

ARCH COAL INC  
Form 10-Q/A  
May 11, 2012

**UNITED STATES**  
**SECURITIES AND EXCHANGE COMMISSION**

WASHINGTON, DC 20549

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**FORM 10-Q/A**

(Amendment No. 1)

(Mark One)

**Quarterly Report Pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934**

For the quarterly period ended March 31, 2012

**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: 1-13105

## Arch Coal, Inc.

(Exact name of registrant as specified in its charter)

**Delaware**  
(State or other jurisdiction  
of incorporation or organization)

**43-0921172**  
(I.R.S. Employer  
Identification Number)

**One CityPlace Drive, Suite 300, St. Louis, Missouri**  
(Address of principal executive offices)

**63141**  
(Zip code)

Registrant's telephone number, including area code: **(314) 994-2700**

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 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 whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes  No

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   
(Do not check if a smaller reporting company)

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

At May 10, 2012 there were 212,247,652 shares of the registrant's common stock outstanding.



**Explanatory Note**

Arch Coal, Inc. (the Company) is filing this Amendment No. 1 (this Amendment) to its Quarterly Report on Form 10-Q for the period ended March 31, 2012, filed with the Securities and Exchange Commission on May 10, 2012 (the Original Report), solely for the purposes of (i) correcting certain numbers contained in Note 17 in the Original Report to conform to the financial statements reported herein and (ii) correcting the inadvertent omission in the Original Report of the number of shares, and total dollar value of such shares, available for purchase under the Company's share repurchase program. This Amendment amends and restates in their entirety Item 1 of Part I, Item 2 of Part II and Item 6 of Part II of the Original Report.

No other amendments, modifications, updates or changes are being made to the Original Report other than as described above. This Amendment speaks as of the date of the filing of the Original Report. The Company has not taken into account any other events occurring after the filing of the Original Report which might have affected any disclosures in the Original Report, nor has the Company amended, modified, updated or otherwise changed any disclosures to reflect any subsequent events.

Part I

## FINANCIAL INFORMATION

**Item 1. Financial Statements.****Arch Coal, Inc. and Subsidiaries****Condensed Consolidated Statements of Income****(in thousands, except per share data)**

|   | <b>Three Months Ended March 31,</b> |             |
|---|-------------------------------------|-------------|
|   | <b>2012</b>                         | <b>2011</b> |
|   | <b>(Unaudited)</b>                  |             |
| <b>Revenues</b>   | \$ 1,039,651                        | \$ 872,938  |
| <b>Costs, expenses and other</b>  |                                     |             |
| Cost of sales   | 850,871                             | 653,684     |
| Depreciation, depletion and amortization                                  | 139,966                             | 83,537      |
| Amortization of acquired sales contracts, net                             | (14,017)                            | 5,944       |
| Selling, general and administrative expenses                              | 30,861                              | 30,435      |
| Change in fair value of coal derivatives and coal trading activities, net | (3,613)                             | (1,784)     |
| Other operating income, net   | (18,498)                            | (1,116)     |
|   | 985,570                             | 770,700     |
| Income from operations  | 54,081                              | 102,238     |
| Interest expense, net:  |                                     |             |
| Interest expense  | (74,772)                            | (34,580)    |
| Interest income   | 1,021                               | 746         |
|   | (73,751)                            | (33,834)    |
| Income before income taxes  | (19,670)                            | 68,404      |
| Provision for (benefit from) income taxes                                 | (21,079)                            | 12,530      |
| Net income  | 1,409                               | 55,874      |
| Less: Net income attributable to noncontrolling interest                  | (203)                               | (273)       |
| Net income attributable to Arch Coal, Inc.                                | \$ 1,206                            | \$ 55,601   |
| <b>Earnings per common share</b>  |                                     |             |
| Basic earnings per common share   | \$ 0.01                             | \$ 0.34     |
| Diluted earnings per common share   | \$ 0.01                             | \$ 0.34     |
| Weighted average shares outstanding                                       |                                     |             |
| Basic   | 211,687                             | 162,576     |
| Diluted   | 211,908                             | 163,773     |
| Dividends declared per common share                                       | \$ 0.11                             | \$ 0.10     |

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The accompanying notes are an integral part of the condensed consolidated financial statements.

Arch Coal, Inc. and Subsidiaries

Condensed Consolidated Statements of Comprehensive Income

(in thousands, except per share data)

|   | Three Months Ended March 31 |           |
|---|-----------------------------|-----------|
|   | 2012                        | 2011      |
|   | (Unaudited)                 |           |
| Net income  | \$ 1,409                    | \$ 55,874 |
| Other comprehensive income, net of income taxes:  |                             |           |
| Pension, postretirement and other post-employment benefits, reclassifications into net income | 463                         | 573       |
| Unrealized gains (losses) on available-for-sale securities                                    | 252                         | 747       |
| Unrealized gains and losses on derivatives, net of reclassifications into net income:         |                             |           |
| Unrealized gains (losses) on derivatives  | 1,760                       | 9,501     |
| Reclassifications of (gains) losses into net income   | 4,825                       | (2,124)   |
| Total other comprehensive income  | 7,300                       | 8,697     |
| Total comprehensive income  | \$ 8,709                    | \$ 64,571 |

**Arch Coal, Inc. and Subsidiaries**  
**Condensed Consolidated Balance Sheets**  
(in thousands, except per share data)

|  | March 31,<br>2012 | December 31,<br>2011 |
|--|-------------------|----------------------|
|  | (Unaudited)       |                      |
| <b>Assets</b>  |                   |                      |
| <b>Current assets</b>                                |                   |                      |
| Cash and cash equivalents                            | \$ 117,770        | \$ 138,149           |
| Restricted cash                                      | 8,866             | 10,322               |
| Trade accounts receivable                            | 295,012           | 380,595              |
| Other receivables                                    | 66,702            | 88,584               |
| Inventories  | 488,686           | 377,490              |
| Prepaid royalties                                    | 18,025            | 21,944               |
| Deferred income taxes                                | 65,531            | 42,051               |
| Coal derivative assets                               | 22,043            | 13,335               |
| Other  | 96,484            | 110,304              |
| Total current assets                                 | 1,179,119         | 1,182,774            |
| <b>Property, plant and equipment, net</b>            | <b>7,892,733</b>  | <b>7,949,150</b>     |
| <b>Other assets</b>                                  |                   |                      |
| Prepaid royalties                                    | 90,221            | 86,626               |
| Goodwill   | 596,103           | 596,103              |
| Equity investments                                   | 230,519           | 225,605              |
| Other  | 176,423           | 173,701              |
| Total other assets                                   | 1,093,266         | 1,082,035            |
| Total assets   | \$ 10,165,118     | \$ 10,213,959        |
| <b>Liabilities and Stockholders Equity</b>           |                   |                      |
| <b>Current liabilities</b>                           |                   |                      |
| Accounts payable                                     | \$ 294,341        | \$ 383,782           |
| Coal derivative liabilities                          | 9,100             | 7,828                |
| Accrued expenses and other current liabilities       | 357,386           | 348,207              |
| Current maturities of debt and short-term borrowings | 102,356           | 280,851              |
| Total current liabilities                            | 763,183           | 1,020,668            |
| Long-term debt                                       | 3,967,796         | 3,762,297            |
| Asset retirement obligations                         | 432,620           | 446,784              |
| Accrued pension benefits                             | 49,378            | 48,244               |
| Accrued postretirement benefits other than pension   | 42,784            | 42,309               |
| Accrued workers compensation                         | 74,012            | 71,948               |
| Deferred income taxes                                | 982,596           | 976,753              |
| Other noncurrent liabilities                         | 268,585           | 255,382              |
| Total liabilities                                    | 6,580,954         | 6,624,385            |
| Redeemable noncontrolling interest                   | 11,739            | 11,534               |
| <b>Stockholders Equity</b>                           |                   |                      |
| Common stock   | 2,141             | 2,136                |
| Paid-in capital                                      | 3,024,553         | 3,015,349            |
| Treasury stock, at cost                              | (53,848)          | (53,848)             |
| Retained earnings                                    | 600,230           | 622,353              |
| Accumulated other comprehensive loss                 | (651)             | (7,950)              |



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|  |    |            |    |            |
|--|----|------------|----|------------|
| Total stockholders' equity                 |    | 3,572,425  |    | 3,578,040  |
| Total liabilities and stockholders' equity | \$ | 10,165,118 | \$ | 10,213,959 |

The accompanying notes are an integral part of the condensed consolidated financial statements.

## Arch Coal, Inc. and Subsidiaries

## Condensed Consolidated Statements of Cash Flows

(in thousands)

|   | Three Months Ended March 31, |           |
|---|------------------------------|-----------|
|   | 2012                         | 2011      |
|   | (Unaudited)                  |           |
| <b>Operating activities</b>   |                              |           |
| Net income  | \$ 1,409                     | \$ 55,874 |
| Adjustments to reconcile to cash provided by operating activities:            |                              |           |
| Depreciation, depletion and amortization                                      | 139,966                      | 83,537    |
| Amortization of acquired sales contracts, net                                 | (14,017)                     | 5,944     |
| Prepaid royalties expensed  | 8,586                        | 8,916     |
| Employee stock-based compensation expense                                     | 4,079                        | 5,290     |
| Amortization relating to financing activities                                 | 4,288                        | 2,442     |
| Changes in:   |                              |           |
| Receivables   | 88,082                       | (53,586)  |
| Inventories   | (111,196)                    | (12,292)  |
| Coal derivative assets and liabilities  | (5,347)                      | (1,087)   |
| Accounts payable, accrued expenses and other current liabilities              | (66,222)                     | (38,054)  |
| Income taxes, net   | 23,002                       | 12,558    |
| Deferred income taxes   | (21,742)                     | (1,026)   |
| Other   | 4,102                        | 17,629    |
| Cash provided by operating activities   | 54,990                       | 86,145    |
| <b>Investing activities</b>   |                              |           |
| Decrease in restricted cash   | 1,455                        |           |
| Capital expenditures  | (93,271)                     | (38,711)  |
| Proceeds from dispositions of property, plant and equipment                   | 22,105                       | 516       |
| Purchases of investments and advances to affiliates                           | (5,777)                      | (34,419)  |
| Additions to prepaid royalties  | (8,262)                      | (20,915)  |
| Cash used in investing activities   | (83,750)                     | (93,529)  |
| <b>Financing activities</b>   |                              |           |
| Payments to retire debt   | (1,330)                      |           |
| Net increase in borrowings under lines of credit and commercial paper program | 34,000                       | 3,681     |
| Net payments on other debt  | (5,993)                      | (5,161)   |
| Debt financing costs  | (100)                        | (8)       |
| Dividends paid  | (23,327)                     | (16,269)  |
| Issuance of common stock under incentive plans                                | 5,131                        | 768       |
| Cash provided by (used in) financing activities                               | 8,381                        | (16,989)  |
| Decrease in cash and cash equivalents   | (20,379)                     | (24,373)  |
| Cash and cash equivalents, beginning of period                                | 138,149                      | 93,593    |
| Cash and cash equivalents, end of period                                      | \$ 117,770                   | \$ 69,220 |

The accompanying notes are an integral part of the condensed consolidated financial statements.



**Arch Coal, Inc. and Subsidiaries**

**Notes to Condensed Consolidated Financial Statements**

**(unaudited)**

**1. Basis of Presentation**

The accompanying unaudited condensed consolidated financial statements include the accounts of Arch Coal, Inc. and its subsidiaries and controlled entities (the Company). The Company's primary business is the production of steam and metallurgical coal from surface and underground mines located throughout the United States, for sale to utility, industrial and export markets. On June 15, 2011, the Company acquired International Coal Group, Inc. (ICG), as described in Note 3, Business Combinations. The Company operates 23 mining complexes in West Virginia, Kentucky, Maryland, Virginia, Illinois, Wyoming, Colorado and Utah. All subsidiaries (except as noted below) are wholly-owned. Intercompany transactions and accounts have been eliminated in consolidation.

The accompanying unaudited condensed consolidated financial statements have been prepared in accordance with accounting principles generally accepted in the United States for interim financial reporting and U.S. Securities and Exchange Commission regulations. In the opinion of management, all adjustments, consisting of normal, recurring accruals considered necessary for a fair presentation, have been included. Results of operations for the three period ended March 31, 2012 are not necessarily indicative of results to be expected for the year ending December 31, 2012. These financial statements should be read in conjunction with the audited financial statements and related notes as of and for the year ended December 31, 2011 included in the Company's Annual Report on Form 10-K/A filed with the U.S. Securities and Exchange Commission.

The Company owns a 99% membership interest in a joint venture named Arch Western Resources, LLC (Arch Western) which operates coal mines in Wyoming, Colorado and Utah. The Company also acts as the managing member of Arch Western. On April 9, 2012, Delta Housing, Inc., the other member in Arch Western, exercised their contractual right to require us to purchase their membership interests in Arch Western. The negotiation of this sale and purchase is ongoing and we expect to complete this acquisition by the end of the third quarter.

**2. Accounting Policies**

There is no new accounting guidance that is expected to have a significant impact on the Company's financial statements.

**3. Business Combination**

On June 15, 2011, the Company completed its acquisition of ICG, a leading coal producer. During the first quarter of 2012, the Company finalized the determination of the fair values of the assets acquired and liabilities assumed in the acquisition, with no material adjustments to what was recorded as of December 31, 2011.

**4. Debt**

|   | March 31,<br>2012 | December 31,<br>2011 |
|---|-------------------|----------------------|
|   | (In thousands)    |                      |
| Indebtedness to banks under credit facilities             | \$ 515,300        | \$ 481,300           |
| 6.75% senior notes (\$450.0 million face value) due 2013  | 450,809           | 450,971              |
| 8.75% senior notes (\$600.0 million face value) due 2016  | 589,463           | 588,974              |
| 7.00% senior notes due in 2019 at par                     | 1,000,000         | 1,000,000            |
| 7.25% senior notes due 2020 at par                        | 500,000           | 500,000              |
| 7.25% senior notes due 2021 at par                        | 1,000,000         | 1,000,000            |
| Other   | 14,580            | 21,903               |
|   | 4,070,152         | 4,043,148            |
| Less current maturities of debt and short-term borrowings | 102,356           | 280,851              |
| Long-term debt  | \$ 3,967,796      | \$ 3,762,297         |

The current maturities of debt include contractual maturities, as well as amounts borrowed that are supported by credit facilities that have a term of less than one year and amounts borrowed under credit facilities with terms longer than one year that the Company does not intend to refinance on a long-term basis, based on cash projections and management's plans.

On April 30, 2012, the Company received commitment letters with lending institutions to refinance certain indebtedness having near-term maturities and to increase the Company's liquidity in order to execute on key long-term growth initiatives, particularly the development of the Company's metallurgical coal properties. As part of the financing package, these lenders have agreed, subject to certain customary conditions, to enter into an amendment to the existing senior secured revolving credit facility which will, among other things, suspend the Company's compliance with the debt-to-EBITDA ratio and other financial covenants in the existing credit agreement over the next 24 months and replace them with minimum performance targets at levels consistent with the current coal market environment. We will also receive a \$1 billion, six-year term loan facility, which will contain no financial maintenance covenants, and the maximum borrowing capacity of the revolving credit facility will be reduced from \$2 billion to \$1 billion. The proceeds of the term loan will be used to retire the outstanding \$450.0 million aggregate principal amount of 6¾% Senior Notes due 2013 issued by Arch Western Finance, LLC (Arch Western Finance), the Company's indirect subsidiary.

On May 1, 2012, Arch Western Finance commenced a cash tender offer for any and all of its outstanding \$450.0 million aggregate principal amount of 6¾% Senior Notes due 2013. In connection with the tender offer, Arch Western Finance is soliciting consents from the holders of the senior notes for certain proposed amendments to the indenture governing the notes that eliminates most of the covenants and certain default provisions applicable to the senior notes, as well as reduce the minimum notice period in the optional redemption provision of the senior notes from 30 days to three days. If Arch Western Finance purchases less than all of the outstanding senior notes in the tender offer, it intends to redeem any senior notes that remain outstanding. The terms and conditions of the tender offer and consent solicitation are described in an Offer to Purchase and Consent Solicitation Statement (the Statement) and a related Consent and Letter of Transmittal (the Letter of Transmittal), which have been sent to holders of the senior notes. The Consent Solicitation expires on May 14, 2012, prior to which the consideration for each \$1,000 of principal is \$1,002.50. For notes tendered after the expiration of the Consent Solicitation and before May 29, 2012, the end of the tender offer, the consideration for each \$1,000 of principal is \$972.50.

## 5. Goodwill

An approximate 20% drop in the Company's stock price during the first quarter of 2012, combined with significant decrease in thermal coal demand during the quarter, indicated that the fair value of the Company's goodwill could be less than its carrying value. Accordingly, we performed the first step of the two-step goodwill impairment test as of March 31, 2012. The fair value of all reporting units that have been assigned goodwill exceeded their respective carrying values, so no further testing was necessary. The value of our Black Thunder reporting unit, where \$115.8 million of goodwill has been allocated, would be sensitive to future volume variations should thermal markets weaken further, which could cause us to perform step 2 of the test. The goodwill allocated to certain Appalachia reporting units is particularly sensitive to volatility in the demand for metallurgical coal. Should metallurgical coal markets weaken, it could cause the fair value of the reporting units to be less than their carrying value, requiring us to perform step 2 of the test for impairment. Additionally, further sustained declines in the Company's stock price below levels experienced in the first quarter would also require us to perform step-2 of the test for impairment. Performance of step 2 of the impairment test, which requires a valuation of individual assets and liabilities of the respective reporting units in order to calculate the implied fair value of goodwill could result in an impairment of goodwill.

**6. Equity Investments and Membership Interests in Joint Ventures**

The Company accounts for its investments and membership interests in joint ventures under the equity method of accounting if the Company has the ability to exercise significant influence, but not control, over the entity. Below are the equity method investments reflected in the condensed consolidated balance sheets:

| (In thousands)                                   | Knight Hawk Holdings, LLC<br>( KH ) | DKRW Advanced Fuels, LLC<br>( DKRW ) | Dominion Terminal Associates<br>( DTA ) | Tenaska Trailblazer Partners, LLC<br>( Tenaska ) | Millennium Bulk Terminals, LLC<br>( MBT ) | Tongue River Railroad, LLC<br>( TRR ) | Total      |
|--|-------------------------------------|--------------------------------------|---|--|---|---------------------------------------|------------|
| Balance at December 31, 2011                     | \$ 135,225                          | \$ 19,715                            | \$ 16,086                               | \$ 15,266  | \$ 26,324                                 | \$ 12,989                             | \$ 225,605 |
| Investments in affiliates                        |                                     |                                      |   |  |   |                                       |            |
| Advances to (distributions from) affiliates, net | (1,801)                             |                                      | 925                                     |  | 2,562                                     | 675                                   | 2,361      |
| Equity in comprehensive income (loss)            | 5,243                               | (879)                                | (1,254)                                 |  | (557)                                     |                                       | 2,553      |
| Balance at March 31, 2012                        | \$ 138,667                          | \$ 18,836                            | \$ 15,757                               | \$ 15,266  | \$ 28,329                                 | \$ 13,664                             | \$ 230,519 |
| Notes receivable from investees:                 |                                     |                                      |   |  |   |                                       |            |
| Balance at December 31, 2011                     | \$                                  | \$ 30,751                            | \$                                      | \$ 5,059   | \$  | \$                                    | \$ 35,810  |
| Balance at March 31, 2012                        | \$                                  | \$ 33,561                            | \$                                      | \$ 5,031   | \$  | \$                                    | \$ 38,592  |

Summarized financial information of the Company's equity method investees follows:

| (In thousands)  | Three Months Ended March 31, |           |
|---|------------------------------|-----------|
|   | 2012                         | 2011      |
| <b>Condensed combined income statement information:</b> |                              |           |
| Revenues  | \$ 51,743                    | \$ 44,470 |
| Gross profit  | 2,475                        | 6,084     |
| Income from operations                                  | (376)                        | 3,643     |
| Net income (loss)                                       | (2,437)                      | 2,283     |

|  | March 31, 2012 | December 31, 2011 |
|--|----------------|-------------------|
| <b>Condensed combined balance sheet information:</b> |                |                   |
| Current assets                                       | \$ 94,811      | \$ 94,645         |
| Noncurrent assets                                    | 361,918        | 332,124           |
| Total assets   | \$ 456,729     | \$ 426,769        |
| Current liabilities                                  | \$ 62,260      | \$ 51,953         |
| Noncurrent liabilities                               | 125,350        | 120,494           |
| Equity   | 268,918        | 254,161           |
| Noncontrolling interest                              | 201            | 161               |
| Total liabilities and equity                         | \$ 456,729     | \$ 426,769        |

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The Company may be required to make future contingent payments of up to \$73.0 million related to development financing for certain of its equity investees. The Company's obligation to make these payments, as well as the timing of any payments required, is contingent upon a number of factors, including project development progress, receipt of permits and construction financing.

### **7. Derivatives**

#### *Diesel fuel price risk management*

The Company is exposed to price risk with respect to diesel fuel purchased for use in its operations. The Company anticipates purchasing approximately 75 to 80 million gallons of diesel fuel for use in its operations during 2012. To reduce the volatility in the



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price of diesel fuel for its operations, the Company uses forward physical diesel purchase contracts, as well as heating oil swaps and purchased call options. At March 31, 2012, the Company had protected the price of approximately 85% of its expected purchases for the remainder of fiscal year 2012 and 50% of its first quarter of 2013 purchases.

At March 31, 2012, the Company had purchased heating oil call options for approximately 59 million gallons for the purpose of managing the price risk associated with future diesel purchases. During the first quarter of 2012 the Company determined, the effectiveness of the heating oil options could not be established as of December 31, 2011 on an ongoing basis. As a result, the amount remaining in accumulated other comprehensive income of \$8.2 million, or \$5.2 million net of income taxes, was recorded in earnings, in the other income, net line on the condensed consolidated statement of income. The out of period adjustment is not deemed material to prior period results, the expected results of the full 2012 fiscal year or for the trend of earnings of the Company.

The Company also purchased heating oil call options to hedge the fuel surcharges on its barge and rail shipments that cover increases in diesel fuel prices. These positions reduce the Company's risk of cash flow fluctuations related to these surcharges but the positions are not accounted for as hedges. At March 31, 2012, Company held purchased call options for approximately 15.5 million gallons for the purpose of managing the fluctuations in cash flows associated with fuel surcharges on future shipments.

### *Coal risk management positions*

The Company may sell or purchase forward contracts, swaps and options in the over-the-counter coal market in order to manage its exposure to coal prices. The Company has exposure to the risk of fluctuating coal prices related to forecasted sales or purchases of coal or to the risk of changes in the fair value of a fixed price physical sales contract. Certain derivative contracts may be designated as hedges of these risks.

At March 31, 2012, the Company held derivatives for risk management purposes that are expected to settle in the following years :

| (Tons in thousands) | 2012    | 2013    | 2014    | 2015  |
|---------------------|---------|---------|---------|-------|
| Coal sales          | (3,025) | (1,117) | (1,440) | (720) |
| Coal purchases      | 417     |         |         |       |

### *Coal trading positions*

The Company may sell or purchase forward contracts, swaps and options in the over-the-counter coal market for trading purposes. The Company is exposed to the risk of changes in coal prices on the value of its coal trading portfolio. The estimated future realization of the value of the trading portfolio is \$4.3 million of losses in 2012 and \$2.2 million of losses in 2013.

### *Tabular derivatives disclosures*

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The Company's contracts with certain of its counterparties allow for the settlement of contracts in an asset position with contracts in a liability position in the event of default or termination. Such netting arrangements reduce the Company's credit exposure related to these counterparties. For classification purposes, the Company records the net fair value of all the positions with a given counterparty as a net asset or liability in the consolidated balance sheets. The amounts shown in the table below represent the fair value position of individual contracts, regardless of the net position presented in the accompanying consolidated balance sheets. The fair value and location of derivatives reflected in the accompanying consolidated balance sheets are as follows:

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| Fair Value of Derivatives<br>(In thousands)                | March 31, 2012      |                         | December 31, 2011   |                         |
|--|---------------------|-------------------------|---------------------|-------------------------|
|  | Asset<br>Derivative | Liability<br>Derivative | Asset<br>Derivative | Liability<br>Derivative |
| <b>Derivatives Designated as Hedging Instruments</b>       |                     |                         |                     |                         |
| Heating oil diesel purchases                               | \$                  | \$                      | \$ 8,997            | \$                      |
| Coal   | 3,256               | (218)                   | 1,109               |                         |
| Total  | 3,256               | (218)                   | 10,106              |                         |
| <b>Derivatives Not Designated as Hedging Instruments</b>   |                     |                         |                     |                         |
| Heating oil diesel purchases                               | 12,869              |                         |                     |                         |
| Heating oil fuel surcharges                                | 2,837               |                         | 1,797               |                         |
| Coal held for trading purposes                             | 26,945              | (33,411)                | 15,505              | (19,927)                |
| Coal   | 22,491              | (6,119)                 | 14,855              | (6,035)                 |
| Total  | 65,142              | (39,530)                | 32,157              | (25,962)                |
| Total derivatives  | 68,398              | (39,748)                | 42,263              | (25,962)                |
| Effect of counterparty netting                             | (30,648)            | 30,648                  | (18,134)            | 18,134                  |
| <b>Net derivatives as classified in the balance sheets</b> | \$ 37,750           | \$ (9,100)              | \$ 28,650           | \$ (7,828)              |
|  |                     |                         | \$ 16,301           |                         |

|   | March 31,<br>2012 | December 31,<br>2011 |
|---|-------------------|----------------------|
| <b>Net derivatives as reflected on the balance sheets</b> |                   |                      |
| <b>Heating oil</b>  |                   |                      |
| Other current assets                                      | \$ 15,707         | \$ 10,794            |
| <b>Coal</b>   |                   |                      |
| Coal derivative assets                                    | 22,043            | 13,335               |
| Coal derivative liabilities                               | (9,100)           | (7,828)              |
|   | \$ 28,650         | \$ 16,301            |

The Company had a current asset for the right to reclaim cash collateral of \$15.0 million and \$12.4 million at March 31, 2012 and December 31, 2011, respectively. These amounts are not included with the derivatives presented in the table above and are included in other current assets in the accompanying consolidated balance sheets.

The effects of derivatives on measures of financial performance are as follows for the three month periods ended March 31:

| Three Months Ended March 31<br>Derivatives used in Fair Value Hedging<br>Relationships (in thousands) | Hedged Items in Fair Value<br>Hedge Relationships |      | Loss on Hedged Items In Fair<br>Value Hedge Relationships |      |
|---|---|------|---|------|
|   | 2012  | 2011 | 2012  | 2011 |
| Coal  | \$  | \$   | Firm commitments  | \$   |
|   |   |      |   | \$   |

| Derivatives used in Cash Flow Hedging Relationships<br>(in thousands) | Gain (Loss) Recognized in OCI |       |                     |        | Gains (Losses) Reclassified from OCI into Income |          |    |       |
|---|-------------------------------|-------|---------------------|--------|--|----------|----|-------|
|   | (Effective Portion)           |       | (Effective Portion) |        | (Effective Portion)                              |          |    |       |
|   | 2012                          | 2011  | 2012                | 2011   | 2012   | 2011     |    |       |
| Heating oil diesel purchases  | \$                            | \$    | 14,258              | \$     | \$   | 3,170(2) |    |       |
| Coal sales  |                               | 2,493 | 1,406               |        | 201  | 87(1)    |    |       |
| Coal purchases  |                               | (202) | (876)               |        |  | (2)      |    |       |
| Totals  | \$                            | 2,291 | \$                  | 14,788 | \$   | 201      | \$ | 3,257 |

|                              | Gain (Loss) Recognized in Income (Ineffective Portion and Amount Excluded from Effectiveness Testing) |      |
|------------------------------|---|------|
|                              | 2012  | 2011 |
| Heating oil diesel purchases | \$  | \$   |
| Coal sales                   |   |      |
| Coal purchases               |   |      |
| Totals                       | \$  | \$   |

|  | Derivatives Not Designated as Hedging Instruments |       |    |            |
|--|---|-------|----|------------|
|  | 2012  | 2011  |    |            |
| Coal unrealized                        | \$  | 7,552 | \$ | (1,045)(3) |
| Coal realized                          |   | 3,158 |    | (4)        |
| Heating oil diesel purchases           |   | 423   |    | (4)        |
| Heating oil fuel surcharges unrealized | \$  | 367   | \$ | (4)        |

**Location in Statement of Income:**

- 
- (1) Revenues
  - (2) Cost of sales
  - (3) Change in fair value of coal derivatives and coal trading activities, net
  - (4) Other operating income, net

The Company recognized net unrealized and realized losses of \$3.9 million and net unrealized and realized gains of \$2.8 million during the three months ended March 31, 2012 and 2011, respectively, related to its trading portfolio (including derivative and non-derivative contracts). These balances are included in the caption "Change in fair value of coal derivatives and coal trading activities, net" in the accompanying consolidated statements of income and are not included in the previous table.

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During the next twelve months, based on fair values at March 31, 2012, gains on derivative contracts designated as hedge instruments in cash flow hedges of approximately \$3.2 million are expected to be reclassified from other comprehensive income into earnings.

**8. Inventories**

Inventories consist of the following:

|                           | March 31<br>2012 |    | December 31<br>2011 |
|---------------------------|------------------|----|---------------------|
|                           | (In thousands)   |    |                     |
| Coal                      | \$ 298,744       | \$ | 206,517             |
| Repair parts and supplies | 174,747          |    | 163,527             |
| Work-in-process           | 15,195           |    | 7,446               |
|                           | \$ 488,686       | \$ | 377,490             |

The repair parts and supplies are stated net of an allowance for slow-moving and obsolete inventories of \$13.4 million at March 31, 2012, and \$13.1 million at December 31, 2011.

**9. Fair Value Measurements**

The hierarchy of fair value measurements prioritizes the inputs to valuation techniques used to measure fair value. The levels of the hierarchy, as defined below, give the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities and the lowest priority to unobservable inputs.

- Level 1 is defined as observable inputs such as quoted prices in active markets for identical assets. Level 1 assets include available-for-sale equity securities and coal futures that are submitted for clearing on the New York Mercantile Exchange.
- Level 2 is defined as observable inputs other than Level 1 prices. These include quoted prices for similar assets or liabilities in an active market, quoted prices for identical assets and liabilities in markets that are not active, or other inputs that are observable or can be corroborated by observable market data for substantially the full term of the assets or liabilities. The Company's level 2 assets and liabilities include commodity contracts (coal and heating oil) with fair values derived from quoted prices in over-the-counter markets or from prices received from direct broker quotes.
- Level 3 is defined as unobservable inputs in which little or no market data exists, therefore requiring an entity to develop its own assumptions. These include the Company's commodity option contracts (primarily coal and heating oil) valued using modeling techniques, such as Black-Scholes, that require the use of inputs, particularly volatility, that are rarely observable. Changes in the unobservable inputs would not have a significant impact on the reported Level 3 fair values at March 31, 2012.

The table below sets forth, by level, the Company's financial assets and liabilities that are recorded at fair value in the accompanying condensed consolidated balance sheet:

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|                                  | Total     | Fair Value at March 31, 2012 |          |    | Level 3 |
|----------------------------------|-----------|------------------------------|----------|----|---------|
|                                  |           | Level 1                      | Level 2  |    |         |
| (In thousands)                   |           |                              |          |    |         |
| <b>Assets:</b>                   |           |                              |          |    |         |
| Investments in equity securities | \$ 7,936  | \$ 7,936                     | \$       | \$ |         |
| Derivatives                      | 37,750    | 20,177                       | 2,068    |    | 15,505  |
| Total assets                     | \$ 45,686 | \$ 28,113                    | \$ 2,068 | \$ | 15,505  |
| <b>Liabilities:</b>              |           |                              |          |    |         |
| Derivatives                      | \$ 9,100  | \$                           | \$ 6,836 | \$ | 2,264   |

The Company's contracts with certain of its counterparties allow for the settlement of contracts in an asset position with contracts in a liability position in the event of default or termination. For classification purposes, the Company records the net fair value of all the positions with these counterparties as a net asset or liability. Each level in the table above displays the underlying contracts according to their classification in the accompanying condensed consolidated balance sheet, based on this counterparty netting.

The following table summarizes the change in the fair values of financial instruments categorized as level 3.

|  | <b>Three Months<br/>Ended<br/>March 31, 2012<br/>(In thousands)</b> |        |
|--|---|--------|
| Balance, beginning of period   | \$  | 6,211  |
| Realized and unrealized losses recognized in earnings, net                   |   | 2,496  |
| Realized and unrealized losses recognized in other comprehensive income, net |   |        |
| Purchases  |   | 5,261  |
| Issuances  |   |        |
| Settlements  |   | (727)  |
| Ending balance   | \$  | 13,241 |

Net unrealized gains during the three month period ended March 31, 2012 related to level 3 financial instruments held on March 31, 2012 were \$2.8 million.

#### *Fair Value of Long-Term Debt*

At March 31, 2012 and December 31, 2011, the fair value of the Company's senior notes and other long-term debt, including amounts classified as current, was \$3.9 billion and \$4.2 billion, respectively. The fair values are based upon observed prices in an active market, and as such are classified as Level 1 in the fair value hierarchy.

#### **10. Stock-Based Compensation and Other Incentive Plans**

During the three months ended March 31, 2012, the Company granted options to purchase approximately 1.1 million shares of common stock with a weighted average exercise price of \$13.93 per share and a weighted average grant-date fair value of \$5.42 per share. The options' fair value was determined using the Black-Scholes option pricing model, using a weighted average risk-free rate of .767%, a weighted average dividend yield of 3.16% and a weighted average volatility of 60.18%. The options' expected life is 4.5 years and the options vest ratably over three years, and provide for the continuation of vesting after retirement for recipients that meet certain criteria. The expense for these options will be recognized through the date that the employee first becomes eligible to retire and is no longer required to provide service to earn all or part of the award.

The Company has a long-term incentive program that allows for the award of performance units. The total number of units earned by a participant is based on financial and operational performance measures, and may be paid out in cash or in shares of the Company's common stock. The Company recognizes compensation expense over the three-year term of the grant. Amounts unpaid for all grants under the plan totaled \$7.5 million and \$9.6 million as of March 31, 2012 and December 31, 2011, respectively.

#### **11. Workers' Compensation Expense**



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The following table details the components of workers' compensation expense:

|   | Three Months Ended March 31, |          |
|---|------------------------------|----------|
|   | 2012                         | 2011     |
|   | (In thousands)               |          |
| Service cost                            | \$ 968                       | \$ 193   |
| Interest cost                           | 680                          | 254      |
| Net amortization                        | 277                          | (101)    |
| Total occupational disease              | 1,925                        | 346      |
| Traumatic injury claims and assessments | 5,176                        | 2,325    |
| Total workers' compensation expense     | \$ 7,101                     | \$ 2,671 |

**12. Employee Benefit Plans**

The following table details the components of pension benefit costs:

|   | <b>Three Months Ended<br/>March 31,</b> |             |
|---|---|-------------|
|   | <b>2012</b>                             | <b>2011</b> |
|   | <b>(In thousands)</b>                   |             |
| Service cost                                | \$ 7,596                                | \$ 4,319    |
| Interest cost                               | 3,980                                   | 4,131       |
| Expected return on plan assets              | (5,538)                                 | (5,468)     |
| Amortization of prior service cost (credit) | (36)                                    | 47          |
| Amortization of other actuarial losses      | 3,571                                   | 2,140       |
| Net benefit cost                            | \$ 9,573                                | \$ 5,169    |

The following table details the components of other postretirement benefit costs (credits):

|                                       | <b>Three Months Ended<br/>March 31,</b> |             |
|---------------------------------------|---|-------------|
|                                       | <b>2012</b>                             | <b>2011</b> |
|                                       | <b>(In thousands)</b>                   |             |
| Service cost                          | \$ 549                                  | \$ 405      |
| Interest cost                         | 491                                     | 498         |
| Amortization of prior service credits | (2,995)                                 | (591)       |
| Amortization of other actuarial gains | (90)                                    | (598)       |
| Net benefit cost (credit)             | \$ (2,045)                              | \$ (287)    |

**13. Earnings per Common Share**

The following table provides the basis for earnings per share calculations by reconciling basic and diluted weighted average shares outstanding:

|  | <b>Three Months Ended March 31</b> |             |
|--|------------------------------------|-------------|
|  | <b>2012</b>                        | <b>2011</b> |
|  | <b>(In thousands)</b>              |             |
| Weighted average shares outstanding:                     |                                    |             |
| Basic weighted average shares outstanding                | 211,687                            | 162,576     |
| Effect of common stock equivalents under incentive plans | 221                                | 1,197       |
| Diluted weighted average shares outstanding              | 211,908                            | 163,773     |

The effect of options to purchase 3.0 million and 1.1 million shares of common stock were excluded from the calculation of diluted weighted average shares outstanding for the three month periods ended March 31, 2012 and 2011, respectively, because the exercise price of these options exceeded the average market price of the Company's common stock for these periods.

**14. Guarantees**

The Company has agreed to continue to provide surety bonds and letters of credit for the reclamation and retiree healthcare obligations of Magnum Coal Company ( Magnum ) related to the properties the Company sold to Magnum on December 31, 2005. Patriot Coal Corporation ( Patriot ) acquired Magnum in July 2008. The purchase agreement requires Magnum to reimburse the Company for costs related to the surety bonds and letters of credit and to use commercially reasonable efforts to replace the obligations. If the surety bonds and letters of credit related to the reclamation obligations are not replaced by Magnum within a specified period of time, Magnum must post a letter of credit in favor of the Company in the amounts of the reclamation obligations. As of March 31, 2012, Patriot has replaced \$48.9 million of the surety bonds and has posted letters of credit of \$16.7 million in the Company s favor. At March 31, 2012, the Company had \$38.5 million of surety bonds remaining related to properties sold to Magnum. The surety bonding amounts are mandated by the state and are not directly related to the estimated cost to reclaim the properties.

Magnum also acquired certain coal supply contracts with customers who have not consented to the contracts' assignment from the Company to Magnum. The Company has committed to purchase coal from Magnum to sell to those customers at the same price it is charging the customers for the sale. Under the amended coal supply contracts, as amended, Magnum has the ability to buy out of its obligations under the contract at prices that are predetermined for the remainder of the agreement. Certain other contracts were assigned to Magnum. If Magnum is unable to supply the coal for these coal sales contracts or pay the buy out amount if elected, then the Company would be required to fulfill Magnum's delivery or payment obligations. The longest of the coal supply contracts extends to the year 2017. At market prices effective at March 31, 2012, the maximum amount to fulfill Magnum's obligations under the contracts that have not been assigned over their duration would be approximately \$64.1 million, and the cost of purchasing 573 thousand tons of coal to supply the assigned and guaranteed contracts over their duration would exceed the sales price under the contracts by approximately \$12.2 million. As the Company does not believe that it is probable that it would have to purchase replacement coal, no losses have been recorded in the consolidated financial statements as of March 31, 2012. However, if the Company would have to perform under these guarantees, it could potentially have a material adverse effect on the business, results of operations and financial condition of the Company.

In connection with the Company's acquisition of the coal operations of Atlantic Richfield Company (ARCO) and the simultaneous combination of the acquired ARCO operations and the Company's Wyoming operations into the Arch Western joint venture, the Company agreed to indemnify the other member of Arch Western against certain tax liabilities in the event that such liabilities arise prior to June 1, 2013 as a result of certain actions taken, including the sale or other disposition of certain properties of Arch Western, the repurchase of certain equity interests in Arch Western by Arch Western or the reduction under certain circumstances of indebtedness incurred by Arch Western in connection with the acquisition. If the Company were to become liable, the maximum amount of potential future tax payments is \$16.3 million at March 31, 2012, which is not recorded as a liability in the Company's condensed consolidated financial statements. Since the indemnification is dependent upon the initiation of activities within the Company's control and the Company does not intend to initiate such activities, it is remote that the Company will become liable for any obligation related to this indemnification. However, if such indemnification obligation were to arise, it could potentially have a material adverse effect on the business, results of operations and financial condition of the Company.

## 15. Contingencies

Allegheny Energy Supply (Allegheny), the sole customer of coal produced at the Company's subsidiary Wolf Run Mining Company's (Wolf Run) Sycamore No. 2 mine, filed a lawsuit against Wolf Run, Hunter Ridge Holdings, Inc. (Hunter Ridge), and ICG in state court in Allegheny County, Pennsylvania on December 28, 2006, and amended its complaint on April 23, 2007. Allegheny claimed that Wolf Run breached a coal supply contract when it declared force majeure under the contract upon idling the Sycamore No. 2 mine in the third quarter of 2006, and that Wolf Run continued to breach the contract by failing to ship in volumes referenced in the contract. The Sycamore No. 2 mine was idled after encountering adverse geologic conditions and abandoned gas wells that were previously unidentified and unmapped. After extensive searching for gas wells and rehabilitation of the mine, it was re-opened in 2007, but with notice to Allegheny that it would necessarily operate at reduced volumes in order to safely and effectively avoid the many gas wells within the reserve. The amended complaint also alleged that the production stoppages constitute a breach of the guarantee agreement by Hunter Ridge and breach of certain representations made upon entering into the contract in early 2005. Allegheny voluntarily dropped the breach of representation claims later. Allegheny claimed that it would incur costs in excess of \$100 million to purchase replacement coal over the life of the contract. ICG, Wolf Run and Hunter Ridge answered the amended complaint on August 13, 2007, disputing all of the remaining claims.

On November 3, 2008, ICG, Wolf Run and Hunter Ridge filed an amended answer and counterclaim against the plaintiffs seeking to void the coal supply agreement due to, among other things, fraudulent inducement and conspiracy. On September 23, 2009, Allegheny filed a second amended complaint alleging several alternative theories of liability in its effort to extend contractual liability to ICG, which was not a party to the original contract and did not exist at the time Wolf Run and Allegheny entered into the contract. No new substantive claims were asserted. ICG answered the second amended complaint on October 13, 2009, denying all of the new claims ICG's counterclaim was dismissed on motion for summary judgment entered on May 11, 2010. Allegheny's claims against ICG were also dismissed by summary judgment, but the claims against Wolf Run and Hunter Ridge were not. The court conducted a non-jury trial of this matter beginning on January 10, 2011 and concluding on February 1, 2011. At the trial, Allegheny presented its evidence for breach of contract and claimed that it is entitled to past and future damages in the aggregate of between \$228.0 million and \$377.0 million. Wolf Run and Hunter Ridge presented their defense of the claims, including evidence with respect to the existence of force majeure conditions and excuse under the contract and applicable law. Wolf Run and

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Hunter Ridge presented evidence that Allegheny's damages calculations were significantly inflated because it did not seek to determine damages as of the time of the breach and in some instances artificially assumed future non-delivery or did not take into account the apparent requirement to supply coal in the future. On May 2, 2011, the trial court entered a Memorandum and Verdict determining that Wolf Run had breached the coal supply contract and that the performance shortfall was not excused by force majeure. ICG and Allegheny filed post-verdict motions in the trial court and on August 23, 2011, the court denied the parties' motions. The court entered a final judgment on August 25, 2011, in the amount of \$104.1 million, which included pre-judgment interest. The parties appealed the lower court's decision to the

Superior Court of Pennsylvania. Wolf Run and Hunter Ridge have filed an appeal bond in the amount of \$124.9 million. Briefing is complete and oral argument is scheduled for May 16, 2012.

As of March 31, 2012 and December 31, 2011, the Company had accrued \$109.8 million and \$108.3 million, respectively, for this lawsuit, including interest. The ultimate resolution of this matter could result in an outcome which may be materially different than what the Company has accrued.

In addition, the Company is a party to numerous claims and lawsuits with respect to various matters. The Company provides for costs related to contingencies when a loss is probable and the amount is reasonably determinable. After conferring with counsel, it is the opinion of management that the ultimate resolution of pending claims, other than as noted above, will not have a material adverse effect on the consolidated financial condition, results of operations or liquidity of the Company.

## 16. Segment Information

The Company has three reportable business segments, which are based on the major coal producing basins in which the Company operates. Each of these reportable business segments includes a number of mine complexes. The Company manages its coal sales by coal basin, not by individual mine complex. Geology, coal transportation routes to customers, regulatory environments and coal quality are characteristic to a basin. Accordingly, market and contract pricing have developed by coal basin. Mine operations are evaluated based on their per-ton operating costs (defined as including all mining costs but excluding pass-through transportation expenses), as well as on other non-financial measures, such as safety and environmental performance. The Company's reportable segments are the Powder River Basin (PRB) segment, with operations in Wyoming; the Western Bituminous (WBIT) segment, with operations in Utah, Colorado and southern Wyoming; the Appalachia (APP) segment, with operations in West Virginia, Kentucky, Maryland and Virginia. The Appalachia segment includes the acquired ICG operations in Appalachia, as well as the Company's previous Central Appalachia segment. The Other operating segment represents primarily the Company's Illinois operations and ADDCAR subsidiary, which manufactures and sells its patented highwall mining system.

Operating segment results for the three months ended March 31, 2012 and 2011 are presented below. Results for the reportable segments include all direct costs of mining, including all depreciation, depletion and amortization related to the mining operations, even if the assets are not recorded at the operating segment level. See discussion of segment assets below. Corporate, Other and Eliminations includes the change in fair value of coal derivatives and coal trading activities, net; corporate overhead; land management; other support functions; and the elimination of intercompany transactions.

The asset amounts below represent an allocation of assets used in the segments' cash-generating activities. The amounts in Corporate, Other and Eliminations represent primarily corporate assets (cash, receivables, investments, plant, property and equipment) as well as unassigned coal reserves, above-market acquired sales contracts and other unassigned assets.

| (in thousands)                           | PRB        | APP        | WBIT       | Other Operating Segments | Corporate, Other and Eliminations | Consolidated |
|--|------------|------------|------------|--------------------------|-----------------------------------|--------------|
| <b>Three months ended March 31, 2012</b> |            |            |            |                          |                                   |              |
| Revenues                                 | \$ 401,177 | \$ 469,058 | \$ 144,559 | \$ 24,857                | \$                                | \$ 1,039,651 |

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|   |           |           |         |         |           |            |
|---|-----------|-----------|---------|---------|-----------|------------|
| Income (loss) from operations                 | 32,543    | 15,835    | 31,241  | (3,750) | (21,788)  | 54,081     |
| Total assets                                  | 2,263,517 | 4,640,344 | 752,197 | 940,245 | 1,568,815 | 10,165,118 |
| Depreciation, depletion and amortization      | 41,223    | 76,017    | 18,600  | 3,687   | 439       | 139,966    |
| Amortization of acquired sales contracts, net | (816)     | (13,088)  |         | (113)   |           | (14,017)   |
| Capital expenditures                          | 3,986     | 66,303    | 15,137  | 5,644   | 2,201     | 93,271     |

**Three months ended March 31, 2011**

|   |    |           |    |         |    |         |    |           |    |           |
|---|----|-----------|----|---------|----|---------|----|-----------|----|-----------|
| Revenues                                      | \$ | 393,113   | \$ | 155,439 | \$ | 324,386 | \$ |           | \$ | 872,938   |
| Income from operations                        |    | 46,874    |    | 26,892  |    | 54,394  |    | (25,922)  |    | 102,238   |
| Total assets                                  |    | 2,244,173 |    | 683,949 |    | 710,324 |    | 1,261,532 |    | 4,899,978 |
| Depreciation, depletion and amortization      |    | 41,691    |    | 20,529  |    | 21,016  |    | 301       |    | 83,537    |
| Amortization of acquired sales contracts, net |    | 5,944     |    |         |    |         |    |           |    | 5,944     |
| Capital expenditures                          |    | 2,838     |    | 11,777  |    | 17,302  |    | 6,794     |    | 38,711    |

A reconciliation of segment income from operations to consolidated income before income taxes follows:

|                            | <b>Three Months Ended March 31</b> |             |
|----------------------------|------------------------------------|-------------|
|                            | <b>2012</b>                        | <b>2011</b> |
|                            | <b>(In thousands)</b>              |             |
| Income from operations     | \$ 54,081                          | \$ 102,238  |
| Interest expense           | (74,772)                           | (34,580)    |
| Interest income            | 1,021                              | 746         |
| Income before income taxes | \$ (19,670)                        | \$ 68,404   |

#### **17. Supplemental Condensed Consolidating Financial Information**

Pursuant to the indentures governing Arch Coal, Inc.'s senior notes, certain wholly-owned subsidiaries of the Company have fully and unconditionally guaranteed the senior notes on a joint and several basis. The following tables present condensed consolidating financial information for (i) the Company, (ii) the issuer of the senior notes, (iii) the guarantors under the senior notes, and (iv) the entities which are not guarantors under the senior notes (Arch Western Resources, LLC and its subsidiaries, Arch Receivable Company, LLC and the Company's subsidiaries outside the U.S.):



## Condensed Consolidating Statements of Income

Three Months Ended March 31, 2012

|  | Parent/Issuer | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations | Consolidated |
|--|---------------|---------------------------|---|--------------|--------------|
| <b>Revenues</b>  | \$            | \$ 498,728                | \$ 540,923                                      | \$           | \$ 1,039,651 |
| <b>Costs, expenses and other</b>   |               |                           |   |              |              |
| Cost of sales  | 2,964         | 425,009                   | 448,054   | (25,156)     | 850,871      |
| Depreciation, depletion and amortization                                     | 1,217         | 100,006                   | 38,744  | (1)          | 139,966      |
| Amortization of acquired sales contracts,<br>net                             |               | (13,201)                  | (816)   |              | (14,017)     |
| Selling, general and administrative<br>expenses                              | 18,642        | 1,987                     | 12,046  | (1,814)      | 30,861       |
| Change in fair value of coal derivatives<br>and coal trading activities, net |               | (3,613)                   |   |              | (3,613)      |
| Other operating (income) expense, net  | (3,110)       | (37,700)                  | (4,659)   | 26,971       | (18,498)     |
|  | 19,713        | 472,488                   | 493,369   |              | 985,570      |
| Income from investment in subsidiaries                                       | 77,312        |                           |   | (77,312)     |              |
| Income from operations   | 57,599        | 26,240                    | 47,554  | (77,312)     | 54,081       |
| Interest expense, net:   |               |                           |   |              |              |
| Interest expense   | (82,096)      | (1,179)                   | (11,344)  | 19,847       | (74,772)     |
| Interest income  | 4,827         | 248                       | 15,793  | (19,847)     | 1,021        |
|  | (77,269)      | (931)                     | 4,449   |              | (73,751)     |
| Income (loss) before income taxes  | (19,670)      | 25,309                    | 52,003  | (77,312)     | (19,670)     |
| Benefit from income taxes  | (22,660)      |                           | 1,581   |              | (21,079)     |
| Net income   | 2,990         | 25,309                    | 50,422  | (77,312)     | 1,409        |
| Less: Net income attributable to<br>noncontrolling interest                  | (203)         |                           |   |              | (203)        |
| Net income attributable to Arch Coal   | \$ 2,787      | \$ 25,309                 | \$ 50,422                                       | \$ (77,312)  | \$ 1,206     |
| Total comprehensive income   | \$ 3,948      | \$ 27,242                 | \$ 54,831                                       | \$ (77,312)  | \$ 8,709     |

## Condensed Consolidating Statements of Income

Three Months Ended March 31, 2011

|  | Parent/Issuer | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations | Consolidated |
|--|---------------|---------------------------|---|--------------|--------------|
| <b>Revenues</b>  | \$            | \$ 338,533                | \$ 534,405                                      | \$           | \$ 872,938   |
| <b>Costs, expenses and other</b>   |               |                           |   |              |              |
| Cost of sales  | 3,279         | 251,884                   | 423,323   | (24,802)     | 653,684      |
| Depreciation, depletion and amortization                                     | 672           | 43,277                    | 39,588  |              | 83,537       |
| Amortization of acquired sales contracts,<br>net                             |               |                           | 5,944   |              | 5,944        |
| Selling, general and administrative<br>expenses                              | 20,336        | 1,883                     | 9,913   | (1,697)      | 30,435       |
| Change in fair value of coal derivatives<br>and coal trading activities, net |               | (1,784)                   |   |              | (1,784)      |
| Other operating (income) expense, net  | (4,567)       | (27,456)                  | 4,408   | 26,499       | (1,116)      |
|  | 19,720        | 267,804                   | 483,176   |              | 770,700      |
| Income from investment in subsidiaries                                       | 125,003       |                           |   | (125,003)    |              |
| Income from operations   | 105,283       | 70,729                    | 51,229  | (125,003)    | 102,238      |
| Interest expense, net:   |               |                           |   |              |              |
| Interest expense   | (40,621)      | (714)                     | (10,982)  | 17,737       | (34,580)     |
| Interest income  | 3,742         | 296                       | 14,445  | (17,737)     | 746          |
|  | (36,879)      | (418)                     | 3,463   |              | (33,834)     |
| Income (loss) before income taxes  | 68,404        | 70,311                    | 54,692  | (125,003)    | 68,404       |
| Benefit from income taxes  | 12,530        |                           |   |              | 12,530       |
| Net income   | 55,874        | 70,311                    | 54,692  | (125,003)    | 55,874       |
| Less: Net income attributable to<br>noncontrolling interest                  | (273)         |                           |   |              | (273)        |
| Net income attributable to Arch Coal   | \$ 55,601     | \$ 70,311                 | \$ 54,692                                       | \$ (125,003) | \$ 55,601    |
| Total comprehensive income   | \$ 66,372     | \$ 70,253                 | \$ 52,949                                       | \$ (125,003) | \$ 64,571    |

## Condensed Consolidating Balance Sheets

March 31, 2012

|  | Parent/Issuer | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations   | Consolidated  |
|--|---------------|---------------------------|---|----------------|---------------|
| <b>Assets</b>  |               |                           |   |                |               |
| Cash and cash equivalents                            | \$ 35,196     | \$ 308                    | \$ 82,266                                       | \$             | \$ 117,770    |
| Restricted cash-retirement of ICG obligations        | 8,866         |                           |   |                | 8,866         |
| Receivables  | 46,832        | 20,771                    | 295,844   | (1,733)        | 361,714       |
| Inventories  |               | 256,896                   | 231,790   |                | 488,686       |
| Other  | 108,080       | 79,817                    | 14,186  |                | 202,083       |
| Total current assets                                 | 198,974       | 357,792                   | 624,086   | (1,733)        | 1,179,119     |
| Property, plant and equipment, net                   | 29,966        | 6,367,590                 | 1,495,177                                       |                | 7,892,733     |
| Investment in subsidiaries                           | 8,886,286     |                           |   | (8,886,286)    |               |
| Intercompany receivables                             | (1,443,557)   | (41,436)                  | 1,484,993                                       |                |               |
| Note receivable from Arch Western                    | 225,000       |                           |   | (225,000)      |               |
| Other  | 450,008       | 626,788                   | 16,470  |                | 1,093,266     |
| Total other assets                                   | 8,117,737     | 585,352                   | 1,501,463                                       | (9,111,286)    | 1,093,266     |
| Total assets   | \$ 8,346,677  | \$ 7,310,734              | \$ 3,620,726                                    | \$ (9,113,019) | \$ 10,165,118 |
| <b>Liabilities and Stockholders Equity</b>           |               |                           |   |                |               |
| Accounts payable                                     | \$ 26,036     | \$ 134,697                | \$ 133,608                                      | \$             | \$ 294,341    |
| Accrued expenses and other current liabilities       | 98,109        | 110,821                   | 159,289   | (1,733)        | 366,486       |
| Current maturities of debt and short-term borrowings | 10,876        | 1,180                     | 90,300  |                | 102,356       |
| Total current liabilities                            | 135,021       | 246,698                   | 383,197   | (1,733)        | 763,183       |
| Long-term debt                                       | 3,514,463     | 2,524                     | 450,809   |                | 3,967,796     |
| Note payable to Arch Coal                            |               |                           | 225,000   | (225,000)      |               |
| Asset retirement obligations                         | 891           | 142,014                   | 289,715   |                | 432,620       |
| Accrued pension benefits                             | 21,409        | 4,001                     | 23,968  |                | 49,378        |
| Accrued postretirement benefits other than pension   | 13,731        | 6,272                     | 22,781  |                | 42,784        |
| Accrued workers compensation                         | 21,350        | 45,823                    | 6,839   |                | 74,012        |
| Deferred income taxes                                | 905,635       | 76,961                    |   |                | 982,596       |
| Other noncurrent liabilities                         | 150,013       | 64,098                    | 54,474  |                | 268,585       |
| Total liabilities                                    | 4,762,513     | 588,391                   | 1,456,783                                       | (226,733)      | 6,580,954     |
| Redeemable noncontrolling interest                   | 11,739        |                           |   |                | 11,739        |
| Stockholders equity                                  | 3,572,425     | 6,722,343                 | 2,163,943                                       | (8,886,286)    | 3,572,425     |
| Total liabilities and stockholders equity            | \$ 8,346,677  | \$ 7,310,734              | \$ 3,620,726                                    | \$ (9,113,019) | \$ 10,165,118 |

## Condensed Consolidating Balance Sheets

December 31, 2011

(unaudited)

|  | Parent/Issuer | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations   | Consolidated  |
|--|---------------|---------------------------|---|----------------|---------------|
| <b>Assets</b>  |               |                           |   |                |               |
| Cash and cash equivalents                            | \$ 61,375     | \$ 332                    | \$ 76,442                                       | \$             | \$ 138,149    |
| Restricted cash-retirement of ICG obligations        | 10,322        |                           |   |                | 10,322        |
| Receivables  | 65,187        | 22,037                    | 383,572   | (1,617)        | 469,179       |
| Inventories  |               | 207,050                   | 170,440   |                | 377,490       |
| Other  | 81,732        | 83,122                    | 22,780  |                | 187,634       |
| Total current assets                                 | 218,616       | 312,541                   | 653,234   | (1,617)        | 1,182,774     |
| Property, plant and equipment, net                   | 21,241        | 6,403,658                 | 1,524,251                                       |                | 7,949,150     |
| Investment in subsidiaries                           | 8,805,731     |                           |   | (8,805,731)    |               |
| Intercompany receivables                             | (1,457,864)   | 7,010                     | 1,450,854                                       |                |               |
| Note receivable from Arch Western                    | 225,000       |                           |   | (225,000)      |               |
| Other  | 184,266       | 884,613                   | 13,156  |                | 1,082,035     |
| Total other assets                                   | 7,757,133     | 891,623                   | 1,464,010                                       | (9,030,731)    | 1,082,035     |
| Total assets   | \$ 7,996,990  | \$ 7,607,822              | \$ 3,641,495                                    | \$ (9,032,348) | \$ 10,213,959 |
| <b>Liabilities and Stockholders Equity</b>           |               |                           |   |                |               |
| Accounts payable                                     | \$ 25,409     | \$ 175,196                | \$ 183,177                                      | \$             | \$ 383,782    |
| Accrued expenses and other current liabilities       | 75,133        | 115,685                   | 166,834   | (1,617)        | 356,035       |
| Current maturities of debt and short-term borrowings | 172,564       | 1,987                     | 106,300   |                | 280,851       |
| Total current liabilities                            | 273,106       | 292,868                   | 456,311   | (1,617)        | 1,020,668     |
| Long-term debt                                       | 3,308,674     | 2,652                     | 450,971   |                | 3,762,297     |
| Note payable to Arch Coal                            |               |                           | 225,000   | (225,000)      |               |
| Asset retirement obligations                         | 877           | 140,861                   | 305,046   |                | 446,784       |
| Accrued pension benefits                             | 19,198        | 4,203                     | 24,843  |                | 48,244        |
| Accrued postretirement benefits other than pension   | 13,843        | 6,271                     | 22,195  |                | 42,309        |
| Accrued workers compensation                         | 17,272        | 48,111                    | 6,565   |                | 71,948        |
| Deferred income taxes                                | 621,483       | 355,270                   |   |                | 976,753       |
| Other noncurrent liabilities                         | 152,963       | 64,795                    | 37,624  |                | 255,382       |
| Total liabilities                                    | 4,407,416     | 915,031                   | 1,528,555                                       | (226,617)      | 6,624,385     |
| Redeemable noncontrolling interest                   | 11,534        |                           |   |                | 11,534        |
| Stockholders equity                                  | 3,578,040     | 6,692,791                 | 2,112,940                                       | (8,805,731)    | 3,578,040     |
| Total liabilities and stockholders equity            | \$ 7,996,990  | \$ 7,607,822              | \$ 3,641,495                                    | \$ (9,032,348) | \$ 10,213,959 |

## Condensed Consolidating Statements of Cash Flows

Three Months Ended March 31, 2012

(unaudited)

|   | Parent/Issuer | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries<br>(In thousands) | Eliminations | Consolidated |
|---|---------------|---------------------------|---|--------------|--------------|
| Cash provided by (used in) operating activities                               | \$ (18,535)   | \$ 34,078                 | \$ 39,447                                       | \$           | \$ 54,990    |
| Investing Activities  |               |                           |   |              |              |
| Change in restricted cash   | 1,455         |                           |   |              | 1,455        |
| Capital expenditures  | (1,177)       | (73,657)                  | (18,437)  |              | (93,271)     |
| Proceeds from dispositions of property, plant and equipment                   |               | 546                       | 21,559  |              | 22,105       |
| Purchases of investments and advances to affiliates                           | (3,619)       | (3,488)                   |   | 1,330        | (5,777)      |
| Additions to prepaid royalties  |               | (4,818)                   | (3,444)   |              | (8,262)      |
| Cash used in investing activities   | (3,341)       | (81,417)                  | (322)   | 1,330        | (83,750)     |
| Financing Activities  |               |                           |   |              |              |
| Payments to retire ICG debt   |               | (1,330)                   |   |              | (1,330)      |
| Net decrease in borrowings under lines of credit and commercial paper program | 34,000        |                           |   |              | 34,000       |
| Net proceeds from other debt  | (5,993)       |                           |   |              | (5,993)      |
| Debt financing costs  | (54)          |                           | (46)  |              | (100)        |
| Dividends paid  | (23,327)      |                           |   |              | (23,327)     |
| Issuance of common stock under incentive plans                                | 5,131         |                           |   |              | 5,131        |
| Transactions with affiliates, net   | (14,060)      | 47,315                    | (33,255)  |              |              |
| Cash provided by (used in) financing activities                               | (4,303)       | 47,315                    | (33,301)  | (1,330)      | 8,381        |
| Increase (decrease) in cash and cash equivalents                              | (26,179)      | (24)                      | 5,824   |              | (20,379)     |
| Cash and cash equivalents, beginning of period                                | 61,375        | 332                       | 76,442  |              | 138,149      |
| Cash and cash equivalents, end of period                                      | \$ 35,196     | \$ 308                    | \$ 82,266                                       | \$           | \$ 117,770   |

## Condensed Consolidating Statements of Cash Flows

Three Months Ended March 31, 2011

|   | Parent/Issuer  | Guarantor<br>Subsidiaries | Non-Guarantor<br>Subsidiaries | Consolidated |
|---|----------------|---------------------------|-------------------------------|--------------|
|   | (In thousands) |                           |                               |              |
| Cash provided by (used in) operating activities                               | \$ (75,477)    | \$ 144,796                | \$ 16,826                     | \$ 86,145    |
| Investing Activities  |                |                           |                               |              |
| Capital expenditures  | (900)          | (23,615)                  | (14,196)                      | (38,711)     |
| Proceeds from dispositions of property, plant and equipment                   |                | 502                       | 14                            | 516          |
| Purchases of investments and advances to affiliates                           | (9,529)        | (24,890)                  |                               | (34,419)     |
| Additions to prepaid royalties  |                | (20,915)                  |                               | (20,915)     |
| Cash used in investing activities   | (10,429)       | (68,918)                  | (14,182)                      | (93,529)     |
| Financing Activities  |                |                           |                               |              |
| Net decrease in borrowings under lines of credit and commercial paper program |                |                           | 3,681                         | 3,681        |
| Net proceeds from other debt  | (5,161)        |                           |                               | (5,161)      |
| Debt financing costs  |                |                           | (8)                           | (8)          |
| Dividends paid  | (16,269)       |                           |                               | (16,269)     |
| Issuance of common stock under incentive plans                                | 768            |                           |                               | 768          |
| Transactions with affiliates, net   | 95,911         | (75,893)                  | (20,018)                      |              |
| Cash provided by (used in) financing activities                               | 75,249         | (75,893)                  | (16,345)                      | (16,989)     |
| Increase (decrease) in cash and cash equivalents                              | (10,657)       | (15)                      | (13,701)                      | (24,373)     |
| Cash and cash equivalents, beginning of period                                | 13,713         | 64                        | 79,816                        | 93,593       |
| Cash and cash equivalents, end of period                                      | \$ 3,056       | \$ 49                     | \$ 66,115                     | \$ 69,220    |

**PART II**

**OTHER INFORMATION**

**Item 2. Unregistered Sales of Equity Securities and Use of Proceeds.**

In September 2006, our board of directors authorized a share repurchase program for the purchase of up to 14,000,000 shares of our common stock. There is no expiration date on the current authorization, and we have not made any decisions to suspend or cancel purchases under the program. As of March 31, 2012, there were 10,925,800 shares of our common stock available for purchase under this program. We did not purchase any shares of our common stock under this program during the quarter ended March 31, 2012. Based on the closing price of our common stock as reported on the New York Stock Exchange on May 7, 2012 the approximate dollar value of our common stock that may yet be purchased under this program was \$88.3 million.

**Item 6. Exhibits.**

The following is a list of exhibits filed as part of this Quarterly Report on Form 10-Q:

|       |  |
|-------|--|
| +10.1 | Form of Non-Qualified Stock Option Agreement   |
| +10.2 | Form of Restricted Stock Unit Contract   |
| +10.3 | Form of Restricted Stock Unit Contract for Non-Employee Directors                    |
| +10.4 | Form of Performance Unit Contract  |
| +12.1 | Computation of ratio of earnings to combined fixed charges and preference dividends. |
| 31.1  | Rule 13a-14(a)/15d-14(a) Certification of John Eaves.                                |
| 31.2  | Rule 13a-14(a)/15d-14(a) Certification of John T. Drexler.                           |
| 32.1  | Section 1350 Certification of John Eaves.  |
| 32.2  | Section 1350 Certification of John T. Drexler.                                       |
| +95   | Mine Safety Disclosure Exhibit   |
| 101   | Interactive Data File  |

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+ Previously filed as an exhibit to Arch Coal, Inc.'s Quarterly Report on Form 10-Q for the period ended March 31, 2012, as filed on May 10, 2012.

**Signatures**

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

Arch Coal, Inc.

By:

/s/ John T. Drexler

John T. Drexler

Senior Vice President and Chief Financial Officer

May 11, 2012