

# Unfair Market Value:

## By Ignoring Exports, BLM Underprices Federal Coal



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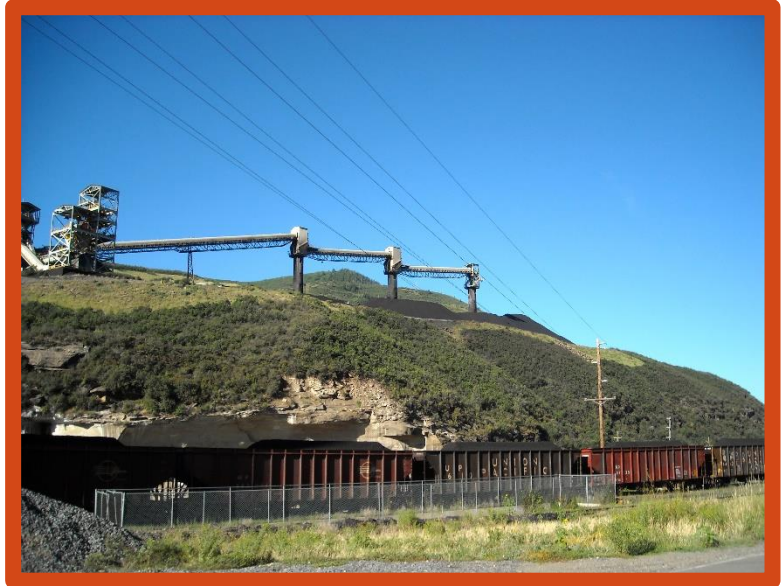
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## Executive Summary

As demand for coal in the United States has declined over the past several years, coal companies have focused on selling more coal to customers overseas, particularly in Asia. Many of these companies have found that coal exports can yield higher revenues and better profit margins than domestic sales, and are now seeking new sources of coal for export markets.

Coal companies operating in the western United States purchase much of their coal through federal coal leasing programs operated by the Bureau of Land Management (BLM), which allow private coal companies to mine and sell coal owned by the American public. Although a growing share of federal coal is exported to overseas customers, the BLM has almost completely ignored the value of export sales when determining the minimum price it will accept for federally owned coal. The failure to assess the economics of coal exports has led the agency to systematically underprice coal owned by the American public, potentially leading to millions of dollars in foregone revenue each year.



This report documents cases in which coal companies have purchased low-cost federal coal, and then resold it overseas at much higher prices. It also documents examples of coal companies that have clearly stated their intention to export even more federal coal in the future. Examples include:

- **Spring Creek Mine, MT.** Cloud Peak reports that it sold 18 million tons of coal to Asian customers from the beginning of 2010 through the first quarter of 2014. The large majority of this coal came from the company's Spring Creek Mine, where Cloud Peak purchased federal coal for \$0.18 per ton. Cloud Peak has developed an ambitious export growth strategy centered on Spring Creek, and has applied for a new 198 million ton coal lease adjacent to the existing mine to supply its export plans.
- **Decker Mine, MT.** Ambre Energy, co-owner of Montana's Decker Mine, markets itself to potential investors as a "vertically integrated" coal export firm that owns both coal mines and coal terminal assets. Ambre has signed long-term coal export agreements to ship up to 5 million tons of coal to Korean utilities per year for 10 years. The company is now seeking an additional 40 million tons of coal on land adjacent to Decker to fulfill its export ambitions.
- **Signal Peak Mine, MT.** Signal Peak Energy, a three-way venture between the Boich Companies, FirstEnergy, and international energy trading firm Gunvor, purchased 35.5 million tons of federal coal for just \$0.30 per ton. In recent years, the company has exported roughly 4 million tons of coal per year to Asia.

- **Bowie Resource Partners.** This mining company, operating in both Utah and Colorado, has export agreements to load up to 3.5 million tons of coal per year for export markets, and has sought additional port capacity to boost its exports. Bowie has asked the BLM for a new 8 million ton coal lease, and the agency has scheduled the lease sale for July 30, 2014. Given the company's statements and actions, it is likely that a substantial portion of any newly leased coal would be sent to overseas markets.
- **West Elk Mine, CO.** Arch Coal shipped half of the output of this bituminous thermal coal mine to Asia in 2013. The company is seeking to expand its reserves with an additional 10.1 million ton coal lease, located largely on US Forest Service lands.
- **Kinney Mine, UT.** In presentations to investors, New Horizon Coal emphasizes Kinney's export advantages—including rail and road infrastructure that provides access to export markets, and a 3 million ton per year port allocation agreement for shipping coal via ocean-going vessels.
- **Mines in the Southern Powder River Basin, WY.** Several major coal producers operating large mines in the southern Powder River Basin (PRB) have shipped coal obtained through federal leases to overseas customers. Arch Coal and Peabody Energy both are seeking additional export capacity at proposed ports in the Pacific Northwest—capacity that the companies hope to fill with PRB coal.

These examples represent only a selection of the publicly owned coal that has already been sold, or that is intended for future sale, to overseas customers. Some energy market analysts even believe that exports have the potential to affect coal markets in more fundamental ways, by creating scarcity in domestic coal markets that could boost prices for domestic coal consumers. And as with all coal sales, coal exports carry significant costs for the climate, air and water quality, and human health – costs that are borne by the public, but are not incorporated into the price that private coal companies pay for federally owned coal.

Given the coal industry's clearly stated intention to expand coal exports, federal officials now have both a duty and an opportunity to conduct a comprehensive review of the economics of coal exports when assessing the "fair market value" of federal coal sold to private firms.

## Introduction

Between 2006 and 2012, US coal companies exported more than 86 million tons of coal from mines in Wyoming, Utah, Colorado, and Montana to customers in Asia, Europe, and other foreign destinations.<sup>1</sup> (See Table 1.)

**Table 1. Coal exports volumes from select states in the Western US, 2006-2012**

	Wyoming	Montana	Colorado	Utah	Total 4 states
<b>2006</b>	5,622,000	447,000	799,000	55,000	<b>6,923,000</b>
<b>2007</b>	7,626,000	387,000	345,000	0	<b>8,358,000</b>
<b>2008</b>	6,094,000	1,480,000	874,000	541,000	<b>8,989,000</b>
<b>2009</b>	3,016,000	2,065,000	850,000	148,000	<b>6,079,000</b>
<b>2010</b>	5,237,000	6,432,000	2,195,000	634,000	<b>14,498,000</b>
<b>2011</b>	4,471,000	13,199,000	3,000,000	1,081,000	<b>21,751,000</b>
<b>2012</b>	3,128,600	9,084,800	6,507,300	1,080,000	<b>19,800,700</b>
<b>Total</b>	<b>35,194,600</b>	<b>33,094,800</b>	<b>14,570,300</b>	<b>3,539,000</b>	<b>86,398,700</b>

Source: US Energy Information Administration, *Annual Coal Distribution Reports*.<sup>2</sup>

Overseas sales have surged in recent years, spurred on by a combination of declining US consumption and growing demand from the Pacific Rim. The growth in coal exports has been far from secret. In fact, many coal mining and marketing firms have gone to great lengths to publicize successful export sales, and have wooed investors with descriptions of growing Asian demand for coal and the robust profit potential of overseas coal sales.

The coal industry in the western US purchases much of its export coal through federal leasing programs administered by the US Bureau of Land Management (BLM). Federal coal leases give private companies the right to mine coal owned by the American public, provided that the companies make lease and royalty payments, and that they comply with environmental requirements. Coal companies acquire most of their federal coal through BLM's lease by application (LBA) process, in which coal companies bid for the right to extract and sell federally owned coal. The 2005 Energy Policy Act also expanded BLM's ability to sell federal coal through "lease modification applications" (LMAs), a fast-track process that allows the BLM to add up to 960 acres to an existing federal lease.

When deciding whether to approve a coal lease, BLM must evaluate whether a private company's bid matches or exceeds the coal's fair market value (FMV). Yet the market for federal coal is anything but fair. Over the past 20 years, for example, 18 of 21 successful coal lease applications in the Powder River Basin (PRB) in Montana and Wyoming had only a single bidder.<sup>3</sup> The absence of a competitive market has allowed private companies to gain access to federally owned coal by offering the lowest possible price, rather than a price that offers the American public a reasonable, robust return for the sale of public assets.

Moreover, BLM has a history of assigning modest FMVs to the coal it leases, allowing private companies to obtain federal coal at exceptionally low prices. Since 1990, in the states of Montana, North Dakota, Wyoming, and Colorado alone, BLM has approved lease sales of 2.4 billion tons of federally owned coal at prices ranging from \$0.004 to \$0.25 per ton. The agency sold an additional billion tons of coal at prices ranging from \$0.30 to \$0.42 per ton; 3.6 billion tons at prices ranging from \$0.71 to \$0.97 per ton; and 1.5 billion tons at prices between \$1.10 and \$1.35 per ton—the maximum value for any private purchase of federally owned coal in those four states.<sup>4</sup> As the Office of Inspector General of the US Department of the Interior remarked in a November 2013 letter on the federal coal leasing program:

*In our opinion, given that only one company historically bids on a lease sale, BLM's FMV represents the only form of competition for the bidder. Accordingly, rather than rationalizing a low price, BLM should more aggressively establish its FMV.*<sup>5</sup>

Lease modifications offer particularly meager returns, with average prices 80 percent below the typical prices for comparable lease sales. According to a 2013 report by the Department of the Interior's Inspector General's office, low-cost lease modifications may have cost the American public \$60 million in foregone revenues since 2000.<sup>6</sup> Outside experts believe that the LMAs may have led to even steeper losses.<sup>7</sup>

BLM's exceptionally low valuations for coal leases look all the more unreasonable given the explosive growth and high profit potential of coal exports. Cloud Peak Energy, for example paid \$0.18 per ton for federal coal at the Spring Creek Mine, but has been able to resell that coal in Asian markets for more than \$60 per ton.<sup>8</sup> During the second quarter of 2012 Cloud Peak realized at least four times as much profit per ton from its exports as from its domestic sales—demonstrating that when market conditions are favorable, exporting federal coal can yield exceptionally high profits.

Yet to date, BLM has largely ignored the potential profits from coal exports when determining the FMV of the coal leases. According to the Inspector General's 2013 report:

*BLM does not fully account for export potential in developing the [fair market values]. The export of public coal has been growing in recent years...especially to Asian markets...Based upon our analysis of appraisals...it appears that several state offices overlook the export potential, thus possibly undervaluing the public's coal.*<sup>9</sup>

BLM responded to these findings in part by downplaying the importance of exports, stating:

*Little Federal coal is currently exported. According to the Energy Information Administration, no more than 1.6 percent of Powder River Basin coal is exported." ...[T]he general discussion of exports in the text of the report...may create the misleading impression that the opposite is the case.*

This response neglects the substantial growth of exports of federal coal *outside* the PRB, as well as the industry's hopes to boost exports from the US West Coast by at least 100 million tons per year, much of which would come from PRB mines. It also ignores the fact that some coal companies seek out new federal coal leases for the express purpose of servicing export markets. Since domestic coal demand has diminished in recent years, some



companies bidding on new federal coal supplies simply would have no financial motivation to expand their leased reserves were it not for the profit potential from exports.

As the following sections of this report demonstrate, coal companies operating in the western US have openly advertised successful export sales of coal from specific mines operating with federal leases, and have made no secret of their ambitions to continue such sales in the future. Moreover, many of these companies have told investors, securities regulators, and the public that they are now pursuing specific federal coal leases and lease modifications in order to take advantage of opportunities to sell coal overseas.

## Cloud Peak Energy's Spring Creek Mine, Montana

Cloud Peak Energy, which bills itself as the only “pure play Powder River Basin (PRB) coal company,”<sup>10</sup> has exported roughly 18 million tons of coal to Asia since 2010, mostly through its contract with the Westshore<sup>11</sup> coal terminal outside of Vancouver, British Columbia.<sup>12</sup> Cloud Peak executives have repeatedly stated—to investors, regulators, and the general public—that the coal that Cloud Peak exports comes from its Spring Creek Mine in southern Montana. As Cloud Peak's Chief Financial Officer, Michael Barrett, recently told investors:

*“[W]e were pleased to increase our export shipments to 4.7 million tons compared to 4.4 million tons last year. We continued to see robust Asian demand for the consistent high-quality coal from our Spring Creek [M]ine.”<sup>13</sup>*

The Spring Creek Mine was developed through two LBA bids. The BLM accepted the first bid in 2001, for \$0.11 per ton, and approved the second bid in 2007, for \$0.18 per ton.<sup>14</sup> During much of 2012, the company sold this coal for more than \$60 per ton. These sales yielded profit margins four to five times as high as the margins that Cloud Peak earned on domestic sales.

Cloud Peak's executives have touted Spring Creek's advantages in the Asian export markets, pointing out that the mine's comparatively high-energy coal and shorter distance to ocean-going terminals gives the mine an export edge over rival coals produced in the southern PRB. More recently, the company's executives have pinned their company's entire growth strategy on exporting coal from Spring Creek and adjacent mines.<sup>15</sup> In the company's third quarter 2013 investor conference call, for example, Barrett stated: “[W]hat we want to do is to try and build on our position around the Spring Creek Complex...so that we can actually then look to build our exports, which we believe [offers] strong growing demand and potentially good margin through the cycle.”<sup>16</sup> And in its most recent presentation to investors,<sup>17</sup> the company outlined its strategy for “Responding to Market Conditions” as:

- **Responding to domestic utility demand and low pricing by reducing domestic shipments over time**
- **Focus on growth through exports**

This strategy represents a remarkable turn for a US coal company: an explicit admission that the domestic market for coal is shrinking and that the company's growth hinges on selling coal overseas.

Spring Creek coal's high sodium content—roughly 8.5 percent in coal ash<sup>18</sup>—limits the mine's domestic market, because high-sodium ash fouls most power plant boilers. In Asian markets, buyers blend Spring Creek coal with other coals to create a mixture with acceptable performance.<sup>19</sup> But for domestic sales, Cloud Peak finds that potential customers prefer alternatives with less sodium. Without export sales, Cloud Peak might be looking to trim back production at Spring Creek to accommodate declining domestic demand, as the company recently announced it would do at its Cordero Rojo Mine in the middle PRB.<sup>20</sup> Instead, the company is hoping to expand production by leasing an additional 198 million tons of federal coal on lands adjacent to the Spring Creek Mine.<sup>21</sup> Since Cloud Peak expects to earn substantial profits by selling coal from the new lease to Asian customers, federal officials evaluating Cloud Peak's LBA application adjacent to Spring Creek have a clear duty to consider export sales when determining the value of federal coal.

## Ambre Energy's Decker Mine, Montana

Based in Australia, Ambre Energy has become one of the key players in coal exports in the Pacific Northwest. The company now operates two coal mines—the Decker Mine in the northern PRB in Montana, and the Black Butte Mine in southern Wyoming. And it is pursuing two coal export terminals in Washington and Oregon. In its own words, Ambre aspires to become “a vertically integrated domestic coal producer and exporter of US thermal coal into the buoyant Asia Pacific market.” The company's 2011 Annual Report announces the company's export strategy boldly, front and center, on page 1. (See image.)<sup>22</sup>



Ambre Energy is building a vertically integrated coal marketing, mining and infrastructure company with aspirations to become the largest supplier of US thermal coal to the Asia Pacific market.

Ambre's two mines—and the Decker Mine in particular—lie at the center of the company's ambition to become a “vertically integrated” coal exporter. In its 2011 annual report, Ambre speaks of its export ambitions for Decker coal:

***Coals such as those at Ambre Energy's newly acquired Decker coal mine based in Montana are the best suited coals for the Asian export market. In addition to the state's geographical advantage to the US west coast, the Montana coals have higher energy levels compared to the southern PRB in Wyoming.***<sup>23</sup> [Emphasis added.]

The 2011 annual report goes on to add:

*The company also intends ultimately to increase coal production [at Decker] to **take advantage of demand for coal from North Asian customers** via Ambre Energy's port infrastructure in the US west coast region. [Emphasis added.]*

By 2012 Ambre crystallized its Asian export strategy by signing agreements with two South Korean utilities to ship up to 5 million metric tons of coal per year for 10 years.<sup>24</sup> In its June 2012 annual report, the company touted the agreements with Korean buyers, describing the key activities of its international coal trading business as:

***Marketing US thermal coal to Asian customers** and securing offtake agreements to supply US thermal coal from Ambre Energy co-owned mines and third party mines **to South Korean power generators Korea South East Power Co. Ltd. (KOSEP) and Korea Southern Power Co. Ltd. (KOSPO).** [Emphasis added.]*



Like the coal from Spring Creek, Decker's high-sodium coal finds a limited domestic market. But the prospects for profits from export sales have prompted Ambre to seek a lease modification that would give the company access to an additional 40 million tons of coal on lands adjacent to its existing lease.<sup>25</sup> A fair and comprehensive evaluation of the FMV of this lease modification must consider Ambre's extensive and detailed plans to sell coal overseas.

## Signal Peak Mine, Montana

Signal Peak Energy, a three-way venture co-owned by FirstEnergy Ventures, the Boich Companies, and the Gunvor Group, operates the Signal Peak Mine, one of the highest-producing longwall mines in the United States.<sup>26</sup> It is also one of the nation's top exporters of thermal coal to Asia.

For more than half a decade, Signal Peak's owners have consistently emphasized Signal Peak's export sales. As early as 2009, FirstEnergy President and CEO Anthony J. Alexander mentioned their Asian export strategy for Signal Peak in an investor conference call, saying: "We've...secured multiple test cargos that will be shipped into the Asian markets in the fourth quarter."<sup>27</sup> Then in a 2010 investor conference call, Signal Peak CFO Mark Clark asserted:

*Signal Peak is doing quite well...They produced 8 million tons last year, somewhere between 4 million and 5 million was cleaned. About half of that comes east, to us, and **about half of it goes into the international market.**<sup>28</sup> [Emphasis added.]*



In 2011, a press release by First Energy and Boich Companies trumpeted Gunvor's acquisition as opening up new possibilities for coal exports.<sup>29</sup> According to Wayne Boich, Jr., President and Chief Executive Officer of Boich Companies:

*"One of the key advantages that Gunvor Group brings to this venture is the ability to utilize their commodity trading relationships in such markets as Japan, China, Korea and Chile to sell more coal." [Emphasis added.]*

In the same press release, Timothy Legge, chairman of Gunvor, said that Signal Peak had good export potential:

*Signal Peak represents our first investment in a coal mine located in the US. It presents Gunvor with the opportunity to use the existing rail and port operations to market this high quality, low sulfur bituminous coal to expanding markets around the world, particularly in the Pacific and Asia markets through our arrangements with Westshore Terminals in Vancouver, the prime coal moving terminal on the West Coast. [Emphasis added.]*

The following year, Reuters cited an anonymous senior Gunvor executive as stating that export sales from Signal Peak:

*were profitable and demand remains strong...Gunvor ships Signal Peak coal to Europe and Latin America as well as China and other Asian countries. "We've just shipped two vessels to China and both were paid for," he said.<sup>30</sup> [Emphasis added.]*

Then in 2013, the Associated Press reported that the company was ramping up its exports:

*[D]omestic demand for the fuel has fallen off sharply over the last several years, primarily due to competition from cheap natural gas...To offset those declines, companies including Signal Peak and Cloud Peak have stepped up sales in Asia, where demand remains strong among developing countries and industrialized nations including Japan and South Korea.<sup>31</sup> [Emphasis added.]*

In 2012 Signal Peak successfully bid on a coal lease that gives the company access to 35.5 million tons of federal coal for \$0.30 per ton.<sup>32</sup> At the same time, the BLM's Wyoming office was leasing coal with lower energy content for prices of up to \$1.35 per ton.<sup>33</sup> Although Gunvor's executives are notoriously tight-lipped about their business, the company and its co-owners at Signal Peak have given every indication that they hope to maintain or increase their sales of federal coal, purchased from the American public at rock-bottom prices, to overseas customers.

## Bowie Resource Partners Mines, Colorado and Utah

In 2013, the Kentucky-based Bowie Resources partnered with private equity firm Galena Private Equity Resource Fund to purchase three bituminous coal mines in Utah from Arch Coal. The two firms created a new company, Bowie Resource Partners (BRP), which now operates the three mines as well as the Bowie #2 Mine, a bituminous mine in Colorado. BRP now advertises itself as "The Nation's Largest Western Bituminous Coal Producer."<sup>34</sup> All four of BRP's mines rely on federal coal leases. The company paid \$0.32 per ton for its coal lease at the Bowie #2 Mine; \$0.28 per ton at the Sufco Mine; \$0.21 per ton at the Dugout Mine; and \$0.23 per ton at the Skyline Mine.<sup>35</sup>

In the announcement of its agreement with Galena, BRP specifically mentioned exports as a key element of the company's coal business plan, touting loading agreements with the ports at Stockton and Richmond, California.

*Bowie has a long-term agreement with Metropolitan Stevedore Company ("Metro Ports") for the Port of Stockton, which will provide BRP with the opportunity to ship up to 2.3 million tons annually, as the Metro Ports/Stockton agreement will be assigned by Bowie to BRP. Separately, Bowie has been in negotiations with Levin Richmond Terminal Corporation for the port of Richmond, which would provide BRP with annual "topping off" capacity of an additional 1.2 million tons. Bowie has also signed a Letter of Intent for significant export capacity via a Pacific port in the Northwestern US, which would also be assigned to BRP.*

*"We think the time is right to introduce the new 'Bowie Brand' into markets where the need and appetite for coal-fired power generation is growing, not abating."<sup>36</sup>*

As of the summer of 2013, Bowie announced that it was successfully loading coal at the two California ports.<sup>37</sup>

*As proposed US Pacific Northwest coal export terminals stall, California has emerged as an option for shipping coal, though on a much smaller scale. Bowie is already partially loading Panamax ships with coal at the Port of Stockton in California and conducting top-off operations at the Port of Richmond, Calif., through Levin-Richmond Terminal Corp.*

*Bowie Resource Partners LLC Chairman John Siegel said in August 2013 that the company loaded a ship with 45,000 tonnes of coal, floated the vessel to the Port of Richmond and topped it off to 62,000 tonnes.*

Meanwhile, BRP has worked diligently to gain additional access to export markets; in February, the Oakland Port Commission unanimously rejected a proposed terminal intended to handle coal, petroleum coke, and other bulk minerals.<sup>38</sup> Officials in the Utah Office of Energy Development have taken note of Bowie's export ambitions.<sup>39</sup>

*OED is working with GOED, the World Trade Center, the US Commercial Service and others to explore opportunities to export coal from Utah.*

*Arch Coal's recent divestment of significant coal holdings in a sale to Bowie Resources, LLC, a Kentucky Company, has enhanced Utah's position with respect to coal exports. This is due to Bowie's access to significant West Coast export capacity.*

Since BRP has made no secret of its ambitions for exporting coal to Asia, the federal government could protect the interests of the American public by evaluating the profits from export sales from the company's two pending LBAs, one for the Spruce Stomp LBA adjacent to the Bowie Mine #2, and the other for the Greens Hollow coal tract, which is on US Forest Service land adjacent to the Sufco Mine.<sup>40</sup> BLM recently announced that it had scheduled sale of the Spruce Stomp coal lease in Colorado for July 30, 2014.<sup>41</sup>

## Arch Coal's West Elk Mine, Colorado

Arch Coal shipped 11.5 million tons of coal overseas in 2013.<sup>42</sup> Most of these shipments were for metallurgical coal produced in Appalachia, but the company also exported a significant volume of coal from its West Elk Mine in Colorado, which produces a bituminous thermal coal. Arch mines West Elk under a federal coal lease, which

the BLM modified most recently in December of 2012 by a total of 1,721 additional acres of federal coal to two of Arch's existing leases.<sup>43</sup>

Much of the West Elk Mine's coal goes to the export market. In Arch's investor conference call for the fourth quarter of 2013, John Eaves, the company's President and CEO, reported:

*As you know our West Elk [M]ine in Colorado is heavily focused on the export market. As 50% of the mine's output were sold in the Europe, Latin America and Asia in 2013. That penetration has been helpful as it has helped to offset a soft demand for Colorado coal domestically. [sic]*<sup>44</sup>

This is not the first time that Arch has mentioned its significant export position at West Elk—and the fact that Colorado bituminous coal has a modest domestic market. In Arch's conference call for the third quarter of 2011, Mr. Eaves stated:

*As we look at Western Bit [bituminous], I will tell you that we're not seeing a lot of improvement in the domestic demand there. We are encouraged by what we're seeing in terms of the international market in Western Bit. We're going to see somewhere around 1.5 million tons there of exports this year and hope to grow that to over 2 million tons next year.*

Arch Coal executives say that the firm has shipped West Elk coal to Japan,<sup>45</sup> that it ships West Elk coal both through West Coast and Gulf Coast ports,<sup>46</sup> and that it expects to ship additional thermal coal overseas as port capacity expands.<sup>47</sup> Arch hopes to expand its West Elk reserves with an additional 10.1 million ton federal coal lease, though a recent US District Court Decision has put that lease sale on hold, at least temporarily.<sup>48</sup>

## New Horizon Coal's Kinney Mine, Utah

Australian firm New Horizon Coal is attempting to develop the so-called Kinney Coal project, located in a "mature coal mining district" about 100 miles from Salt Lake City. In developing the mine, New Horizon hopes to combine two separate coal leases: one for coal controlled by Carbon County, UT, and a second for federal coal controlled by the BLM.<sup>49</sup>

Although nearby coal-fired power stations provide a potential market for the mine's coal, Kinney's proponents are clearly aiming for export markets as well. In its most recent presentation to investors, New Horizon Coal repeatedly spotlights the Kinney Mine's export potential. Examples include:

- **Rail and road access:** The presentation emphasizes nearby "Rail and road infrastructure" that would allow Kinney coal "to reach domestic **and export markets**." (Emphasis added.)
- **Port allocation:** New Horizon Coal touts its "Secure Port Allocation and Export Logistics," including an agreement with the signed for a "port allocation" at the Texas Deepwater Industrial Port starting at 1.5 million tons per year, and expandable to 3 million tons per year.
- **Premium export prices, high export profits:** The presentation cites industry analysts who forecast "premium pricing on domestic **and export markets**" for Kinney coal. The presentation includes a chart that highlights coal prices in the Gulf of Mexico, from which New Horizon hopes to export, showing

export profit margins starting at \$20 per ton in the short term, and rising to \$80 per ton in 2029. A separate presentation states that “the project is expected to realize strong cash flows utilizing a mixture of domestic and export sales.”<sup>50</sup>

- **Suitability for export:** The presentation explicitly states that Kinney’s high-calorie, low-sulfur coal is “suitable to” export markets, including Europe, Latin America, and Asia.
- **Marketing and Logistics:** The presentation highlights the “significant blending opportunities” for Kinney coal to be mixed with other fast-growing export coals with lower energy content or higher sulfur levels. New Horizon points to its Texas port allocation as a “one stop shop” to blend and export” its coal.

Provided that the information that New Horizon Coal has given its investors is accurate, any evaluation of the FMV of the Kinney coal project must include the company’s export plans—which appear to be a significant and potentially profitable component of their business.

## Southern Powder River Basin Mines, WY

The southern PRB is home to the nation’s nine largest and highest-producing coal mines. Yet domestic demand for southern PRB coal has been on the decline in recent years, leading to a 17 percent fall in Wyoming coal production between 2008 and 2012.<sup>51</sup> This steep drop has prompted companies operating in the southern PRB to seek overseas customers for their coal, and to promote exports as a way to revitalize the region’s coal industry.



Take, for example, Arch Coal. The company operates two mines in the southern PRB, including Black Thunder, which in 2010 produced more coal than any other mine in the nation.<sup>52</sup> Arch mines Black Thunder through several coal leases granted by the Wyoming office of the BLM.<sup>53</sup>

Repeated public statements by Arch show that the company is keen to export PRB coal to overseas customers. In 2010 Arch advertised its success in coal from its Black Thunder Mine “to the West Coast for export to China and the Asia-Pacific market.”<sup>54</sup> The company website also states that it ships PRB coal overseas.<sup>55</sup> And in an investor conference call, the company reported that it had shipped thermal coal from the PRB to customers in Korea.<sup>56</sup> The company now owns a 38 percent stake in the proposed Millennium Bulk Terminal project in Longview, WA, which would export 44 million metric tons of coal per year. Arch’s involvement in the Millennium project suggests that they hope to ship significant quantities of coal from the southern PRB to customers in Asia.

Peabody Energy operates three mines in the southern PRB, including the North Antelope/Rochelle Mine.<sup>57</sup> The company announced in 2010 that it had shipped PRB coal to Great Britain.<sup>58</sup> In February 2011 it inked a long-

term deal with port operator SSA Marine to ship up to 24 million tons of coal per year, principally to Asia, through the proposed Gateway Pacific coal terminal outside of Bellingham, WA—arguing that “Powder River Basin coal offers a competitive and reliable alternative for customers in China, South Korea, Japan, India and other Asian nations.”<sup>59</sup> Then in mid-2012, as progress on Northwest terminal projects stalled, the company announced plans to export PRB coal through terminals in Houston and New Orleans.<sup>60</sup>



In 2012 Peabody added 1.2 billion tons in coal reserves to its North Antelope mining complex, through two successful LBA bids: one for the North Porcupine LBA, at \$1.10 per ton, and another for the South Porcupine LBA, at \$1.11 per ton.<sup>61</sup> The company hopes to add an additional billion tons of coal to North Antelope through the Antelope Ridge lease that is currently pending with the BLM.<sup>62</sup> Peabody’s plans for a substantial increase in exports of PRB coal raise serious questions about the economics of these bids. By ignoring the economics of coal exports, the BLM likely underestimated the “fair market value” of coal at North and South Porcupine. And the agency now risks doing the same at Antelope Ridge.

BLM’s reluctance to consider exports is especially surprising, given the agency’s public statements about the fundamental purposes of the coal leasing program that it administers. For example, in its record of decision for the North Porcupine LBA, which was granted to Peabody Energy, the agency declares:

*The Federal Coal Program encourages the development of domestic coal reserves and the **reduction of the United States’ dependence on foreign sources of energy**. BLM recognizes that coal extraction is currently necessary in order to **meet the nation’s energy needs**. A primary goal of the National Energy Policy is to **add energy supplies from diverse sources including domestic oil, gas, and coal**. [Emphasis added.]*

Although exporting federally owned coal furthers none of these stated goals, BLM has given little added scrutiny to export sales in its analysis of federal coal leases.

## Effects on Domestic Prices

As coal companies have increasingly incorporated export sales into their long-term strategies, some energy industry analysts have begun to point out that export sales can have profound effects on the domestic coal market. By taking coal out of the US market, the growth of coal exports can tighten domestic coal supplies—leading both to higher prices for US coal consumers, and to higher profits for coal companies. As a recent research paper from the Program on Energy and Sustainable Development at Stanford University argues:

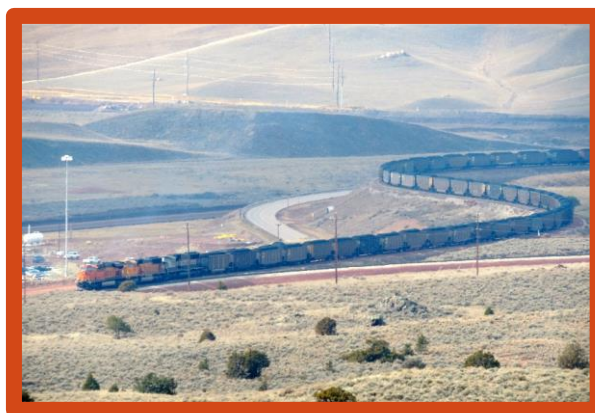
*Removing constraints on exports tends to **increase the price of an energy commodity in the exporting country** and decrease it in importing countries.<sup>63</sup> [Emphasis added.]*



The author emphasizes that, while nobody can predict the precise pricing impacts of coal exports, selling more coal to foreign customers will tend to boost the price paid by domestic coal consumers. Similarly, the National Rural Electric Cooperative Association (NRECA) recently warned that coal exports could boost coal prices for their member utilities.

*A rise in exports...could be troublesome for electric cooperatives which get the majority of their coal from the Powder River Basin region—the region forecast to supply the uptick in trade... “Should exports increase, prices for coal could increase for our members,” said Mike Casper, NRECA senior manager, generation and fuels.<sup>64</sup>*

Comparable concerns about exports have been raised about other energy commodities. In a robust modeling effort in 2012, for example, the US Energy Information Administration concluded that increased natural gas exports would lead to increased prices for US consumers.<sup>65</sup> This evidence suggests that a substantial increase in US coal exports could boost domestic coal prices, while lowering or stabilizing prices for overseas customers. Coal industry shareholders and executives would clearly benefit, while domestic coal customers and the public at large stand the most to lose.



## Conclusion

The evidence is irrefutable. Coal companies operating in the western United States ship significant volumes of federally owned coal to overseas customers. Exporting coal to customers in Asia and Europe can often yield higher profits than coal companies can realize from selling the same coal in domestic markets. And in many cases, coal companies have clearly stated that they are pursuing specific federal coal leases as part of a detailed strategy to boost overseas coal sales. Yet BLM has almost completely ignored coal exports when assessing the “fair market value” of federal coal.

BLM has a duty to ensure that the American public receives appropriate compensation for selling public mineral resources to private firms. The agency has an equal duty to ensure that federal coal sales are truly in the public interest. The rapid growth in overseas sales of federal coal raises serious questions about both of these duties, since exports can boost coal industry profits for coal sold both domestically and overseas, while raising domestic coal prices and undermining the public interest through increased carbon pollution. The clear intention of US coal companies to export more coal in the future gives BLM both a responsibility and an opportunity to conduct a thorough economic review of the effects of coal exports. To be truly comprehensive, such an analysis would consider not only how exports affect the value of specific coal leases, but also the potential for coal exports to raise domestic coal prices more generally, boosting the value that coal companies receive from all sales of federal coal. Further, such an analysis would also consider the true cost of exporting carbon pollution, particularly in light of the growing urgency of combating climate change in the US and abroad.

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## Report Collaborators



Sightline Institute's mission is to make the Northwest a global model of sustainability—strong communities, a green economy, and a healthy environment.

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Northern Plains organizes Montana citizens to protect our water quality, family farms and ranches and unique quality of life.

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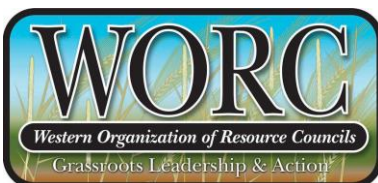
Powder River Basin Resource Council is committed to empowerment of people through community organizing. More than ever, it is crucial that Wyoming's voice for responsible development, Powder River Basin Resource Council, be a part of the debate that will determine Wyoming's future.

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WildEarth Guardians protects and restores the wildlife, wild places, wild rivers, and health of the American West. Through its Climate and Energy Program, Guardians works to combat climate change by advancing clean energy solutions and confronting the impacts of fossil fuels.

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