

SXCP Qualifying Income Status FAQs

June 2015

Does SXCP qualify for MLP status?

- Yes
- Pursuant to Internal Revenue Code Section 7704(c)(2), in order to qualify for MLP status, more than 90 percent of the income of a partnership must be from the exploration, development, mining or production, *processing*, *refining*, marketing and transportation of minerals and natural resources
- It is an established principal of statutory interpretation that when the terms of a statute are not defined, as in this case, those terms should be given their ordinary and accepted meanings
- We believe that the conversion of coal to coke is both *processing* and *refining* within the common sense meaning of those terms; therefore, we believe that more than 90% of SXCP's income is derived from qualifying sources as required by Section 7704(c)(2)

How did SXCP originally determine if cokemaking generated qualifying income?

- SXCP worked with outside counsel, Vinson & Elkins
- At the time of its IPO, SXCP received an opinion from Vinson & Elkins stating that following the closing of the IPO, SXCP's income generated from cokemaking is qualifying income under Section 7704(d)(1)(E)
- Vinson & Elkins has advised us that after considering the analysis and discussion in the release issuing the proposed regulations, they have not changed their opinion that cokemaking is *processing* and/or *refining* as those terms are used in Code Section 7704(d)(1)(E)
- Vinson & Elkins also concurred with our conclusion that SXCP should seek clarification of the proposed regulations through the comment process to eliminate any uncertainty regarding cokemaking created by the way the proposed regulations attempt to define *processing*

What is a "will opinion"?

- The opinion we received from Vinson & Elkins is a "will level" opinion. A will level opinion is the highest level opinion a law firm can provide; these are provided based on a thorough review and understanding of the statute and legislative history and a determination by the law firm that the matter opined upon will comply as opposed to may, should or likely will comply

Will SXCP continue to qualify for MLP status under the proposed new MLP regulations?

- We believe we will
- The proposed regulations provide that "an activity constitutes...refining of ores or minerals if it meets the definition of ...refining under [current Treasury Regulation] §1.613-4(g)(6)(iii)..."
- Treasury Regulation § 1.613-4(g)(6)(iii) states "the term refining refers to processes...used to eliminate impurities or foreign matter from smelted or partially processed metallic and nonmetallic ores and minerals, as, for example, the refining of blister copper. In general, a refining process is designed to achieve a high degree of purity by removing relatively small amounts of impurities or foreign matter from smelted or partially processed ores or minerals
- Cokemaking involves heating coal to high temperature in an oxygen deficient atmosphere in order to concentrate the carbon and eliminate impurities, including water, coal-gas, and coal-tar
- Coke, like coal, is a fuel; but, as a purer form of carbon, it is suitable for use in smelting iron ore and has historically been burned instead of coal, where less smoke is desired
- Cokemaking is very similar to the smelting of metallic ores and the conversion of crude oil to petroleum coke, which are other qualifying activities
- Further, we believe that when you apply the word *processing* or *refining* to what occurs in converting coal to coke, it is common sense that cokemaking would be considered *processing* and/or *refining*

- Therefore, under the proposed new regulations, we believe we will continue to qualify for MLP status as a *refiner* of ores or minerals as defined in the Treasury Regulation 1.613-4(g)(6)(iii) even if the regulations are finalized in their current form

Why, then, did SXCP file comments on the proposed regulations with the IRS?

- In our comment letter, we are asking the IRS to change the manner in which the proposed regulations define *processing* ores and minerals
- The core of the problem we have with the current regulation's definition of *processing* is that the proposed regulations appear to limit the meaning of *processing* of ores and minerals to "mining processes"
- However, the commonly understood meaning of *processing*, like *refining*, is that it occurs after mining, which is itself, a qualifying activity under Section 7704(d)(1)(E). Therefore, we believe the proposed regulations should use the commonly understood meaning of the word *processing* and clearly define the term to include activities like cokemaking which occurs after mining
- While we are generally ok with the definition of *refining* in the proposed new regulations, for the sake of clarity, we would like to see the definition of *processing* in the final regulations specifically identify cokemaking as a qualifying activity
- We note that the proposed regulations clearly identify the conversion of crude oil to petroleum coke as a qualifying *processing* and *refining* activity within the meaning of Section 7704(d)(1)(E). We do not believe that the IRS intends that the conversion of coal to coke be treated differently, and therefore, the IRS should make the clarifications we are seeking
- Our comments to the IRS request that the final regulations clearly reflect this common sense approach

How did the IRS's proposed new MLP regulations impact the growth opportunities you are considering?

- We are focused on growing both organically via greenfield development and inorganically via the acquisition of other industrial materials businesses that generate MLP qualifying income
- We are pursuing a variety of opportunities in a variety of industrial materials verticals that will generate qualifying income under the proposed new regulations, and the pipeline of potential opportunities we may pursue remains robust under the proposed new regulations
- We believe that if the meaning of *refining* and *processing* under the proposed new MLP regulations more closely conform to the common sense meaning of these terms as used in Section 7704(d)(1)(e), we will have a somewhat broader scope of growth opportunities to pursue which generate qualifying income

Why didn't you seek a Private Letter Ruling (PLR) for cokemaking when SXCP went public?

- Generally, PLRs are obtained when a taxpayer is uncertain of how the IRS would tax a specific activity; after reviewing our cokemaking activity with Vinson & Elkins, our outside counsel, we concluded that the cokemaking activities would qualify as *refining* and *processing* of a natural resource based on Code Section 7704(d)(1)(E)
- Vinson & Elkins provided a *will opinion*, and a PLR was not pursued

Why did you seek PLR's for iron ore and DRI?

- While the concentrating, pelletizing and direct reduction of iron ore (DRI) is *processing* or *refining* of an ore and appear to qualify, upon review of the specific activities with Vinson & Elkins, we concluded a PLR was necessary as Vinson & Elkins was uncertain as to whether they could provide us a *will opinion* on those specific activities
- We are reviewing the status of these PLRs in view of the proposed new regulations

What happens at the IRS once comments have been submitted?

- The comment period on the proposed new regulations ends on August 5, 2015. When the comment period closes, the IRS will review and analyze the comments received. During this time, they may consult with

industry experts and others to fully understand the matter. However, there is no set time frame for this process and it can take months or years to finalize the proposed new regulations

What are the impacts to SXC and SXCP assuming the IRS regulations no longer consider cokemaking a qualifying activity?

- We believe SXCP will continue to qualify for MLP status once the final regulations are implemented
- However, given that we have acted reasonably and prudently, in the unlikely scenario where SXCP no longer qualifies, we will receive the 10-year transition period the IRS outlines in their proposed regulations and will be allowed to treat the income earned from cokemaking as qualifying income