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

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, DC 20549

FORM 10-Q/A

(Amendment No. 1)

(Mark One)

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

For the quarterly period ended March 31, 2012

o **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 x No o

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 x No o

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

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

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)

	Three Months Ended March 31, 2012	2011
	(Unaudited)	
Revenues	$ 1,039,651	$ 872,938
Costs, expenses and other		
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
Earnings per common share		
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

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, 2012 (Unaudited)	December 31, 2011
Assets		
Current assets		
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
Property, plant and equipment, net	7,892,733	7,949,150
Other assets		
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
Liabilities and Stockholders Equity		
Current liabilities		
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
Stockholders Equity		
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)

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	Three Months Ended March 31, 2011
	(Unaudited)	
Operating activities		
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
Investing activities		
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)
Financing activities		
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.

6

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, 2012	December 31, 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 6 ¾% 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 6 ¾% 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 (KH)	DKRW Advanced Fuels, LLC (DKRW)	Dominion Terminal Associates (DTA)	Tenaska Trailblazer Partners, LLC (Tenaska)	Millennium Bulk Terminals, LLC (MBT)	Tongue River Railroad, LLC (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
Condensed combined income statement information:		
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
Condensed combined balance sheet information:		
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

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 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

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:

	March 31, 2012			December 31, 2011		
Fair Value of Derivatives (In thousands)	**Asset Derivative**	**Liability Derivative**		**Asset Derivative**	**Liability Derivative**	
Derivatives Designated as Hedging Instruments						
Heating oil diesel purchases	$	$		$ 8,997	$	
Coal	3,256	(218)		1,109		
Total	3,256	(218)		10,106		
Derivatives Not Designated as Hedging Instruments						
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	
Net derivatives as classified in the balance sheets	$ 37,750	$ (9,100)	$ 28,650	$ 24,129	$ (7,828)	$ 16,301

		March 31, 2012	December 31, 2011
Net derivatives as reflected on the balance sheets			
Heating oil	Other current assets	$ 15,707	$ 10,794
Coal	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 Derivatives used in Fair Value Hedging Relationships (in thousands)	**Hedged Items in Fair Value Hedge Relationships**			**Loss on Hedged Items In Fair Value Hedge Relationships**	
	2012	**2011**		**2012**	**2011**
Coal	$	$	Firm commitments	$	$

11

Derivatives used in Cash Flow Hedging Relationships (in thousands)	Gain (Loss) Recognized in OCI (Effective Portion) 2012	2011	Gains (Losses) Reclassified from OCI into Income (Effective Portion) 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		