

FILED

**BEFORE THE ENVIRONMENTAL QUALITY COUNCIL
STATE OF WYOMING**

FEB 27 2009

**Jim Ruby, Executive Secretary
Environmental Quality Council**

**IN THE MATTER OF THE APPEAL OF)
PENNACO ENERGY, INC. OF) DOCKET NO. _____
CONDITIONS IN RENEWAL OF)
WYPDES PERMIT NO. WY0040797)**

NOTICE OF APPEAL AND PETITION FOR HEARING

Pursuant to section 802 of the Environmental Quality Act, Wyo. Stat. Ann. § 35-11-802, Pennaco Energy, Inc. ("Pennaco"), through its undersigned counsel, hereby petitions for review of certain conditions contained in WYPDES Permit No. WY0040797 ("the Permit") issued by the Department of Environmental Quality ("DEQ") to Pennaco on December 31, 2008, and requests a hearing pursuant to the Environmental Quality Act, the Wyoming Administrative Procedure Act ("WAPA"), and the Rules of Practice and Procedure of the Environmental Quality Council ("EQC"). In support of this appeal, Petitioner advises the EQC as follows:

I. Information About the Petitioner

The petitioner filing this appeal is:

Pennaco Energy, Inc.
3601 Southern Drive
Gillette, Wyoming 82718

Petitioner is represented in this matter by Brent Kunz of Hathaway & Kunz, P.C., 2515 Warren Avenue, Suite 500, Cheyenne, Wyoming 82003 and by Duane Siler and John Martin of Patton Boggs LLP, 2550 M Street, Washington, D.C. 20037. Correspondence and information related to this appeal should be served on the undersigned counsel and on Mr. David T. Hill at Pennaco Energy, Inc. at the Gillette address above.

II. Action Being Appealed

Pennaco appeals the proposed permit limitations for Outfalls 025 and 032-038 (Wild Horse Creek) and 002-007, 010-024, 026-031, 039-045, and 047-048 (Middle Prong Wild Horse Creek) because DEQ has erroneously placed limits on effluent from these outfalls, including both direct discharges and discharges to on-channel reservoirs, for purposes of “irrigation use protection.” These effluent limits include end-of-pipe limits on specific conductance (EC) for all of these outfalls. In addition, the Statement of Basis – though not the permit -- says that end-of-pipe limits are imposed on SAR for those outfalls that are direct discharges. DEQ has notified Pennaco of its intent to administratively modify the permit to conform the permit to the Statement of Basis and impose end-of-pipe SAR limits on outfalls that direct-discharge to Middle Prong and Wild Horse Creek.

There is no “artificial” irrigation use of water in either of these drainages downstream from Pennaco’s discharges that are covered by the aforementioned outfalls, i.e., no diversion of water for irrigation of crops. DEQ has imposed “irrigation use protection limits” on the indicated outfalls solely because, according to DEQ, these discharges are located above, and may impact, “naturally irrigated bottomlands” as those areas are defined in DEQ’s Agricultural Use Protection Policy (“AUPP”).¹ DEQ’s application of the AUPP to “naturally irrigated bottomlands” is based on an

¹ Pennaco has consistently disputed the imposition of irrigation use protections under the AUPP on outfalls in this permit that are not located above artificial irrigation structures or uses. Pennaco stated in its July 3, 2008 renewal application that:

[N]aturally sub-irrigated lands have been recently identified along Middle Prong Wild Horse Creek. While Pennaco does not agree that the identified sub-irrigated areas are properly considered “irrigated lands” for purposes of the Chapter 1, Section 20 standard, we are providing irrigation monitoring points (IMP 1-IMP 8) locations above these sub-irrigated areas.

Section 23 of Pennaco’s permit application noted that artificially irrigated lands had been identified in a February 2006 Section 20 study for Middle Prong as being located in the upper reaches of the Middle Prong drainage on the Spellmans’ property above the discharges covered by the permit renewal. Subsequently,

erroneous assumption that vegetation on lands adjacent to ephemeral streams (or to streams perennialized by CBM discharges) is the result of natural irrigation from flows within the channel. Scientific information recently presented to the Environmental Quality Council in hearings on the proposed Agricultural Use Protection Rule demonstrates that such areas do not exist as a result of, and are not supported by, in-stream flows either through periodic overtopping and flooding or through subsurface migration. Rather, the requisite water to support vegetation in these stream-adjacent areas comes from precipitation runoff from areas outside the stream channel.²

Thus, vegetated areas that DEQ has identified from infrared photography as supposed “naturally irrigated bottomlands” adjacent to Wild Horse Creek and to Middle Prong are in fact areas of vegetation that are supported, not by water from either of those channels, but rather by other sources of nearby precipitation runoff which are unaffected by water quality in these drainages except during very rare flooding, during which any CBM water in the water that escapes the channel will be overwhelmed by the volume of associated precipitation runoff.³ It is unreasonable and arbitrary and capricious to set effluent limits in this WYPDES permit to protect supposed naturally

DEQ staff identified from aerial photography “naturally sub-irrigated lands” on lower reaches of Middle Prong and on Wild Horse Creek. DEQ then compelled Pennaco to designate IMPs for these bottomlands in order to have a technically sufficient application. In comments filed December 23, 2008, Pennaco again objected to irrigation protections for these bottomlands and requested that “the proposed permit be revised to remove all requirements associated with the protection of ‘naturally irrigated bottomlands.’” In those comments, Pennaco cited the Oct. 28, 2008 testimony of Andrew Strike, discussed below.

² See Testimony of Andrew Strike, Before the Environmental Quality Council; WQD Chapter 1, Section 20, Agricultural Water Supply, Transcript of Hearing Proceedings, p. 100, lines 3-16; p. 102, lines 11-21; p. 103, lines 13-15; p. 104, lines 2-8; p. 110, lines 13-17 (Oct. 28, 2008) (“Direct precipitation on soils and topography are the main factors responsible for the field productivity [O]verbank flows that occur are rare and of short duration and don’t supply significant water to the naturally irrigated lands. . . . [I]nfiltration plays a minimal role in supporting vegetation in areas beyond a very short distance from the stream bank [T]he amount of water that gets wicked out of the channel and is available for floodplain usage is only confined within 1 to 2 meters from where that water is running down the channel.”)

³ This is confirmed by the fact that these discharges have been in existence since the original issuance of WY0040797 in 2000. Even if CBM produced water discharges has been reaching these vegetated areas, the water self-evidently has had no detrimental effect on them.

irrigated bottomlands from EC, SAR or other pollutants in water to which these lands are *not* exposed.

The renewal permit's end-of-pipe limits under the AUPP on direct discharges above supposed "naturally irrigated bottom lands" are unlawful for the further reason that DEQ has failed to recognize or consider the draconian effects of the permit on Pennaco's ability to operate the impacted CBM wells. Pennaco has no feasible way to meet the SAR limits on the direct-discharge outfalls and will be required under the modified permit to shut in as many as 124 wells served by these outfalls. Pennaco has operated under WY0040797 and renewals thereof for many years without limits on SAR and has established infrastructure to manage water from these wells accordingly. In reliance on the absence of downstream irrigation uses, Pennaco has invested substantial resources in developing a partial treatment system for produced water from some of these 124 wells, to be operated only two months per year to reduce TDS and sodium to comply with DEQ's Powder River Assimilative Capacity Policy. Produced water from only some of the wells can feasibly be directed to the planned treatment unit -- which was not designed to operate year-round -- and, in any case, this produced water cannot be treated successfully to achieve the new end-of-pipe EC and SAR limits that DEQ has belatedly imposed in the renewed permit.

To now re-route all the wells to the proposed treatment plant and to upgrade it (assuming that is even technically feasible) would be cost-prohibitive and involve extensive damage to landowners' properties, leaving Pennaco no realistic alternative but to shut in the wells served by these outfalls. DEQ's failure to consider these impacts on Pennaco is irrational and arbitrary and capricious. DEQ should have recognized, among other things, that WY0040797 has been in effect since 2000 and all the discharges that would be covered by the renewed permit have been occurring without any harm to the environment for almost a decade. DEQ should have recognized the social and economic value of these produced water discharges to several landowners who rely on them for

livestock watering, as well as their value to the mineral owners to whom Pennaco pays royalties for this production. DEQ should have considered the technical impracticability of meeting the end-of-pipe EC and SAR limits and the unreasonably high cost to Pennaco associated with shutting in as many as a hundred or more CBM wells, including potentially the loss of some of these leases if Pennaco cannot produce methane gas from them. DEQ failed to consider any of these factors, or otherwise to consider either the reasonableness of imposing irrigation protection limitations on direct discharges occurring solely above ostensible “naturally irrigated bottomlands,” or the dramatically negative impact in this case of imposing those limits on Pennaco’s operations.⁴ Imposition of these new limits on discharges that have been in existence and permitted for almost a decade, without record evidence of harm to irrigated crops or soils, is arbitrary and capricious. Unless modified by the Council, these limits, under which Pennaco will have no alternative to shutting in substantial CBM production, will violate Pennaco’s due process rights and will take Pennaco’s property without just compensation.

⁴ While it was arbitrary and capricious under the Wyoming Administrative Procedure Act for DEQ to fail to consider these factors, it also appears that the water quality article of the Wyoming Environmental Quality Act requires the Water Quality Division to consider just such impacts in issuing a permit (as well as when recommending “permit systems” or standards for permits, also addressed in this section of the act):

In recommending any standards, rules, regulations or **permits** [to the director], the administrator . . . shall consider all the facts and circumstances bearing upon the reasonableness of the pollution involved including:

- (A) The character and degree of injury to or interference with the health and well being of the people, animals, wildlife, aquatic life and plant life affected;
- (B) The social and economic value of the source of pollution;
- (C) The priority of location in the area involved;
- (D) The technical practicability and economic reasonableness of reducing or eliminating the source of pollution; and
- (E) The effect upon the environment.

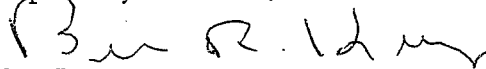
Wyo.Stat. Ann. § 35-11-302(a)(vi) (emphasis added).

III. Relief Requested

Petitioner respectfully requests that the EQC grant the following relief:

1. Grant Petitioner a contested case hearing on the challenged provisions of WYPDES Permit No. WY0040797 pursuant to the EQA, the WAPA, and the EQC's Rules of Practice and Procedure.
2. Finally determine Pennaco's application for renewal of WYPDES Permit No. WY0040797; reject the permit provisions referenced herein, i.e., end-of-pipe effluent limitations on EC and SAR to protect "irrigation" under DEQ's Agricultural Use Protection Policy, for any discharge under this permit; and order that the renewed permit shall be finally issued without those provisions.
3. Provide such other relief as the EQC determines just and reasonable under the circumstances.

Respectfully submitted,



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Dated: February 27, 2009

CERTIFICATE OF SERVICE

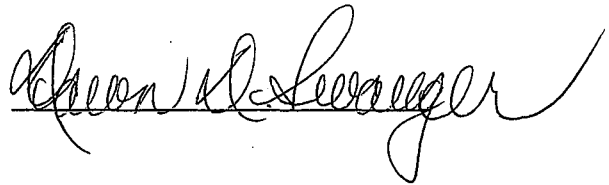
The undersigned certifies that on February 27, 2009, the foregoing Notice of Appeal and Petition for Hearing was served by hand as follows:

Original and 10 copies to:

Jim Ruby, Executive Secretary
Environmental Quality Council
Herschler Building, Room 114
122 West 25th Street
Cheyenne, Wyoming 82002

Two copies to:

John Corra, Director
Department of Environmental Quality
Herschler Building, 4th Floor West
122 West 25th Street
Cheyenne, Wyoming 82002

A handwritten signature in black ink, appearing to read "Donald A. Leavenger". The signature is written in a cursive style and is positioned on the right side of the page.