CLOUD PEAK ENERGY®

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Hyla Hurst
Regulatory Specialist
Office of Natural Resources Revenue
P.O. Box 25165
MS61013C
Denver, Colorado 80225

Subject: Comments for Regulation Identification Number (RIN) 1012-AA00 Regarding Advance Notice of Proposed Rulemaking on Federal and Indian Coal Valuation

Dear Ms. Hurst:

The following comments and attached supporting materials are in response to the May 27, 2011 Federal Register notice requesting public comments and suggestions relevant to valuation and royalties for coal produced from Federal and Indian leases.

This comment package is being submitted on behalf of Cloud Peak Energy Inc. Cloud Peak Energy Inc. is one of the safest producers of low sulfur, high quality subbituminous coal in the United States. The company wholly owns and operates three Powder River Basin (PRB) coal mines, which have been shipping coal since the mid-1970s. Coal from the PRB powers almost half of all U.S. coal-fired electric generation. The Antelope and Cordero Rojo mines are located in northeast Wyoming and the Spring Creek Mine is located in southeast Montana near Decker. Cloud Peak Energy (NYSE: CLD) is the only Wyoming headquartered company listed on the New York Stock Exchange. With approximately 1,550 employees, the company works to create the most sustainable value from its resources while providing fuel to help power the country. Cloud Peak Energy also owns a 50 percent non-operating interest in the Decker Mine in southern Montana.

The May 27, 2011 Federal Register notice includes requests for comments and suggestions on several aspects of coal valuation and royalty considerations. In general, Cloud Peak Energy believes that the existing regulations are quite workable, that reporting and compliance systems have been established specifically for the current version of the regulations and that they should not be revised. Below are several of the requests, shown in italics, accompanied by Cloud Peak Energy's corresponding responses.

A. Alternative Valuation Methods to the current basis of Arm's-Length Gross Proceeds

- *What alternatives to gross proceeds would you recommend?*

  Cloud Peak Energy comments: Upon reviewing potential options CPE does not believe that there are any alternatives to the current Gross Proceeds system that would provide equivalent or better streamlined benefits to lessees, ONRR, or to county governments receiving a portion of the proceeds. Any alternative that would deviate from a market-based valuation system would increase the potential for arbitrary interpretations and/or inconsistent application, leading to a more cumbersome and uncertain process.

- *Would a dollars per energy content unit or dollars per weight method be reasonable? If so, how should such a value be established?*

  Cloud Peak Energy comments: No. Similar to the responses for alternatives for the gross proceeds system, changing from the current system to an energy content basis or dollars per weight basis would introduce potential for arbitrary interpretations and/or inconsistent application, leading to a more cumbersome and uncertain process. Either the energy content or dollar-weight-based alternatives would require development of unique valuations for each mine to sustain a revenue neutral position for each jurisdiction. While this might have some feasibility for a constructed dollar-weight-based system, it would remove any royalty certainty for longer-term contracts, penalizing that part of the market. As those longer-term contracts provide stability in the coal valuation process, and are essential for large-scale capital investment in western coal mining operations, such an alternative would be counterproductive to improving the current status.

- *Should such "fixed" royalty values be revised from time to time? If so, on what basis..?*

  Cloud Peak Energy comments: No. The fixed royalty approach in the current system is one of the foundation points in the current system that provides a measure of certainty to coal lessees. It should not be revised in any way that does not increase that level of certainty.

- *Are there published index prices that accurately reflect the actual market value of coal? If so, what are those index prices and to what areas of the country or to what types of coal do they apply?*

  Cloud Peak Energy comments: Available price indices are generally limited in geographic coverage and often have different focal points that don't lend themselves to universal use. For this reason, revisions that would use these indices as a base would likely be problematic. For example, indices are published for 8800 Btu and 8400 Btu subbituminous products for the Powder River Basin area of Wyoming, but they are not available for southwestern Wyoming, Montana, Colorado, Utah or New Mexico. Neither are those indices available for any of the regional Indian coal. Additionally, our review indicates that some indices focus on short-term pricing while others target long-term pricing, which would contribute to issues of interpretation and applicability. In some cases the volumes involved in the indices are quite low, leading to questions of how representative they may be.

B. Changes to the benchmarking methods to address Non-Arm's-Length Arrangements

- *Should the current non-arm's length benchmarks and their current sequential priority be retained? If not, what other methodologies might ONRR use to determine the royalty value of coal not sold at arm's length?*

  Cloud Peak Energy comments: Yes with modifications to the first benchmark. Due to the unique properties of coal produced from leases at individual mines and the commercial difficulty in obtaining contract sales data about comparable third party sales or purchases in the area, comparable arm's length sales at the lessee's own mine should be included as part of the first benchmark in setting the value for any non-arm's length sales. This provides the most accurate comparison to arm's length sales and the same quality of coal, over the same tenure, at the same time of execution for comparable delivery times; i.e., it matches all factors to be most comparable. If sufficient comparable arm's length sales data are not available to establish applicable values for the non-arm's length sales, then applying an applicable index base, or an appropriately amended index base, should be the preferred alternative. While the indices have utility as a secondary option, they are not appropriate for system-wide substitution as a preferred option for reasons detailed in comments above and below. In any considerations, for coal consumed by the lessee or an affiliated company, the current point-of-sale benchmarks need to be retained as they represent the most reliable methods providing certainty to the lessee and to the agency.

- *Should the factors for determining the comparability of arm's length contracts to non-arm's length contracts … be amended, clarified, or removed?*

  Cloud Peak Energy comments: No changes should be implemented. The current system of determining applicability of arm's length contracts to non-arm's length contracts is workable. However, if system improvements are contemplated they should be focused on specific comparable parameters of price, time of execution, time of delivery, duration, and/or quality-quantity of coal specified in the arm's length contract as these are the relevant factors. Using alternative bases or other less relevant factors, such as market considerations or contract term, would generally increase the potential for issues with interpretation and applicability.

- *Should the royalty value of coal initially sold under non-arm's length conditions be based on the gross proceeds received from the first arm's length sale…?*

  Cloud Peak Energy comments: No. This suggested change would make it impossible for any lessee to compete for sales away from the mine. Unlike a mining company, a non-mine broker could buy the same type of coal, transport it and sell it without paying any royalties. Such a change would put coal companies at a severe disadvantage, penalizing coal companies that endeavor to develop the business and to maintain and increase the jobs base. The suggested change would be counterproductive for the coal leasing, production and royalty system and should not be implemented.

- *Should the royalty value of coal sold under non-arm's length conditions be based on a published index price? If so, which index and why?*

  Cloud Peak Energy comments: As noted above, indices have utility only as a secondary alternative; the preferred method needs to remain comparable arm's length sales at each mine. However, indices are not appropriate as a system-wide first priority option - as noted in other responses above, available price indices are generally limited in geographic coverage and often have differing focal points in time scale. For these reasons, revisions that would mandate use these indices as a first priority base would likely be problematic for both the lessee and the agency.

- *Should the royalty value be determined by calculating the cost to produce the coal plus a return on capital investment, if the particular coal is never sold at arm's length? If so, how should the return on capital investment be calculated?*

  Cloud Peak Energy comments: No. Attempts to identify and concur upon methods for "calculating the cost to produce the coal" at state and local levels have been prone to a high level of complexity in interpretations and compliance. Based on those experiences we would not support such a proposal on a federal level. If these changes are contemplated, however, we would suggest that the "return on capital investment" provisions should be the equivalent of the existing cost of capital provisions for gas processing at 30 CFR § 1206.159(b)(2)(v). That is: *The rate of return must be the industrial rate associated with Standard and Poor's BBB rating. The rate of return must be the monthly average rate as published in Standard and Poor's Bond Guide for the first month for which the allowance is applicable. The rate must be redetermined at the beginning of each subsequent calendar year.*

C. Potential Changes to the Transportation Allowances (and Washing Allowances)

- *Can the process of determining appropriate transportation and washing deductions or allowances be simplified? If so, how?*

  Cloud Peak Energy comments: For any consideration of transportation and/or washing deductions for arm's length transactions, the current approach of relying on actual cost remains the best option and this needs to be retained as the deduction base. For non-arm's length transactions the current benchmarks are workable, provided that the mine of origin is the first consideration for setting market value. Non-arm's length transactions need to be valued based on comparable sales from the same mine whenever possible.

- *Should ONRR allow bundled charges for coal transportation or washing?*

  Cloud Peak Energy comments: If any changes are implemented they should be structured to ensure that the point of first sale remains as the point of royalty assessment.

- *Should ONRR set standard cents per ton allowance amounts for washing and transportation in lieu of calculating actual costs? If so, how...?*

  Cloud Peak Energy comments: No. Due to the unpredictability of the variable costs involved and the diversity of transportation and washing options, standard allowances will not address the range of cost outcomes and should not be set for these items.

- *Should transportation allowances be based on yearly averages from one region to another?*

  Cloud Peak Energy comments: No. The current reliance on actual costs is the most appropriate and avoids issues that would arise from variability in transportation volumes throughout the year, the various combinations of transportation methods and the variability of costs for each shipment. The latter would include variable fuel surcharges imposed by carriers based on variation in diesel costs. Additionally, given the numerous regional destinations of coal from any one region (e.g., Powder River Basin coal is shipped virtually throughout the US) this would require an unworkable matrix of interregional averages that would need to be constantly adjusted for variables.

- Should the coal transportation and washing allowances be limited to a maximum percentage in a manner similar to gas transportation and processing allowances? If coal washing and transportation allowances should be limited,..., what would be an appropriate percentage?

  Cloud Peak Energy comments: No changes are warranted in the current approach.

D. Potential combination of Federal and Indian coal valuation regulations

Cloud Peak Energy comments: The current approaches for Federal and Indian coal valuation are well understood, and state, county and tribal governments as well as lessees have systems in place to collect information and report within the current structures. Any efforts to combine these regulations would result in changes to those structures, with attendant transitional costs, which are not warranted. Additionally, associated issues of sovereignty would likely accompany any modifications to the current regulatory structure.

Thank you in advance for your considerations of these comments and for incorporation of these points into any subsequent phases of this proposed rulemaking process. Please feel free to contact me if additional details or explanations of these comments would be helpful in that process.

Sincerely,

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