

COVANTA HOLDING CORP

Form 10-K

February 26, 2008

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**UNITED STATES SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549**

Form 10-K

- ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the fiscal year ended December 31, 2007**
- or**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the transition period from to**

Commission file number: 1-06732
COVANTA HOLDING CORPORATION
(Exact name of registrant as specified in its charter)

Delaware
*(State or Other Jurisdiction of
Incorporation or Organization)*

40 Lane Road, Fairfield, N.J.
(Address of Principal Executive Offices)

95-6021257
*(I.R.S. Employee
Identification No.)*

07004
(Zip Code)

**Registrant's telephone number, including area code:
(973) 882-9000**

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, \$0.10 par value per share	New York Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: N/A

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act. Yes No

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Exchange Act. Yes No

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was

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required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes No

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting Company
(Do not check if a smaller reporting company)

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes No

As of June 29, 2007, the aggregate market value of the registrant's common stock held by non-affiliates of the registrant was \$2,962,710,442. The aggregate market value was computed by using the closing price of the common stock as of that date on the New York Stock Exchange. (For purposes of calculating this amount only, all directors and executive officers of the registrant have been treated as affiliates.)

Indicate the number of shares outstanding of each of the registrant's classes of common stock, as of the latest practicable date.

Class	February 14, 2008
Common Stock, \$0.10 par value per share	153,921,882 shares

Documents Incorporated By Reference:

Part of Form 10-K of Covanta Holding Corporation

Documents Incorporated by Reference

Part III

Portions of the Proxy Statement to be filed with the Securities and Exchange Commission in connection with the Annual Meeting of Stockholders.

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CAUTIONARY NOTE REGARDING FORWARD-LOOKING STATEMENTS

Certain statements in this Annual Report on Form 10-K may constitute forward-looking statements as defined in Section 27A of the Securities Act of 1933 (the Securities Act), Section 21E of the Securities Exchange Act of 1934 (the Exchange Act), the Private Securities Litigation Reform Act of 1995 (the PSLRA) or in releases made by the Securities and Exchange Commission (SEC), all as may be amended from time to time. Such forward-looking statements involve known and unknown risks, uncertainties and other important factors that could cause the actual results, performance or achievements of Covanta Holding Corporation and its subsidiaries (Covanta) or industry results, to differ materially from any future results, performance or achievements expressed or implied by such forward-looking statements. Statements that are not historical fact are forward-looking statements. Forward-looking statements can be identified by, among other things, the use of forward-looking language, such as the words plan, believe, expect, anticipate, intend, estimate, project, may, will, would, could, should, seeks, similar words, or the negative of these terms or other variations of these terms or comparable language, or by discussion of strategy or intentions. These cautionary statements are being made pursuant to the Securities Act, the Exchange Act and the PSLRA with the intention of obtaining the benefits of the safe harbor provisions of such laws. Covanta cautions investors that any forward-looking statements made by Covanta are not guarantees or indicative of future performance. Important assumptions and other important factors that could cause actual results to differ materially from those forward-looking statements with respect to Covanta, include, but are not limited to, the risks and uncertainties affecting its businesses described in Item 1A. Risk Factors of this Annual Report on Form 10-K for the year ended December 31, 2007 and in other filings by Covanta with the SEC.

Although Covanta believes that its plans, intentions and expectations reflected in or suggested by such forward-looking statements are reasonable, actual results could differ materially from a projection or assumption in any of its forward-looking statements. Covanta s future financial condition and results of operations, as well as any forward-looking statements, are subject to change and inherent risks and uncertainties. The forward-looking statements contained in this Annual Report on Form 10-K are made only as of the date hereof and Covanta does not have, or undertake, any obligation to update or revise any forward-looking statements whether as a result of new information, subsequent events or otherwise, unless otherwise required by law.

AVAILABILITY OF INFORMATION

You may read and copy any materials Covanta files with the SEC at the SEC s Public Reference Room at 100 F Street, N.E., Room 1580, Washington, D.C. 20549. Copies of such materials also can be obtained at the SEC s website, www.sec.gov or by mail from the Public Reference Room of the SEC, at prescribed rates. Please call the SEC at 1-800-SEC-0330 for further information on the Public Reference Room. Covanta s SEC filings are also available to the public, free of charge, on its corporate website, www.covantaholding.com as soon as reasonably practicable after Covanta electronically files such material with, or furnishes it to, the SEC. Covanta s common stock is traded on the New York Stock Exchange. Material filed by Covanta can be inspected at the offices of the New York Stock Exchange at 20 Broad Street, New York, N.Y. 10005.

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PART I

Item 1. BUSINESS

The terms we, our, ours, us, Covanta and Company refer to Covanta Holding Corporation and its subsidiaries. The term Covanta Energy refers to our subsidiary Covanta Energy Corporation and its subsidiaries.

About Covanta Holding Corporation

We are a leading developer, owner and operator of infrastructure for the conversion of waste to energy (known as energy-from-waste), as well as other waste disposal and renewable energy production businesses in the United States, Europe and Asia. We are organized as a holding company which was incorporated in Delaware on April 16, 1992. We conduct all of our operations through subsidiaries which are engaged predominantly in the businesses of waste and energy services. We also engage in the independent power production business outside the United States.

We own, have equity investments in, and/or operate 57 energy generation facilities, 47 of which are in the United States and 10 of which are located outside the United States. Our energy generation facilities use a variety of fuels, including municipal solid waste, wood waste (biomass), landfill gas, water (hydroelectric), natural gas, coal, and heavy fuel-oil. We also own or operate several businesses that are associated with our energy-from-waste business, including a waste procurement business, three landfills, and several waste transfer stations.

Revenues were \$1,433 million, \$1,269 million and \$979 million and operating income was \$237 million, \$227 million and \$146 million for the years ended December 31, 2007, 2006 and 2005, respectively. The increase in revenues and operating income over the past three years is primarily attributable to the successful execution of our operating and growth strategies described below and in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Overview, Acquisitions and Business Development*.

Our Business Strategy

Our mission is to be the world's leading energy-from-waste company, with a complementary network of other renewable energy generation and waste disposal assets. We expect to build value for our stockholders by satisfying our clients' waste disposal and energy generation needs with safe, reliable and environmentally superior solutions. In order to accomplish this mission and create additional value for our stockholders, we are focused on:

- providing customers with superior service and effectively managing our existing businesses;
- generating sufficient cash to meet our liquidity needs and invest in the business; and
- developing new projects and making acquisitions to grow our business in the United States, Europe and Asia.

Our business is capital intensive because it is based on building and operating municipal solid waste processing and energy generating facilities. In order to provide meaningful growth through development, we must be able to invest our funds, obtain equity and/or debt financing, and provide support to our operating subsidiaries. During the first quarter of 2007, we completed a comprehensive recapitalization utilizing a series of equity and debt financings. With this refinancing, we now have greater flexibility to pursue strategic opportunities by investing in our business and making acquisitions. Additional information related to our recapitalization is described in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources - 2007 Recapitalization* and Note 6. Long-Term Debt of the Notes to the Consolidated Financial Statements (Notes).

Our senior management team has extensive experience in developing, constructing, operating, acquiring and integrating waste and energy services businesses. We intend to continue to focus our efforts on pursuing development

and acquisition-based growth. We anticipate that a part of our future growth will come from acquiring or investing in additional energy-from-waste, waste disposal and renewable energy production businesses in the United States, Europe and Asia.

Our domestic project development efforts include working with our client communities to expand existing energy-from-waste project capacities, new energy-from-waste and other renewable energy projects, contract

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extensions, and businesses ancillary to our existing businesses, such as additional waste transfer, transportation, processing and landfill businesses.

We are pursuing international waste and/or energy business opportunities, particularly in markets where the market demand, regulatory environment or other factors encourage technologies such as energy-from-waste in order to reduce dependence on landfilling. In particular, we are focusing on the United Kingdom, Ireland and China, as well as Italy, Canada and certain other countries.

During 2007, we expanded our network of waste and energy services businesses through acquisitions, equity investments and additional operating and development contracts. In our domestic business, we added three energy-from-waste facilities, one ash landfill, five transfer stations and two biomass projects. In addition, we completed the expansion of the energy-from-waste facility located in and owned by Lee County, Florida, and continued to make progress on the expansion of the Hillsborough County, Florida energy-from-waste facility. In our international business, we announced that we have entered into definitive agreements for the development of a 1,700 metric ton per day (tpd) energy-from-waste project serving the City of Dublin, Ireland and surrounding communities. We also purchased an equity interest in one company and agreed to acquire an equity interest in another company both of which are located in China and will be used to develop energy-from-waste projects in China, and one of which has equity interests in two existing energy-from-waste facilities. Additional information related to our acquisitions and business development during 2007 is described in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Overview Acquisitions and Business Development*.

We believe that our business offers solutions to public sector leaders around the world in two related elements of critical infrastructure: waste disposal and renewable energy generation. We believe that the environmental benefits of energy-from-waste, as an alternative to landfilling, are clear and compelling: utilizing energy-from-waste reduces greenhouse gas (GHG) emissions, lowers the risk of groundwater contamination, and conserves land. At the same time, energy-from-waste generates clean, reliable energy from a renewable fuel source, thus reducing dependence on fossil fuels, the combustion of which is itself a major contributor to GHG emissions. As public planners in the United States, Europe and Asia address their needs for more environmentally sensitive waste disposal and energy generation in the years ahead, we believe that energy-from-waste will be an increasingly attractive alternative.

Business Segments

Prior to January 1, 2007, we had two reportable business segments – Waste and Energy Services and Other Services. Given our increased focus on developing our international business, during the first quarter of 2007, we segregated what we previously reported as our Waste and Energy Services segment into two new segments: Domestic and International. Our remaining operations, which we previously reported as our Other Services segment and was comprised of the holding company and insurance subsidiaries' operations, did not meet the quantitative thresholds which required separate disclosure as a reportable segment. Therefore, our reportable segments are now Domestic and International, which are comprised of our domestic and international waste and energy services operations, respectively.

The financial results of the holding company primarily consist of interest expense and income. General and administrative expenses related to officer salaries, legal and other professional fees and insurance are reimbursed by the operating subsidiaries.

Our predominant business is the waste and energy services business, however our historical consolidated operations were conducted in the insurance industry prior to the acquisition of Covanta Energy in March 2004. Our insurance business continues to represent an important element of our structure in that our net operating loss carryforwards (NOLs) were primarily generated through the operations of these former subsidiaries. See Note 9. Income Taxes of

the Notes for more information about our NOLs.

Additional information about our business segments is contained in *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Overview Business Segments* and in Note 5. Financial Information by Business Segments of the Notes.

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DOMESTIC BUSINESS

Energy-From-Waste Projects

Energy-from-waste projects have two essential purposes: to provide waste disposal services, typically to municipal clients who sponsor the projects, and to use that waste as a fuel source to generate renewable energy. The electricity or steam generated is generally sold to local utilities or industrial customers, and most of the resulting revenues reduce the overall cost of waste disposal services to the municipal clients. These projects are capable of providing waste disposal services and generating electricity or steam, if properly operated and maintained, for several decades. Generally, we provide these waste disposal services and sell the electricity and steam generated under long-term contracts, which expire on various dates between 2008 and 2034. Many of our service contracts may be renewed for varying periods of time, at the option of the municipal client.

We receive revenue in the form of fees pursuant to the service or waste contracts, and in some cases, energy purchase agreements, at facilities we own or operate. We market waste disposal services to third parties predominantly to efficiently utilize that portion of the waste disposal capacity of our energy-from-waste projects which is not dedicated to municipal clients.

We currently operate energy-from-waste projects in 15 states. Most of our energy-from-waste projects were developed and structured contractually as part of competitive procurement processes conducted by municipal entities. As a result, many of these projects have common features. However, each service agreement is different reflecting the specific needs and concerns of a client community, applicable regulatory requirements and other factors. The following describes features generally common to these agreements, as well as important distinctions among them:

We design the facility, help to arrange for financing and then we either construct and equip the facility on a fixed price and schedule basis, or we undertake an alternative role, such as construction management, if that better meets the goals of our municipal client.

For the domestic energy-from-waste projects we own, financing is generally accomplished through tax-exempt and taxable revenue bonds issued by or on behalf of the client community. For these facilities, the bond issuer loans the bond proceeds to us to pay for facility construction and to fund a debt service reserve for the project, which is generally sufficient to pay principal and interest for one year. Project-related debt is included as project debt and the debt service reserves are included as restricted funds held in trust in our consolidated financial statements. Generally, project debt is secured by the revenues pledged under the respective indentures and is collateralized by the facility and the contracts and other assets of our project subsidiary.

Following construction and during operations, we receive revenue from two primary sources: fees we receive for operating projects or for processing waste received, and payments we receive for electricity and/or steam we sell. We have 24 energy-from-waste projects at which we receive a fixed fee (which escalates over time pursuant to contractual indices) which we refer to as having a Service Fee structure. We also have 10 energy-from-waste projects at which we receive a per-ton fee under contracts for processing waste, which we refer to as having a Tip Fee structure. At our Tip Fee projects, we contract on both a long-term and short-term basis to utilize project disposal capacity, and as such we have a greater exposure to waste market price fluctuation, as well as a greater exposure to project operating disruptions that may cause us to reduce waste acceptance.

At projects we own where a Service Fee structure exists, a portion of the revenue we receive represents payments by the client community of debt service on project debt, which we pass along to a bond trustee for payment to bondholders of principal and interest when due. These payments will continue until cash in project debt service reserves is sufficient to pay all remaining debt service payments. Generally, this occurs in the final

year of the service contracts, and during that year we will receive little or no payments representing project debt principal, and as a result we record little or no cash provided by operating activities during that period with respect to the debt for such projects.

We generally sell the energy output from our projects to local utilities pursuant to long-term contracts. Where a Service Fee structure exists, our client community usually retains most (generally 90%) of the energy revenues generated and pays the balance to us. Where Tip Fee structures exist, we retain 100% of the

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energy revenues. At three of our projects, we sell energy output under short-term contracts or on a spot-basis into the regional electricity grid. At our Tip Fee projects, we generally have a greater exposure to energy market price fluctuation, as well as a greater exposure to variability in project operating performance.

We agree to operate the facility and meet minimum waste processing capacity and efficiency standards, energy production levels and environmental standards. Failure to meet these requirements or satisfy the other material terms of our agreement (unless the failure is caused by our client community or by events beyond our control), may result in damages charged to us or, if the breach is substantial, continuing and unremedied, termination of the applicable agreement. These damages could include amounts sufficient to repay project debt (as reduced by amounts held in trust and/or proceeds from sales of facilities securing project debt) and as such, these contingent obligations cannot readily be quantified. We have issued performance guarantees to our client communities and, in some cases other parties, which guarantee that our project subsidiaries will perform in accordance with contractual terms including, where required, the payment of such damages. In circumstances where one or more contracts have been terminated for our default, these contractual damages may be material to our cash flow and financial condition. To date, we have not incurred material liabilities under such performance guarantees.

The client community generally must deliver minimum quantities of municipal solid waste to the facility on a put-or-pay basis and is obligated to pay a fee for its disposal. A put-or-pay commitment means that the client community promises to deliver a stated quantity of waste and pay an agreed amount for its disposal, regardless of whether the full amount of waste is actually delivered. Where a Service Fee structure exists, portions of the service fee escalate to reflect indices for inflation, and in many cases, the client community must also pay for other costs, such as insurance, taxes, and transportation and disposal of the ash residue to the disposal site. Generally, expenses resulting from the delivery of unacceptable and hazardous waste on the site are also borne by the client community. In addition, the contracts generally require the client community to pay increased expenses and capital costs resulting from unforeseen circumstances, subject to specified limits. At three publicly-owned facilities we operate, our client community may terminate the operating contract under limited circumstances but without cause.

Our service and waste disposal agreements, as well as our energy contracts, expire at various times. The extent to which any such expiration will affect us will depend upon a variety of factors, including whether we own the project, market conditions then prevailing, and whether the municipal client exercises options it may have to extend the contract term. As our contracts expire, we will become subject to greater market risk in maintaining and enhancing our revenues. As service agreements at municipally-owned facilities expire, we intend to seek to enter into renewal or replacement contracts to operate such facilities. We will also seek to bid competitively in the market for additional contracts to operate other facilities as similar contracts of other vendors expire. As our service and waste disposal agreements at facilities we own or lease begin to expire, we intend to seek replacement or additional contracts, and because project debt on these facilities will be paid off at such time, we expect to be able to offer rates that will attract sufficient quantities of waste while providing acceptable revenues to us. At facilities we own, the expiration of existing energy contracts will require us to sell our output either into the local electricity grid at prevailing rates or pursuant to new contracts. See discussion under *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Overview Contract Duration* for additional information concerning the expiration of existing contracts.

To date, we have been successful in extending our existing contracts to operate energy-from-waste facilities owned by municipal clients where market conditions and other factors make it attractive for both us and our municipal clients to do so. See discussion under *Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations Overview Acquisitions and Business Development* for additional information concerning development projects. The extent to which additional extensions will be attractive to us and to our municipal clients who own their projects will depend upon the market and other factors noted above. However, we do not believe that either our success or lack of success in entering into additional negotiated extensions to operate such facilities will have a

material impact on our cash flow and profitability. See *Item 1A. Risk Factors* *We may face increased risk of market influences on our revenues after our contracts expire.*

In conjunction with our domestic energy-from-waste business, we also operate ten transfer stations and three landfills in the northeast United States, which we utilize to supplement and manage more efficiently the fuel and ash

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disposal requirements at our energy-from-waste operations. We provide waste procurement services to our waste disposal and transfer facilities which have available capacity to receive waste. With these services we seek to maximize our revenue and ensure that our energy-from-waste facilities are being utilized most efficiently, taking into account maintenance schedules and operating restrictions that may exist from time to time at each facility. We also provide management and marketing of ferrous and non-ferrous metals recovered from energy-from-waste operations, as well as services related to non-hazardous special waste destruction and residue management for our energy-from-waste projects.

Other Renewable Energy Projects

We also engage domestically in developing, owning and/or operating renewable energy production facilities utilizing a variety of energy sources including waste wood (biomass), water (hydroelectric), and landfill gas. We sell the electrical output from each facility, with one exception, to local utilities. We derive our revenues from these facilities primarily from the sale of energy and capacity under energy contracts.

Biomass We own five wood-fired generation facilities and have a 55% interest in a partnership which owns a sixth wood-fired generation facility, all of which are located in California. We procure fuel for the facilities from local sources, primarily through short-term supply agreements. The price of the fuel varies depending on the time of the year, supply and price of energy. These projects sell energy and capacity to utilities under energy contracts that expire between 2014 and 2017.

Hydroelectric We own a 50% equity interest in two run-of-river hydroelectric facilities which have a combined gross generating capacity of 17 megawatts (MW). Both facilities are located in the State of Washington and both sell energy and capacity to Puget Sound Energy under long-term energy contracts. We provide operation and maintenance services at one of the facilities under a cost plus fixed-fee agreement.

Landfill Gas We own and operate four landfill gas projects located in California and one in Massachusetts which produce electricity by burning methane gas produced in landfills. These projects sell energy to various utilities. Upon the expiration of the energy contracts, we expect that these projects will enter into new power off-take arrangements or will be shut down.

Summary information with respect to our domestic projects that are currently operating is provided in the following table:

	Location	Design Capacity		Nature of Interest	Contract Expiration Dates		
		Waste Disposal (TPD)	Gross Electric (MW)		Service/Waste Disposal	Energy	
A. ENERGY-FROM-WASTE PROJECTS							
TIP FEE STRUCTURES							
1.	Alexandria/Arlington	Virginia	975	22.0	Owner/Operator	2013	2023
2.	Delaware Valley	Pennsylvania	2,688	87.0	Lessee/Operator	2017	2016
3.	Haverhill	Massachusetts	1,650	44.6	Owner/Operator	N/A	2019
4.	Hempstead(1)	New York	2,671	75.0	Owner/Operator	2034	2009
5.	Niagara(2)	New York	2,250	50.0	Owner/Operator	N/A	2014
6.	Pittsfield	Massachusetts	240	8.6	Owner/Operator	2015	2015

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7.	Southeast Massachusetts(3)	Massachusetts	2,700	78.0	Owner/Operator	N/A	2015
8.	Springfield	Massachusetts	400	9.4	Owner/Operator	2014	2010
9.	Union County	New Jersey	1,440	42.1	Lessee/Operator	2023	N/A
10.	Warren County	New Jersey	450	13.5	Owner/Operator	N/A	2013

SERVICE FEE STRUCTURES

11.	Babylon	New York	750	16.8	Owner/Operator	2019	2019
12.	Bristol	Connecticut	650	16.3	Owner/Operator	2014	2014
13.	Detroit(2)(3)(4)	Michigan	2,832	68.0	Lessee/Operator	2009	2008
14.	Essex County	New Jersey	2,700	64.0	Owner/Operator	2020	2020
15.	Fairfax County	Virginia	3,000	93.0	Owner/Operator	2011	2015
16.	Harrisburg(5)	Pennsylvania	800	20.8	Operator	2018	2009
17.	Hartford(3)(6)	Connecticut	2,000	68.5	Operator	2012	2012
18.	Hennepin County	Minnesota	1,212	38.7	Operator	2018	2018
19.	Hillsborough County(7)	Florida	1,800	46.5	Operator	2027	2010
20.	Honolulu(3)(4)	Hawaii	2,160	57.0	Lessee/Operator	2010	2015
21.	Huntington(8)	New York	750	24.3	Owner/Operator	2012	2012

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			Design Capacity			Contract Expiration Dates	
		Location	Waste Disposal (TPD)	Gross Electric (MW)	Nature of Interest	Service/Waste Disposal	Energy
22.	Huntsville(2)	Alabama	690		Operator	2016	2014
23.	Indianapolis(2)(9)	Indiana	2,362	6.5	Owner/Operator	2008	2028
24.	Kent County(2)	Michigan	625	16.8	Operator	2010	2022
25.	Lake County	Florida	528	14.5	Owner/Operator	2014	2014
26.	Lancaster County	Pennsylvania	1,200	33.1	Operator	2016	2016
27.	Lee County	Florida	1,836	57.3	Operator	2024	2015
28.	Marion County	Oregon	550	13.1	Owner/Operator	2014	2014
29.	Montgomery County	Maryland	1,800	63.4	Operator	2016	2010
30.	Onondaga County	New York	990	36.8	Owner/Operator	2015	2025
31.	Pasco County	Florida	1,050	29.7	Operator	2011	2024