
Tangible Net Worth	$18,253	$18,119	$17,143	$17,655	$17,655	$17,655	$17,655
Net Income plus DDA	$1,478	$1,144	$1,881	$2,296	$2,296	$2,296	$2,296
Alternative Test I NMAC (19.10.12.1208.G(8)(a))							
a. Is Tangible Net Worth at least $10 million?	$18,253	$18,119	$17,143	$17,655	$17,655	$17,655	$17,655
	Pass	Pass	Pass	Pass	Pass	Pass	Pass
b. i. Is Tangible Net Worth at least six times Total	34.8	40.3	38.2	28.5	14.7	28.5	19.6
Obligated Guarantees?	Pass	Pass	Pass	Pass	Pass	Pass	Pass
b. ii Is Net Working Capital at least six times Total	6.4	7.7	14.5	11.2	5.8	5.8	5.9
Obligated Guarantees?	Pass	Pass	Pass	Pass	Fail	Fail	Fail
c. Are 90% of Guarantor's assets located In the	43%	43%	42%	44%	44%	44%	44%
United States?	Fail	Fail	Fail	Fail	Fail	Fail	Fail
d. is the amount of Guarantor's assets located In	23.4	26.9	25.5	19.3	10.0	19.3	13.3
the U.S. more than six times Total Obligated	Pass	Pass	Pass	Pass	Pass	Pass	Pass
e. Meets two of the three financial ratios:							
e. i. Is ratio of Total Liabilities to Net Worth less	0.5	0.5	0.6	0.5	0.5	0.5	0.5
than 2.0?	Pass	Pass	Pass	Pass	Pass	Pass	Pass
a. ii. Is ratio of sum of Net Income plus Depreciation, Depletion and Amortization to Total	0.15	0.12	0.20	0.25	0.25	0.25	0.25
Liabilities greater than 0.1?	Pass	Pass	Pass	Pass	Pass	Pass	Pass
a. iii. Is ratio of Current Assets to Current	3.2	3.4	3.9	3.9	3.9	3.9	3.9
Liabilities greater than 1.5?	Pass	Pass	Pass	Pass	Pass	Pass	Pass