Dear Shareholder,

We are writing to you on behalf of landowners in Vermilion County, Illinois and regional stakeholders who stand to be affected by a proposed underground coal mine.

Stand Up To Coal is a grassroots association of farmers, landowners, villagers, and those who have a stake in the life and well-being of the Allerton, Broadlands, Fairmount, Homer and Sidell area of Champaign and Vermilion Counties in east central Illinois. Prairie Rivers Network (PRN) is the state affiliate of the National Wildlife Federation, a non-profit organization that strives to protect the rivers, streams and lakes of Illinois and to promote the lasting health and beauty of watershed communities.

This letter has been sent to those investing in Hallador Energy Company (NASDAQ: HNRG). As you may already know, a significant portion of Hallador's business is devoted to coal mining through Sunrise Coal, LLC – a wholly-owned subsidiary serving the electric power generation industry. Sunrise Coal has recently entered Vermilion County's rural communities with the intention of developing an underground coal mine approximately 23,000 acres in size.

The initial stages of the project began in 2009, when representatives started soliciting mineral rights and leases with landowners. Although the lease-signing process began covertly, within a year the work of Sunrise Coal became the most salient issue in the community. Living room conversations between Sunrise representatives and landowners soon shifted to village board meetings, packed with landowners firmly opposed to the mine as well as several who had signed mineral leases, but are now filled with regret and looking for a way out.

In public meetings across the county, Sunrise Coal has stated that they plan on opening the "Bulldog Mine" in 2014, but given widespread public opposition and ongoing struggles in acquiring necessary resources, this projected starting date may be overly idealistic.

Local landowners feel that they have been forced to sort through blatant misinformation broadcast by Sunrise Coal – and having read Hallador Energy Company's SEC filing, many suspect that investors have been victims of factual perversion as well. With this letter, we would like to draw attention to the setbacks and blunders of Sunrise Coal's effort that do not likely bode well for the stock of Hallador Energy, a company with expertise in oil and gas. The circulation of local knowledge has had a tremendous influence in delaying the mine's progress thus far, yet this perspective seldom reaches shareholders who may find the information to be indispensable.

Status of the Bulldog Mine: A Puzzle with (quite a few) Missing Pieces

With any coal mine, the company must acquire (1) Rights to the coal seam, (2) Land for processing the coal, (3) Access to those resources necessary for processing, (4) Access to shipment routes, and (5) Permits to proceed throughout the process.

1. Rights to the coal seam:

Sunrise Coal has been working to collect mineral leases for years, yet huge swaths of land remain out of reach. Several local residents, some with very large land holdings, are standing firm in denying access to the minerals beneath their family farms. While these inaccessible areas do not preclude the mining of coal where access has been given, each parcel that is not possessed makes the production process increasingly more expensive. Any coal company would prefer to mine swaths of coal deposits with only geologic restrictions, rather than continuously altering mining plans on a checkerboard with no guarantees of stability.

2. Land for processing coal:

Although Sunrise Coal has acquired the land to be used for surface facilities, there is no doubt that difficulties will be presented down the road in the realm of regulatory compliance. Some coal facilities across the state are placed in locations visible only to those driving by (or hardly visible at all), allowing costly regulatory mistakes to go unnoticed. The Sunrise facility, however, is in plain sight of residents who know the regulations – and are among those most staunchly opposed to the mine. This presents a critical variable that has not likely been considered in Hallador Energy's calculus.

3. Access to the resources necessary for processing:

A substantial portion of Sunrise Coal's efforts to this point has been focused on acquiring water – 20,000 gallons of treated water each day for drinking and shower houses and up to 500,000 gallons of typically untreated water to wash rock, clay, and other impurities from coal. The former was acquired last spring after a lengthy and contentious battle in the community, but access to untreated water was denied. The company was therefore forced to acquire 500,000 gallons of *treated* water to wash the coal.

Not only will Sunrise Coal need to pay a premium for treated water, but an additional cost will be required for the construction and maintenance of new infrastructure needed to pump the water 12 miles from the city contracting the water to the mine site. Before construction may begin, easements for the infrastructure remain to be acquired, either through the politically volatile (and legally suspect) act of eminent domain or through negotiation with dozens of individual landowners.

It remains to be answered whether Sunrise Coal is prepared to confront another grassroots effort and whether the lawyers of the Indiana-based company are sufficiently familiar with the intricacies of preemption and Illinois' water, eminent domain, and public utilities laws.

4. Access to shipment routes:

Not unlike the struggle Sunrise Coal is facing with mineral leases, rail spurs remain to be built connecting the processing facilities to the regional distribution network. While railroad easements have been negotiated with some landowners, a number of citizens with large and necessary property holdings are preventing construction and will continue to do so.

5. Permit acquisition:

At this point, Sunrise Coal has applied for a Surface Coal Mining and Reclamation Operations permit with the Illinois Department of Natural Resources. The application was returned, requiring far more corrections than the norm. As an Indiana company, Sunrise Coal continues to face challenges in working through the Illinois regulatory system. Moreover, as relatively small companies based out of state, Sunrise Coal and Hallador Energy may lack the political clout that has allowed for the continued survival of other coal companies in Illinois. Sunrise Coal has yet to file an application for the National Pollutant Discharge Elimination System (NPDES) permit required under the Clean Water Act to discharge polluted water from the washing process. This permit process could be expected to last approximately eighteen months.

Status of Coal: A Poor Investment for the Next 20 Years

Reconciling the position of Sunrise Coal and Hallador Energy, given the political environment in Illinois, is a difficult task. Reconciling Hallador Energy Company's interest in coal, rather than their traditional interest in gas and oil, is even more perplexing.

According to data from the Energy Information Administration, coal has been reclaiming a small portion of its market share in 2013.[1] The low gas prices that devastated the coal industry over the past two years were not sustainable in perpetuity. Colder winters, scaled-back drilling, and additional storage facilities have prevented the extreme surplus of gas on the market.

Nevertheless, coal is not in the place to be considered a contender with natural gas. In December 2013, "To Divest or Not to Divest? Options for Reducing Fossil Fuel Exposure" appeared as number 1 in the annual edition of MSCI's *ESG Trends to Watch*.[2] Investor concern stems from the notion of the "carbon bubble," that fossil fuel investments are currently overvalued and may become "stranded assets" with the implementation of stringent greenhouse gas limits.[3] As the report indicates:

"Purely from a financial perspective, even the outside chance that some reserves could become 'stranded assets' if a red line is breached should prompt a hard look at the assumptions underlying the valuation of fossil fuel producers… [It] could well be that if enough investors become concerned about a potential carbon bubble, there could be a self-fulfilling prophesy to how the financial community values current and future carbon reserves."[2]

As it stands, the US Environmental Protection Agency is finalizing stationary source limits on carbon dioxide that would effectively place a moratorium on the construction of new coal-fired power plants.[4] In order to meet carbon regulations, plants would be forced to turn to carbon capture and sequestration technology, which remains largely unproven on the commercial scale. Moreover, the Congressional Budget Office has indicated that plants using such storage technology can be expected to cost 75 percent more than traditional coal plants.[5] These are the prime conditions for the creation of stranded assets.

While new coal plants, averaging 1,768 pounds of carbon dioxide emissions per megawatt-hour, will be challenged to meet the 1,100 pound limit, the EPA is also on track to finalize carbon regulations applied to the 6,500 existing power plants by 2015. A recent study by Duke's Nicholas School of the Environment found that upwards of 65 percent of this existing coal fleet could become uneconomical by 2016.[6]

The future of coal in the United States is bleak. The U.S. Energy Information Administration projects that natural gas prices will stay under $6 per million BTU for the next two decades. As a result, the agency does not expect any coal plants will be built between 2018 and 2035.[7] Even upon considering energy use overseas, the future of coal exports does not provide a hopeful picture. Commenting on the position of coal, one Goldman Sachs analyst stated that "thermal coal's current position atop the fuel mix for global power generation will be gradually eroded … most thermal coal growth projects will struggle to earn a positive return."[8]

Political action is also working against exports. The United States has pledged to no longer finance overseas coal plants through the U.S. Export-Import Bank. Moreover the World Bank and European Investment Bank, both of which have provided $10 billion in assistance over the past five years, have also dropped their support.[8] Even those countries with the most demand may be changing course. A recent analysis by Citigroup predicts peak coal demand in China will flatten before 2020, or up to 15 years earlier than usually supposed.[9]

In light of these conditions, it is not surprising that Bevis Longstreth, Former SEC Commissioner, has urged investors to note "the rapidly changing future prospects for the major fossil fuel companies," and remove their holdings in such companies, avoiding stranded and worthless assets.[10]

If these experts are correct in predicting that coal assets are likely to be left stranded, this is not only a concern for investors, but for those in the local community as well. Community members have seen the impact of mining in towns across the state, many having suffered since tying their economies to the boom-and-bust cycle of the coal industry. Livelihoods and the vitality of communities have been linked to the land – the most productive and valuable farmland in America. Residents resist mining now for the protection of farmland, but there is increasing resistance to mining due to its poor economic prospects.

There is no doubt that Hallador Energy Company and Sunrise Coal face a difficult road ahead. We would be very interested in communicating our concerns in greater depth and would be happy to hear your thoughts as well. Feel free to contact us at standuptocoal@gmail.com or trotche@prairierivers.org. Additional information can be found at standuptocoal.org and prairierivers.org. Thank you.

Sincerely,

Members of Stand Up to Coal

&

Tyler A. Rotche
Water Policy Specialist, Prairie Rivers Network

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