# ENERGIZING THE WORLD ONE BTU AT A TIME

Peabody

**2009 Annual Report**
**Peabody Energy NYSE: BTU**

# ENERGY

# ONE BTU AT A TIME

Peabody Energy (NYSE: BTU) is the world's largest private-sector coal company. The strength of our global platform, strategies and people allowed us to deliver the second best performance in our history in the face of a severe recession.

BTU is energy. We are serving high-growth markets, lighting lives and fueling economies in dozens of nations on six continents. We are the only global pure-play coal investment and a global leader in clean coal solutions. We are One BTU… and we are energizing the world, one Btu at a time.

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# THERE'S ONLY ONE BTU

Peabody's coal fuels energy needs in developing Asia and around the world. Increased use of coal drives improved lifestyles and economies.

Gregory H. Boyce
Chairman and Chief Executive Officer

**Dear Shareholder:**

One BTU. The phrase points to the unique nature of the world's largest private-sector coal company. It points to the combined power of our people and projects serving customers on six continents. It points to a ticker symbol of an energy leader that generated a 100 percent total shareholder return in 2009. And it points to the simple building block of energy that empowers lives and global economies.

Peabody is the only global pure-play coal investment. And with the industry's leading reserve position, Peabody is Btu-rich, housing an enormous supply of energy to fuel the fastest growing markets in the world… from the steel mills of northern China to the new generating stations of coastal India to the baseload power plants of the United States.

BTU fuels the most basic energy needs… bringing light and warmth to countless families in developing nations. We power 21st Century classrooms… state-of-the-art surgical suites… and modern research facilities, providing energy that lifts people everywhere to a better quality of life.

We have the best talent and assets in the industry, and we're using the combined strength of our strategic initiatives and the power of our global platform… energizing the world one Btu at a time.

**Peabody is using the combined strength of our strategic initiatives and the power of our global platform… energizing the world one Btu at a time.**

**Your company turned in superior results, delivering the second best financial performance in our history** in the face of a severe global recession. In 2009, BTU:

- Reported record global safety performance, improving our safety rate 21 percent over the prior year;
- Generated a 100 percent total shareholder return;
- Expanded U.S. margins per ton 22 percent, resulting in record U.S. mining EBITDA of $1.0 billion;
- Accelerated Australian coal shipments in the second half of 2009, unveiled a plan to increase Australian volumes up to 40 million tons annually by 2014, and advanced rail and port access in Australia;
- Contained costs through comprehensive process improvement and operational cost management programs;
- Achieved operating cash flows of more than $1 billion, generating significant end-of-year liquidity of $2.5 billion;
- Expanded our global footprint in developing Asia, opening a trading hub in Singapore, a new business development office in Indonesia and creating the Peabody-Polo joint venture in Mongolia;
- Advanced major clean coal and Btu Conversion initiatives in the United States, China and Australia;
- Ranked among the top 25 companies in the *Forbes* 2009 Platinum List of Best Managed Companies and was recognized as one of the top investments by *Fortune* for the prior one- and five-year periods; and
- Achieved more than 30 awards for safety, financial and environmental performance, including Global Energy Award honors for our innovative coal education program.

**BTU delivered a total shareholder return that was nearly four times that of the S&P 500 in 2009.** We manage the company for long-term shareholder value. Your company's results are exemplary, outperforming coal peers more than twelvefold since our initial public offering in 2001. During the same period, we also delivered a 646 percent return compared to 7 percent for the S&P 500.

What is driving Peabody's long-term growth thesis? Simply put, we are well positioned to fuel the world's fastest developing markets: the Asia-Pacific region globally, and markets served by the Powder River and Illinois basins in the United States. Developing nations lifted the world from recession in 2009, and these economies are expected to grow at multiples of developed nations in 2010. U.S. markets appear to have stabilized and should continue to recover this year.

**Looking forward, BTU remains focused on increasing shareholder value by serving the fastest growing markets.** Peabody has strong access to high-growth regions through our expanding Australian platform, trading activities and Asian growth projects. We have an excellent U.S. position as the largest producer in the fastest growing regions. We have outstanding liquidity to create shareholder value.

Our goal is to deliver on growth this year by:

- Increasing our Australian metallurgical and thermal exports 20 to 30 percent;
- Maintaining U.S. production and benefiting from a strategy that has our U.S. volumes fully contracted for 2010, with leverage to improving markets in later years;
- Continuing to expand our business development and trading activities in the Australia-Asia region; and
- Investing in longer-term growth projects while targeting value-added acquisitions and joint ventures.

**Greater use of coal is the world's best solution for fueling energy needs** and achieving important economic and environmental goals… what I call the 3Es.

Peabody's executive team (from left) includes Greg Boyce, Fred Palmer, Alex Schoch, Mike Crews, Eric Ford, Sharon Fiehler and Rick Navarre.

Every day we use more coal, more cleanly, to benefit the world's people and economies.

It is clear that China, India and emerging Asia represent stunning long-term growth opportunities. China is expected to quickly become the world's second largest economy behind the United States, with annual coal use set to grow the equivalent of two times current U.S. coal use in the next decade.

India, too, is moving full throttle and is likely to become the world's fastest growing coal importer. Forecasts suggest India will become the second largest coal consumer behind China in as little as two decades. Should China and India alone use as much coal per person as the United States, the world would consume nearly twice as much coal as it does today.

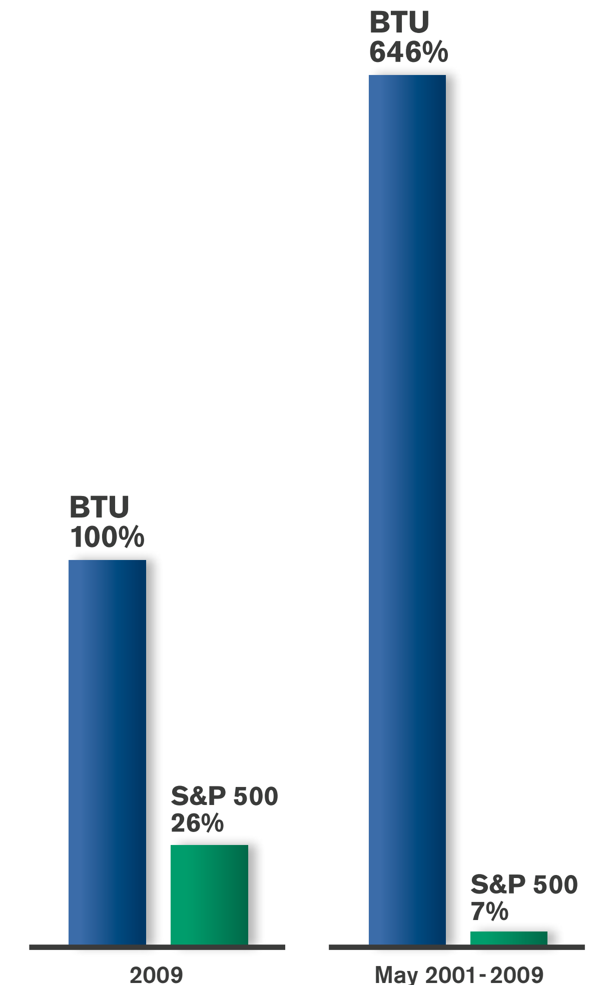
My visits to the GreenGen construction site near Tianjin, China, demonstrate the momentum we are gaining for deployment of clean coal technologies. Peabody is the only non-Chinese equity partner in GreenGen, which will be among the world's largest coal plants with near-zero emissions. It will begin phase one generation as quickly as next year, ultimately capturing carbon to enhance oil recovery from nearby oil fields.

As the United States and China pursue greater cooperation on clean energy solutions, President Barack Obama and China President Hu Jintao jointly cite GreenGen as a world model. Peabody is a global leader in clean coal solutions, and GreenGen is among a dozen projects and partnerships we are advancing around the world.

**The foundation for our success is guided by best practices** that are supported by our Board of Directors. This past year we welcomed Frances Keeth, former Executive Vice President of Royal Dutch Shell, plc; and Robert Malone, past Chairman and President of BP America Inc.

Fran and Bob further expand our perspective on global energy markets and are welcome additions as BTU continues to pursue strategic global growth opportunities.

## BTU STRONGLY OUTPERFORMS S&P 500 IN 2009 AND LONG TERM




BTU delivered a 100 percent total shareholder return in 2009, nearly four times that of the S&P 500. And since our May 2001 initial public offering, BTU achieved a 646 percent return compared to 7 percent for the S&P 500.

I thank our Board of Directors for its energy and wisdom, and I applaud our 7,300 employees who are energizing the world, every day… one Btu at a time.

Sincerely,

Gregory H. Boyce
Chairman and Chief Executive Officer
March 15, 2010

BTU is expanding its access to transportation infrastructure in Australia through development of the Newcastle Coal Infrastructure Group (NCIG) terminal, which is set to begin operating in the second half of 2010. NCIG will add 30 million tonnes of export volume, and longer-term expansion is planned.

# MANY COUNTRIES, MULTIPLE PROJECTS
# ONE BTU

Around the world and around the clock, Peabody's business platform serves six continents and creates strategic advantage and shareholder value. BTU fuels major economies in high-growth regions.

Coal has been the fastest growing fuel in the world for each of the past six years, far outpacing increases in oil, natural gas and nuclear power. And coal demand growth is expected to exceed the combined increase from gas, oil, nuclear and hydro through 2030.

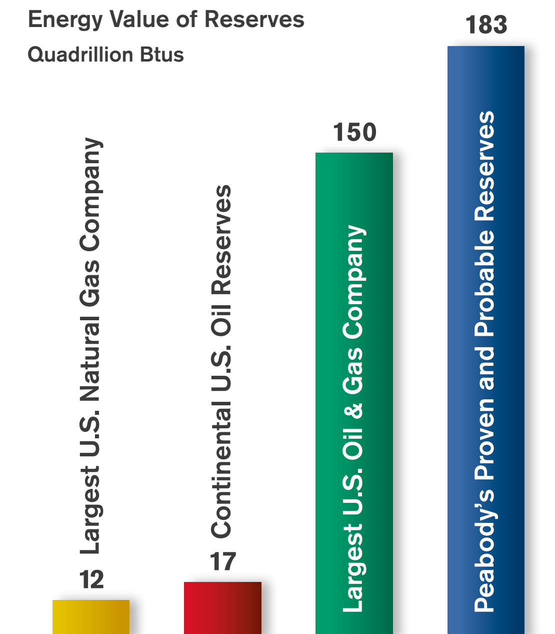
Asia-Pacific markets will lead the way, propelled by China and India, which are experiencing surging electrification, industrialization and urbanization all at once. Ultimately India is likely to be the world's fastest growing coal importer.

The highly efficient El Segundo Mine in New Mexico powered into full production in 2009 to serve long-term customer contracts with Southwest utilities.

## THE POWER OF BTU IS UNMATCHED

**Energy Value of Reserves**

**Quadrillion Btus**




The energy in BTU's reserves is equal to 183 quadrillion Btus, exceeding the oil and gas reserves of the largest U.S. private-sector oil company and the proven oil reserves in the Continental United States.

*Source: BP Annual Reports and Accounts Performance Review, and company reports.*

China, long a coal exporter, became a net importer of more than 100 million tonnes of coal in 2009. By 2030, coal generation is expected to grow 2.5 times in China and 3.5 times in India, fueling enormous energy needs that have redefined the landscape for global coal imports.

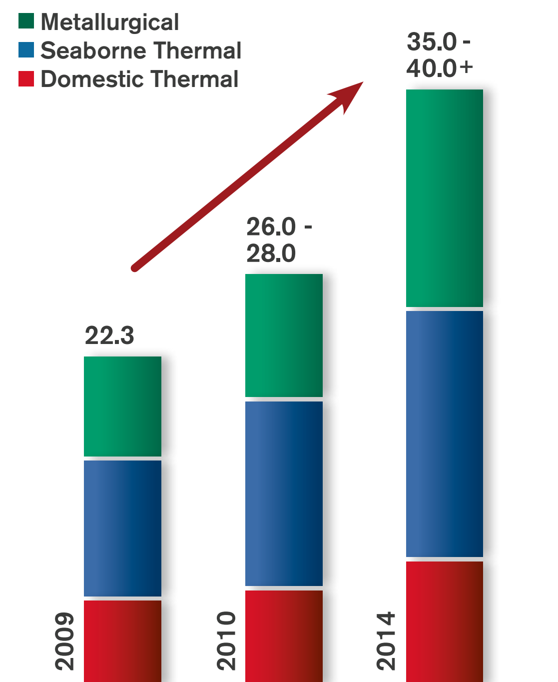
## The Energy to Fuel Asian Growth

BTU is powering Asian growth. We are expanding our Australian operations, increasing global trading activities, and advancing projects and partnerships with major coal, power, steel and rail companies in China and Mongolia.

Peabody is investing in a major capital program to expand its Australian metallurgical and thermal production. We are increasing our metallurgical coal production in Queensland and New South Wales, targeting 12 million to 15 million tons per year of seaborne metallurgical coal by 2014. The company is proceeding with permitting for the large Denham Mine, extending our operations at the Burton Mine and increasing output at the Millennium and Metropolitan mines.

The low-cost Wilpinjong Mine in New South Wales will increase thermal coal production by 2 million to 3 million tons annually. Wilpinjong is among the most productive mines in Australia.

**AUSTRALIAN VOLUMES SET TO GROW UP TO 40 MILLION TONS BY 2014**




A dramatic build-out of BTU's Australian platform will increase metallurgical and thermal exports. Peabody annually is targeting 35 million to 40 million tons of Australian production by 2014.

These volumes are vital for steel producers in China, India and other Asia-Pacific nations that are significantly short of quality metallurgical coal.

In New South Wales, expansion of the Wambo complex and the low-cost Wilpinjong Mine is planned to increase Peabody's thermal coal exports, with 15 million to 17 million tons per year targeted by 2014. Peabody's thermal exports serve growing coal demand in China, India and other Asian nations that are expected to account for 90 percent of coal growth the next two decades.

We have access to growing transportation networks in Australia through new contracts with rail providers and access to port throughput. Peabody has the second largest interest in the Newcastle Coal Infrastructure Group (NCIG) export terminal in New South Wales, which will be operational in the second half of this year. The terminal will add 30 million tonnes of capacity at a time when Australia is setting export records.

ONE BTU

Expansion at the Metropolitan Mine in New South Wales will increase capacity by one million tons annually by 2014. The mine serves steel producers in China, India and other Asia-Pacific nations.

## Largest Producer in Fastest Growing U.S. Regions

Improved realized pricing and cost containment grew Peabody's U.S. margins by 22 percent in 2009, and this year Peabody celebrates 40 years of leadership as the largest U.S. coal producer. Peabody also has the largest production and reserve position in the Powder River Basin and the Illinois Basin. These basins serve the fastest growing U.S. regions and the majority of new coal plants that are coming on line in the next several years.

In the Powder River Basin, Peabody is consolidating volumes into the most productive coal mine in the world: the North Antelope Rochelle Mine. In the Southwest, the new low-cost El Segundo Mine is reaching its stride and is the most productive U.S. mine outside of the Powder River Basin. And in the Midwest, the 8 million ton-per-year Bear Run Mine will begin operations in the second half of 2010. Bear Run is the largest new surface mine to be built in the Eastern United States and is anchored by long-term customer contracts that are expected to deliver billions of dollars in revenues.

As BTU continues to advocate greater use of coal, we also continue to advance near-zero emissions and carbon management. Peabody is the only non-Chinese equity partner in GreenGen; a founding member of the FutureGen Alliance; and a founding partner of COAL21 in Australia. BTU is also a founding member of the U.S. and China Energy Cooperative Program; and the Global Carbon Capture and Storage Institute, which seeks to develop ten large scale demonstration projects worldwide by 2020.

One person at a time… one project at a time… one nation at a time, BTU is powering clean energy solutions that are energizing the world.

The Bear Run Mine in Indiana is expected to produce 3 million to 4 million tons of coal this year. It will be the largest surface mine in the Eastern United States, with eventual annual capacity of 8 million tons.

Every day, coal lights countless cities in the developing world, improving lives and powering fast growing economies. A coal vessel approaches a port in China, a nation that became a net importer of more than 100 million tonnes of coal this past year.

# ENERGIZING THE WORLD ONE BTU AT A TIME

Each year, the typical American consumes as much as 325 million Btus of energy to fuel a high tech, high quality lifestyle. That is more than five times the per capita electricity use of the average citizen in China and 25 times that of the typical resident in India. But China and India are quickly catching up. On an energy equivalency basis with the United States, China and India will need at least 2,100 additional 500 megawatt power plants in coming decades… and most are likely to be coal fueled.

As developing economies like China and India gain greater access to the benefits of energy, Peabody is seizing the opportunity to energize the world and drive economic growth and a better quality of life.

The world is expected to require an additional 148 quadrillion Btus of electricity by 2030, the equivalent power of 150 Californias. Coal's affordability, abundance and security of supply mean that coal powers more electricity than any other fuel. And coal's versatility adds to its attraction: the energy in coal can be converted into other high demand energy forms, including substitute natural gas and transportation fuels.

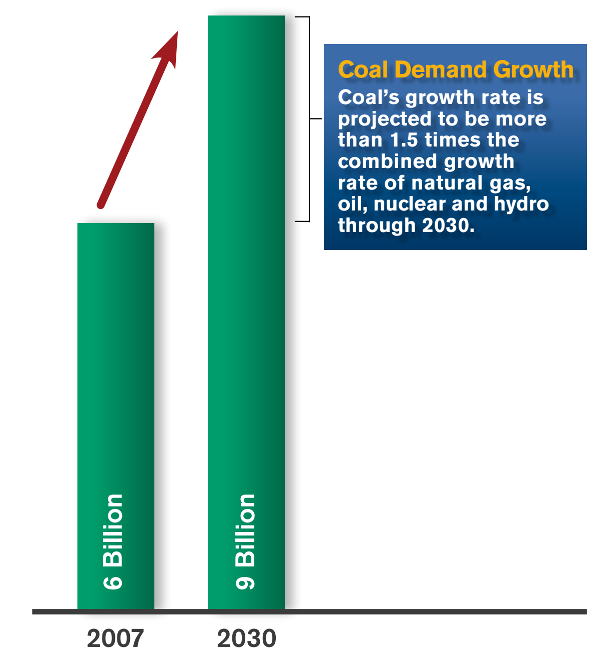
## The Solution for Social Progress

Energy is essential, like food, shelter and oxygen. Yet even in the second decade of the 21st Century, more than half of the world's population still lacks adequate access to electric power that is so vital for the most basic needs: warmth, light and clean water.

For every child born in France, 30 are born in India. Some 600 million people live in China's cities while German cities have 62 million. Developing nations are growing at an unprecedented pace, and must have access to the same low-cost energy and high quality of life mature economies enjoy.

### GLOBAL COAL USE ESTIMATED TO GROW 53 PERCENT BY 2030

Tons of Coal




Coal's best days are ahead, with coal forecast to grow faster than other fuels through 2030. Asia is expected to represent 90 percent of the approximately 3 billion tons of coal demand growth during this time.

*Source: International Energy Agency 2009 World Energy Outlook.*

The world needs all sources of energy to meet enormous demand. But alternatives to coal are harder to find, more difficult to drill and more expensive to produce. Coal produces reliable baseload power every hour of every day at a fraction of the delivered cost of oil and natural gas.

Around the world, nations are using coal to power their progress. There are about 250 gigawatts of coal-fueled generation under construction, representing 950 million tonnes per year of incremental coal demand, along with 4.5 million jobs and $1 trillion in economic benefits.

This is the largest build-out of new coal-fueled electricity in a generation. In 2010 alone, 92 gigawatts of coal are expected to come on line, requiring nearly 365 million tonnes of new coal supplies.

## Technology Drives Environmental Solutions

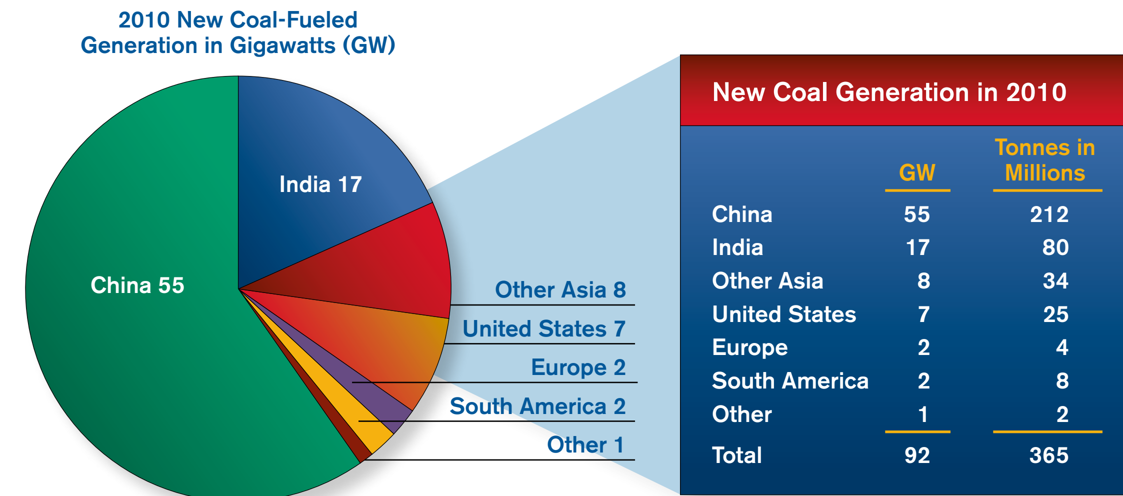
Coal's economic stimulus and energy security carries over into environmental progress. Since 1970 when the first major U.S. Clean Air Act was written, electricity use from coal and gross domestic product have tripled. Yet during the same period, regulated emissions were reduced 84 percent per megawatt hour.

## CARBON CAPTURE AND STORAGE PROJECTS ACCELERATE AROUND THE WORLD

Carbon capture and storage (CCS) projects are advancing rapidly around the world, with global leaders calling for development of 100 CCS projects this decade. BTU is advancing a dozen clean coal, low carbon projects and partnerships, including China's GreenGen near-zero emissions power plant; Australia's COAL21 Callide initiative to reduce carbon dioxide during combustion; and the Western Kentucky Carbon Storage Project, a study to evaluate geology for long-term storage. Greater deployment of CCS will enable nations to meet increasing electricity demand and strengthen national security through enhanced domestic oil production.
*Source: World Coal Institute 2010 Carbon Capture and Storage Projects.*

## MAJOR GLOBAL COAL-FUELED GENERATION BUILD-OUT UNDER WAY

**85+ Percent of New 2010 Coal Plants in Asia**




New Coal Generation in 2010

| | GW | Tonnes in Millions |
|---|---|---|
| China | 55 | 212 |
| India | 17 | 80 |
| Other Asia | 8 | 34 |
| United States | 7 | 25 |
| Europe | 2 | 4 |
| South America | 2 | 8 |
| Other | 1 | 2 |
| Total | 92 | 365 |

China, India and developing Asia are expected to account for more than 85 percent of the global build-out of new generation. This year 92 gigawatts are expected to come on line, representing 365 million tonnes of coal demand and continuing to demonstrate the enormous power of the world's fastest growing fuel.
*Source: Platts Worldwide Power Plant Database, China Electricity Council and Peabody analysis.*

The next generation of supercritical, gasification and carbon capture and storage (CCS) technologies under development place the ultimate green goal of near-zero emissions from coal within reach.

Research suggests that coal with CCS is the low-cost, low carbon energy solution, which could be 15 to 50 percent less expensive than nuclear, wind or natural gas with CCS. Peabody is a global leader in clean coal solutions, advancing signature projects in Asia, Australia and North America.

There is increasing global interest in managing carbon. The Obama administration is encouraging broad deployment of CCS technologies, with as many as ten commercial CCS demonstrations on line as quickly as 2016.

World leaders have set aside more than $30 billion for demonstration plants; Australia has committed $100 million in annual government funding for 20 commercial scale projects worldwide by 2020; and the International Energy Agency is calling for 100 large scale CCS plants around the world in the next decade.

Coal provides a path to a better way of life for billions of people. It forms the foundation of our global economy. And it fuels a sustainable future. Through greater use of clean coal, Peabody is defining the progress and delivering the prosperity of the 21st Century… one Btu at a time.

## COAL IS THE SOLUTION FOR ALLEVIATING ENERGY POVERTY

Access to modern energy is a basic necessity. Yet 56 percent of the world's population has no access or inadequate access to electricity. Peabody believes that coal is the only energy source with the scale and low cost to alleviate energy poverty.
*Source: U.S. Census Bureau and World Coal Institute, "Coal Tackling Poverty."*

ONE BTU

## Selected Financial Data

*All prior years adjusted to reflect continuing operations*

| Years Ended December 31 (In millions, except per share data) | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|
| **Results of Operations Data** | | | | | |
| Total revenues | **$6,012.4** | $6,561.0 | $4,523.8 | $4,045.6 | $3,597.9 |
| Costs and expenses | **5,167.6** | 5,164.7 | 3,924.1 | 3,432.8 | 3,166.3 |
| Operating profit | **844.8** | 1,396.3 | 599.7 | 612.8 | 431.6 |
| Interest expense, net | **193.1** | 217.0 | 228.8 | 127.8 | 88.9 |
| Income from continuing operations before income taxes | **651.7** | 1,179.3 | 370.9 | 485.0 | 342.7 |
| Income tax provision (benefit) | **193.8** | 191.4 | (70.7) | (85.6) | 62.3 |
| Income from continuing operations, net of income taxes | **457.9** | 987.9 | 441.6 | 570.6 | 280.4 |
| Income (loss) from discontinued operations, net of income taxes | **5.1** | (28.8) | (180.1) | 30.7 | 144.8 |
| Net income | **463.0** | 959.1 | 261.5 | 601.3 | 425.2 |
| Less: net income (loss) attributable to noncontrolling interests | **14.8** | 6.2 | (2.3) | 0.6 | 2.5 |
| Net income attributable to common stockholders | **$ 448.2** | $ 952.9 | $ 263.8 | $ 600.7 | $ 422.7 |
| Basic earnings per share from continuing operations [1] | **$ 1.66** | $ 3.63 | $ 1.67 | $ 2.15 | $ 1.06 |
| Diluted earnings per share from continuing operations [1] | **$ 1.64** | $ 3.60 | $ 1.64 | $ 2.11 | $ 1.04 |
| Weighted average shares used in calculating basic earnings per share | **265.5** | 268.9 | 264.1 | 263.4 | 261.5 |
| Weighted average shares used in calculating diluted earnings per share | **267.5** | 270.7 | 268.6 | 268.8 | 267.3 |
| Dividends declared per share | **$ 0.25** | $ 0.24 | $ 0.24 | $ 0.24 | $ 0.17 |
| **Other Data** | | | | | |
| Tons sold | **243.6** | 255.0 | 235.5 | 221.2 | 213.7 |
| Net cash provided by (used in) continuing operations: | | | | | |
| Operating activities | **$1,053.5** | $1,409.8 | $ 460.7 | $ 611.1 | $ 672.4 |
| Investing activities | **(408.2)** | (419.3) | (538.9) | (2,055.6) | (506.3) |
| Financing activities | **(102.3)** | (487.0) | 41.7 | 1,403.0 | (41.4) |
| Adjusted EBITDA [2] | **1,290.1** | 1,846.9 | 969.7 | 909.7 | 696.4 |
| **Balance Sheet Data (at period end)** | | | | | |
| Total assets | **$9,955.3** | $9,695.6 | $9,082.3 | $9,504.7 | $6,852.0 |
| Total long-term debt (including capital leases) | **2,752.3** | 2,793.6 | 2,909.0 | 2,911.6 | 1,332.0 |
| Total stockholders' equity | **3,755.9** | 3,119.5 | 2,735.3 | 2,587.0 | 2,178.5 |

*[1] Effective January 1, 2009, we adopted the two-class method to compute basic and diluted earnings per share. This method has been retrospectively applied to all periods presented.*

*[2] We define Adjusted EBITDA as income from continuing operations before deducting net interest expense, income taxes, asset retirement obligation expense and depreciation, depletion and amortization. Adjusted EBITDA is used by management to measure our segments' operating performance, and management also believes it is a useful indicator of our ability to meet debt service and capital expenditure requirements. Because Adjusted EBITDA is not calculated identically by all companies, our calculation may not be comparable to similarly titled measures of other companies. Adjusted EBITDA is reconciled to its most comparable measure, under United States generally accepted accounting principles, as reflected in Note 22 to our consolidated financial statements.*

| Adjusted EBITDA is calculated as follows, (unaudited): | 2009 | 2008 | 2007 | 2006 | 2005 |
|---|---|---|---|---|---|
| Income from continuing operations, net of income taxes | **$ 457.9** | $ 987.9 | $ 441.6 | $ 570.6 | $ 280.4 |
| Income tax provision (benefit) | **193.8** | 191.4 | (70.7) | (85.6) | 62.3 |
| Depreciation, depletion and amortization | **405.2** | 402.4 | 346.3 | 282.7 | 244.9 |
| Asset retirement obligation expense | **40.1** | 48.2 | 23.7 | 14.2 | 19.9 |
| Interest expense, net | **193.1** | 217.0 | 228.8 | 127.8 | 88.9 |
| Adjusted EBITDA | **$1,290.1** | $1,846.9 | $ 969.7 | $ 909.7 | $ 696.4 |

## Management's Discussion and Analysis of Financial Condition and Results of Operations

### OVERVIEW

We are the world's largest private sector coal company, with majority interests in 28 coal mining operations in the United States (U.S.) and Australia. In 2009, we produced 210.0 million tons of coal and sold 243.6 million tons of coal. For 2009, our U.S. sales represented 19% of U.S. coal consumption and were approximately 50% greater than the sales of our closest U.S. competitor.

We conduct business through four principal segments: Western U.S. Mining, Midwestern U.S. Mining, Australian Mining, and Trading and Brokerage. The principal business of the Western and Midwestern U.S. Mining segments is the mining, preparation and sale of thermal coal, sold primarily to electric utilities. Our Western U.S. Mining operations consist of our Powder River Basin, Southwest and Colorado operations. Our Midwestern U.S. Mining operations consist of our Illinois and Indiana operations. The business of our Australian Mining Segment is the mining of various qualities of low-sulfur, high Btu coal (metallurgical coal) as well as thermal coal primarily sold to an international customer base with a portion sold to Australian steel producers and power generators. Metallurgical coal is produced primarily from five of our Australian mines. In 2009, metallurgical coal was approximately 3% of our total sales volume, but represented a larger share of our revenue, approximately 23%.

We typically sell coal to utility customers under long-term contracts (those with terms longer than one year). During 2009, approximately 93% of our worldwide sales (by volume) were under long-term contracts. For the year ended December 31, 2009, 81% of our total sales (by volume) were to U.S. electricity generators, 17% were to customers outside the U.S. and 2% were to the U.S. industrial sector.

Our Trading and Brokerage segment's principal business is the brokering of coal sales of other producers both as principal and agent, and the trading of coal, freight and freight-related contracts. We also provide transportation-related services in support of our coal trading strategy, as well as hedging activities in support of our mining operations.

Our fifth segment, Corporate and Other, includes mining and export/transportation joint ventures, energy-related commercial activities, as well as the management of our vast coal reserve and real estate holdings.

We continue to pursue development of coal-fueled generating and Btu Conversion projects in areas of the U.S. where electricity demand is strong and where there is access to land, water, transmission lines and low-cost coal. Coal-fueled generating projects may involve mine-mouth generating plants using our surface lands and coal reserves. Our ultimate role in these projects could take numerous forms, including, but not limited to, equity partner, contract miner or coal sales. Currently, we own 5.06% of the 1,600-megawatt Prairie State Energy Campus (Prairie State) that is under construction in Washington County, Illinois.

We are determining how to best participate in Btu Conversion technologies to economically convert our coal resources to natural gas and transportation fuels through the Kentucky NewGas and GreatPoint Energy projects in the U.S. We are also advancing the development of clean coal technologies, including carbon capture and sequestration, through a number of initiatives that include the FutureGen Alliance and university research programs in the U.S., GreenGen in China and COAL21 Fund in Australia.

As discussed more fully in Item 1A. Risk Factors, our results of operations in the near term could be negatively impacted by the rate of the economic recovery, adverse weather conditions, unforeseen geologic conditions or equipment problems at mining locations and by the availability of transportation for coal shipments. On a long-term basis, our results of operations could be impacted by our ability to secure or acquire high-quality coal reserves, find replacement buyers for coal under contracts with comparable terms to existing contracts, or the passage of new or expanded regulations that could limit our ability to mine, increase our mining costs, or limit our customers' ability to utilize coal as fuel for electricity generation. In the past, we have achieved production levels that are relatively consistent with our projections. We may adjust our production levels further in response to changes in market demand.

## YEAR ENDED DECEMBER 31, 2009 COMPARED TO YEAR ENDED DECEMBER 31, 2008

### *Summary*

Our overall results for 2009 compared to 2008 reflect the unfavorable impact of lower global demand for coal as a result of the global economic recession. Despite the recession, our 2009 Adjusted EBITDA was the second highest in our 126-year history and second only to our 2008 Adjusted EBITDA. We also ended 2009 with total available liquidity of $2.5 billion. We continue to focus on strong cost control and productivity improvements, increased contributions from our high-margin operations and exercising tight capital discipline.

Our 2009 tons sold were below prior year levels reflecting planned production reductions in the Powder River Basin to match lower demand, partially offset by increased volumes associated with the full-year operation of our El Segundo Mine in the Southwest. In the U.S., the decreased demand from lower industrial output, lower natural gas prices that resulted in higher fuel switching, and higher coal stockpiles in the U.S. led to an 8.5 million ton decline in sales volume. In Australia, lower demand from steel customers resulted in a 1.3 million ton decline in metallurgical coal volume, although volumes in the second half of 2009 began to increase on an improved economic outlook led by demand from Asian-Pacific markets.

Our 2009 revenues declined compared to 2008 and were primarily impacted by Australia's lower annual export contract pricing that commenced on April 1, 2009 as compared to 2008's record pricing and the overall decline in volume. Lower revenues were also driven by the decline in Trading and Brokerage revenues that resulted from lower coal pricing volatility. The lower Australian and Trading and Brokerage revenues were partially offset by an increase in U.S. revenues per ton that reflect multi-year contracts signed at higher prices in recent years.

While our Segment Adjusted EBITDA reflects the lower revenue discussed above, our 2009 margins also reflect the impact of producing at reduced levels as well as higher sales related costs. In addition, our costs in Australia were higher due to two additional longwall moves compared to 2008 and the impact of mining in difficult geologic conditions that also included higher costs for overburden removal.

Net income declined in 2009 compared to 2008 reflecting the above items, as well as lower results from equity affiliates and decreased net gains on disposals of assets. Income from continuing operations, net of income taxes was $457.9 million in 2009, or $1.64 per diluted share, 53.6% below 2008 income from continuing operations, net of income taxes of $987.9 million, or $3.60 per diluted share.

### *Tons Sold*

The following table presents tons sold by operating segment for the years ended December 31, 2009 and 2008:

| *(Tons in millions)* | ***2009*** | *2008* | *Increase (Decrease) Tons* | *%* |
|---|---|---|---|---|
| Western U.S. Mining | **160.1** | 169.7 | (9.6) | (5.7%) |
| Midwestern U.S. Mining | **31.8** | 30.7 | 1.1 | 3.6% |
| Australian Mining | **22.3** | 23.4 | (1.1) | (4.7%) |
| Trading and Brokerage | **29.4** | 31.2 | (1.8) | (5.8%) |
| Total tons sold | **243.6** | 255.0 | (11.4) | (4.5%) |

### *Revenues*

The following table presents revenues for the years ended December 31, 2009 and 2008:

| *(Dollars in millions)* | ***2009*** | *2008* | *Increase (Decrease) to Revenues $* | *%* |
|---|---|---|---|---|
| Western U.S. Mining | **$2,612.6** | $2,533.1 | $ 79.5 | 3.1% |
| Midwestern U.S. Mining | **1,303.8** | 1,154.6 | 149.2 | 12.9% |
| Australian Mining | **1,678.0** | 2,242.8 | (564.8) | (25.2%) |
| Trading and Brokerage | **391.0** | 601.8 | (210.8) | (35.0%) |
| Other | **27.0** | 28.7 | (1.7) | (5.9%) |
| Total revenues | **$6,012.4** | $6,561.0 | $(548.6) | (8.4%) |

2009 revenues were below prior year driven by decreases in our Australian Mining and Trading and Brokerage segments as discussed below:

- Australian Mining operations' average sales price decreased 21.4% from the prior year reflecting the lower annual export contract pricing that commenced April 1, 2009 compared to the record pricing realized in 2008. The price decreases were combined with volume decreases from the prior year (4.7%) due to overall lower demand experienced in the first half of 2009. 2009 metallurgical coal shipments of 6.9 million tons were 1.3 million tons below prior year. In the second half of 2009, 5.0 million tons of metallurgical coal were shipped, reflecting a partial recovery from the lower metallurgical coal shipments that occurred in the first half of the year.
- Trading and Brokerage revenues decreased from the prior year primarily due to lower coal pricing volatility in 2009 resulting in lower margins on trading transactions, partially offset by profit from business contracted in 2008 that was realized in 2009 on an international brokerage arrangement.

These decreases to revenues were partially offset by revenue increases in our Midwestern U.S. and Western U.S. Mining segments as discussed below:

- Midwestern U.S. Mining operations' average sales price increased over the prior year (9.3%) driven by the benefit of higher Illinois Basin prices and increased shipments, including purchased coal used to satisfy certain coal supply agreements.
- Western U.S. Mining operations' average sales price increased over the prior year (9.2%) due to a combination of higher contract pricing and a shift in sales mix. Revenues were also higher due to increased shipments from our El Segundo Mine (commissioned in June 2008) and customer contract termination and restructuring agreements. These increases were partially offset by the prior year revenue recovery on a long-term coal supply agreement ($56.9 million) and an overall volume decrease (5.7%) reflecting our planned Powder River Basin production decreases to match demand.

### *Segment Adjusted EBITDA*

The following table presents segment Adjusted EBITDA for the years ended December 31, 2009 and 2008:

| *(Dollars in millions)* | ***2009*** | *2008* | *Increase (Decrease) to Segment Adjusted EBITDA $* | *%* |
|---|---|---|---|---|
| Western U.S. Mining | **$ 721.5** | $ 681.3 | $ 40.2 | 5.9% |
| Midwestern U.S. Mining | **281.9** | 177.3 | 104.6 | 59.0% |
| Australian Mining | **437.8** | 1,016.6 | (578.8) | (56.9%) |
| Trading and Brokerage | **193.4** | 218.9 | (25.5) | (11.6%) |
| Total Segment Adjusted EBITDA | **$1,634.6** | $2,094.1 | $(459.5) | (21.9%) |

Australian Mining operations' Adjusted EBITDA decreased compared to the prior year due to lower annual export contract pricing and lower sales volume due to reduced demand ($416.0 million) as discussed above. Also impacting the segment's Adjusted EBITDA was higher production costs ($170.7 million) driven by increased overburden stripping ratios and decreased longwall mine performance, which included higher costs associated with two additional longwall moves in 2009 compared to 2008.

Trading and Brokerage Adjusted EBITDA decreased compared to prior year primarily due to lower net revenue discussed above.

Western U.S. Mining operations' Adjusted EBITDA increased over the prior year driven by higher pricing ($205.5 million), partially offset by lower demand ($63.2 million), a prior year revenue recovery on a long-term coal supply agreement ($56.9 million), higher sales related costs ($52.0 million) and lower productivity due to increased stripping ratios ($20.8 million). The impact of lower demand was partially mitigated by revenues from customer contract termination and restructuring agreements ($27.8 million).

Midwestern U.S. Mining operations' Adjusted EBITDA increased over the prior year primarily due to higher pricing ($110.7 million) and decreased commodity costs ($16.0 million), partially offset by higher costs associated with mining in more difficult geological conditions compared to the prior year ($20.7 million).

### *Income From Continuing Operations Before Income Taxes*

The following table presents income from continuing operations before income taxes for the years ended December 31, 2009 and 2008:

| (Dollars in millions) | 2009 | 2008 | Increase (Decrease) to Income $ | % |
|---|---|---|---|---|
| Total Segment Adjusted EBITDA | **$1,634.6** | $2,094.1 | $(459.5) | (21.9%) |
| Corporate and Other Adjusted EBITDA | **(344.5)** | (247.2) | (97.3) | (39.4%) |
| Depreciation, depletion and amortization | **(405.2)** | (402.4) | (2.8) | (0.7%) |
| Asset retirement obligation expense | **(40.1)** | (48.2) | 8.1 | 16.8% |
| Interest expense | **(201.2)** | (227.0) | 25.8 | 11.4% |
| Interest income | **8.1** | 10.0 | (1.9) | (19.0%) |
| Income from continuing operations before income taxes | **$ 651.7** | $1,179.3 | $(527.6) | (44.7%) |

Income from continuing operations before income taxes decreased from prior year primarily due to the lower Total Segment Adjusted EBITDA discussed above and lower Corporate and Other Adjusted EBITDA, partially offset by lower interest expense and asset retirement obligation expense.

The decrease of $97.3 million in Corporate and Other Adjusted EBITDA during 2009 compared to 2008 was due to the following:

- Lower results from equity affiliates ($69.1 million) primarily from our joint venture interest in Carbones del Guasare (owner and operator of the Paso Diablo Mine in Venezuela). Carbones del Guasare incurred unfavorable results in 2009 compared to 2008 (our share of which was $25.6 million) due to lower productivity, higher operating costs and ongoing labor issues; in addition, we recognized a $34.7 million impairment loss on this investment. See Note 1 to our consolidated financial statements for additional information concerning this joint venture interest.
- Lower net gains on disposal or exchange of assets ($49.7 million) was due primarily to a $54.0 million gain in the prior year from the sale of non-strategic coal reserves and surface lands located in Kentucky.
- The above decreases to Corporate and Other Adjusted EBITDA were offset by lower costs associated with Btu Conversion activities ($16.9 million).

Interest expense was lower than prior year due to lower variable interest rates on our Term Loan Facility and accounts receivable securitization program and lower average borrowings on our Revolving Credit Facility.

Asset retirement obligation expense decreased in 2009 as compared to the prior year due primarily to a decrease in the ongoing and closed mine reclamation rates reflecting lower fuel and re-vegetation costs incurred in our Midwestern U.S. Mining segment.

### *Net Income Attributable to Common Stockholders*

The following table presents net income attributable to common stockholders for the years ended December 31, 2009 and 2008:

| (Dollars in millions) | 2009 | 2008 | Increase (Decrease) to Income $ | % |
|---|---|---|---|---|
| Income from continuing operations before income taxes | **$ 651.7** | $1,179.3 | $(527.6) | (44.7%) |
| Income tax provision | **(193.8)** | (191.4) | (2.4) | (1.3%) |
| Income from continuing operations, net of income taxes | **457.9** | 987.9 | (530.0) | (53.6%) |
| Income (loss) from discontinued operations, net of income taxes | **5.1** | (28.8) | 33.9 | 117.7% |
| Net income | **463.0** | 959.1 | (496.1) | (51.7%) |
| Net income attributable to noncontrolling interests | **(14.8)** | (6.2) | (8.6) | (138.7%) |
| Net income attributable to common stockholders | **$ 448.2** | $ 952.9 | $(504.7) | (53.0%) |

Net income attributable to common stockholders decreased in 2009 compared to the prior year due to the decrease in income from continuing operations before incomes taxes discussed above.

Income tax provision was impacted by the following:

- Increased expense associated with the remeasurement of non-U.S. tax accounts as a result of the strengthening Australian dollar against the U.S. dollar ($139.6 million; exchange rate rose 29% in 2009 compared to a 21% decrease in 2008, as illustrated below); and

| | December 31, 2009 | 2008 | 2007 | Rate Change 2009 | 2008 |
|---|---|---|---|---|---|
| Australian dollar to U.S. dollar exchange rate | **$0.8969** | $0.6928 | $0.8816 | **$0.2041** | ($0.1888) |

- The prior year release of a foreign valuation allowance related to our Australian net operating loss carry forwards ($45.3 million) as a result of significantly higher earnings resulting from the higher contract pricing that was secured during 2008.
- The above increases to income tax expense were partially offset by lower pre-tax earnings in 2009, which drove a decrease to the income tax provision ($184.6 million).

Income from discontinued operations increased compared to the prior year as the prior year included operating losses, net of a $26.2 million gain on the sale of our Baralaba Mine, and an $11.7 million write-off of a coal excise tax receivable in the first quarter of 2008. In late 2008, legislation was passed which contained provisions that allowed for the refund of coal excise tax collected on certain coal shipments. In 2009, we received a coal excise tax refund resulting in approximately $35 million, net of income taxes, recorded in "Income (loss) from discontinued operations, net of income taxes" (see Note 2 to the consolidated financial statements for more information related to the excise tax refund). Partially offsetting the 2009 excise tax refund were operating losses associated with discontinued operations and assets held for sale ($20.6 million) and a $10.0 million loss on the sale of our Chain Valley Mine in Australia.

## YEAR ENDED DECEMBER 31, 2008 COMPARED TO YEAR ENDED DECEMBER 31, 2007

### *Summary*

Higher average sales prices and volumes across all operating regions, particularly in Australia, contributed to an increase in revenues in 2008 compared to 2007. Segment Adjusted EBITDA rose primarily on the higher pricing mentioned above and favorable results from Trading and Brokerage. Increases in sales prices and volumes were partially offset by higher commodity, material, supply, sales-related and labor costs in all operating regions. Income from continuing operations, net of income taxes was $987.9 million in 2008, or $3.60 per diluted share, 123.7% above 2007 income from continuing operations, net of income taxes of $441.6 million, or $1.64 per diluted share.

### *Tons Sold*

The following table presents tons sold by operating segment for the years ended December 31, 2008 and 2007:

| (Tons in millions) | 2008 | 2007 | Increase Tons | % |
|---|---|---|---|---|
| Western U.S. Mining | 169.7 | 161.4 | 8.3 | 5.1% |
| Midwestern U.S. Mining | 30.7 | 29.6 | 1.1 | 3.7% |
| Australian Mining | 23.4 | 20.4 | 3.0 | 14.7% |
| Trading and Brokerage | 31.2 | 24.1 | 7.1 | 29.5% |
| Total tons sold | 255.0 | 235.5 | 19.5 | 8.3% |

### *Revenues*

The following table presents revenues for the years ended December 31, 2008 and 2007:

| (Dollars in millions) | 2008 | 2007 | Increase (Decrease) to Revenues $ | % |
|---|---|---|---|---|
| Western U.S. Mining | $2,533.1 | $2,063.2 | $ 469.9 | 22.8% |
| Midwestern U.S. Mining | 1,154.6 | 987.1 | 167.5 | 17.0% |
| Australian Mining | 2,242.8 | 1,117.6 | 1,125.2 | 100.7% |
| Trading and Brokerage | 601.8 | 320.7 | 281.1 | 87.7% |
| Other | 28.7 | 35.2 | (6.5) | (18.5%) |
| Total revenues | $6,561.0 | $4,523.8 | $2,037.2 | 45.0% |

Total revenues increased in 2008 compared to the prior year across all operating segments. The primary drivers of the increases included the following:

- An increase in average sales price at our Australian Mining operations (75.0%), primarily driven by the strength of metallurgical coal prices on our Australian contracts that reprice annually in the second quarter of each year.
- U.S. Mining operations' average sales price increased over the prior year (15.2%) driven by the benefit of higher priced coal supply agreements signed in recent years.
- Australia's volumes increased over the prior year (14.7%) from strong demand during the first three quarters of 2008 and additional production from recently completed mines. Year-over-year increases were partially offset by heavy rainfall and flooding in Queensland during the first quarter of 2008 and customer shipment deferrals in the fourth quarter of 2008 due to the global economic slowdown.
- Increased demand also led to higher volumes across our U.S. operating segments, which overcame slightly lower volumes at some of our Midwestern U.S. Mining surface operations due to poor weather in that operating region that impacted production during the first and second quarters. The volume increase of 5.1% at our Western U.S. Mining operations resulted from greater throughput from capital improvements and contributions from our new El Segundo Mine, partially offset by the flooding in the midwestern U.S. that impacted railroad shipping performance related to western U.S. production during the second quarter of 2008.
- Trading and Brokerage revenues increased over the prior year due to increased trading positions allowing us to capture market movements derived from the volatility of both domestic and international coal markets.
- Also impacting year-over-year revenues in our Western U.S. Mining operations was an agreement to recover previously recognized postretirement healthcare and reclamation costs of $56.9 million in the second quarter of 2008.

### *Segment Adjusted EBITDA*

The following table presents segment Adjusted EBITDA for the years ended December 31, 2008 and 2007:

| (Dollars in millions) | 2008 | 2007 | Increase (Decrease) to Segment Adjusted EBITDA $ | % |
|---|---|---|---|---|
| Western U.S. Mining | $ 681.3 | $ 595.4 | $ 85.9 | 14.4% |
| Midwestern U.S. Mining | 177.3 | 200.0 | (22.7) | (11.4%) |
| Australian Mining | 1,016.6 | 167.2 | 849.4 | 508.0% |
| Trading and Brokerage | 218.9 | 116.6 | 102.3 | 87.7% |
| Total Segment Adjusted EBITDA | $2,094.1 | $1,079.2 | $1,014.9 | 94.0% |

Adjusted EBITDA from our Western U.S. Mining operations increased in 2008 over the prior year primarily driven by an overall increase in average sales prices per ton across the region ($2.10) and higher volumes in the region due to increased demand and greater throughput as a result of capital improvements. Also contributing to the increase was the recovery of postretirement healthcare and reclamation costs discussed above. Partially offsetting the pricing and volume contributions were higher per ton costs ($1.78). The cost increases were primarily due to higher sales related costs, higher material, supply and labor costs, higher repair and maintenance costs in the Powder River Basin and increased commodity costs, net of hedging activities, driven by higher average fuel and explosives pricing.

Midwestern U.S. Mining operations' Adjusted EBITDA decreased in 2008 as increases in average sales price per ton ($4.22) were offset by cost increases resulting from higher costs for commodities, net of hedging activities, driven by higher average fuel and explosives prices, as well as higher material, supply and labor costs. Heavy rains and flooding in the midwestern U.S. affected sales volume at some of our mines, particularly in the first half of the year. Also affecting the Midwestern U.S. Mining segment was the decrease in revenues from coal sold to synthetic fuel plants in the prior year ($28.9 million) due to the producers exiting the synthetic fuel market after expiration of federal tax credits at the end of 2007.

Our Australian Mining operations' Adjusted EBITDA increased in 2008 primarily due to higher pricing negotiated in the second quarter of 2008 ($41.06 per ton), higher overall volumes as a result of strong export demand and contributions from our recently completed mines and lower demurrage costs. These favorable impacts were partially offset by higher fuel costs, an increase in labor and overburden removal expenses and higher contractor costs (five of ten Australian mines are managed utilizing contract miners).

Trading and Brokerage Adjusted EBITDA increased in 2008 over the prior year due to increased trading volumes and higher coal price volatility.

### *Income From Continuing Operations Before Income Taxes*

The following table presents income from continuing operations before income taxes for the years ended December 31, 2008 and 2007:

| (Dollars in millions) | 2008 | 2007 | Increase (Decrease) to Income $ | % |
|---|---|---|---|---|
| Total Segment Adjusted EBITDA | $2,094.1 | $1,079.2 | $1,014.9 | 94.0% |
| Corporate and Other Adjusted EBITDA | (247.2) | (109.5) | (137.7) | (125.8%) |
| Depreciation, depletion and amortization | (402.4) | (346.3) | (56.1) | (16.2%) |
| Asset retirement obligation expense | (48.2) | (23.7) | (24.5) | (103.4%) |
| Interest expense | (227.0) | (235.8) | 8.8 | 3.7% |
| Interest income | 10.0 | 7.0 | 3.0 | 42.9% |
| Income from continuing operations before income taxes | $1,179.3 | $ 370.9 | $ 808.4 | 218.0% |

Income from continuing operations before income taxes increased over the prior year primarily due to the higher Total Segment Adjusted EBITDA discussed above, partially offset by lower Corporate and Other Adjusted EBITDA, higher depreciation, depletion and amortization, and higher asset retirement obligation expense.

The decrease in Corporate and Other Adjusted EBITDA during 2008 compared to 2007 was due to the following:

- Higher selling and administrative expenses ($54.7 million) primarily driven by an increase in performance-based incentive costs and legal expenses;
- Cost reimbursement and partner fees received in the prior year for the Prairie State project, primarily related to the entrance of new project partners ($29.5 million);
- Lower net gains on disposals or exchanges of assets ($15.7 million). 2008 activity included a gain of $54.0 million on the sale of approximately 58 million tons of non-strategic coal reserves and surface lands located in Kentucky. 2007 activity included a gain of $50.5 million on the exchange of oil and gas rights and assets in more than 860,000 acres in the Illinois Basin, West Virginia, New Mexico and the Powder River Basin for coal reserves in West Virginia and Kentucky and cash proceeds. The prior year also included a gain of $26.4 million on the sale of approximately 172 million tons of coal reserves and surface lands to the Prairie State equity partners; and
- Lower equity income ($15.5 million) from our joint venture interest in Carbones del Guasare (owner and operator of the Paso Diablo Mine in Venezuela) and higher costs associated with Btu Conversion activities of $14.3 million in 2008.

Depreciation, depletion and amortization was higher in 2008 compared to the prior year because of increased depletion across our operating platform resulting from the volume increases and the impact of mining higher value coal reserves. In addition, depreciation and depletion increases resulted from our recently completed Australian mines and depletion at our El Segundo Mine.

Asset retirement obligation expense increased in 2008 as compared to the prior year due to an increase in the ongoing and closed mine reclamation rates that reflect higher fuel, labor and re-vegetation costs, as well as an overall increase in the number of acres disturbed. The addition of the El Segundo Mine, which was completed in June 2008, also contributed to higher asset retirement obligation expense.

### *Net Income Attributable to Common Stockholders*

The following table presents net income attributable to common stockholders for the years ended December 31, 2008 and 2007:

| *(Dollars in millions)* | 2008 | 2007 | Increase (Decrease) to Income $ | % |
|---|---|---|---|---|
| Income from continuing operations before income taxes | $1,179.3 | $ 370.9 | $ 808.4 | 218.0% |
| Income tax (provision) benefit | (191.4) | 70.7 | (262.1) | (370.7%) |
| Income from continuing operations, net of income taxes | 987.9 | 441.6 | 546.3 | 123.7% |
| Loss from discontinued operations, net of income taxes | (28.8) | (180.1) | 151.3 | 84.0% |
| Net income | 959.1 | 261.5 | 697.6 | 266.8% |
| Net (income) loss attributable to noncontrolling interests | (6.2) | 2.3 | (8.5) | (369.6%) |
| Net income attributable to common stockholders | $ 952.9 | $ 263.8 | $ 689.1 | 261.2% |

Net income attributable to common stockholders increased in 2008 compared to the prior year due to the increase in income from continuing operations before incomes taxes discussed above.

Income tax provision was impacted by the following:

- Increased expense in 2008 due to higher pre-tax earnings ($282.9 million); and
- Valuation allowance release against federal net operating loss credits recognized into income in 2007 ($197.8 million); partially offset by
- Income tax benefit associated with the remeasurement of non-U.S. tax accounts as a result of the weakening Australian dollar against the U.S. dollar in 2008 ($121.2 million; exchange rate fell 21% in 2008 compared to an 11% increase in 2007, as illustrated below); and

| | December 31, 2008 | 2007 | 2006 | Rate Change 2008 | 2007 |
|---|---|---|---|---|---|
| Australian dollar to U.S. dollar exchange rate | $0.6928 | $0.8816 | $0.7913 | ($0.1888) | $0.0903 |

- The favorable rate difference resulting from higher foreign generated income in 2008 ($106.2 million); and
- The release of a foreign valuation allowance against a portion of our Australian net operating loss carryforwards in 2008 ($45.3 million) as a result of significantly higher earnings resulting from the higher contract pricing that was secured during 2008.

Net income for 2008 was also impacted by a lower loss from discontinued operations as compared to the prior year due primarily to losses incurred for Patriot Coal Corporation (Patriot) operations in 2007. The loss from discontinued operations for 2008 related to operating losses, net of a $26.2 million gain on the sale of our Baralaba Mine, and an $11.7 million write-off of an excise tax refund receivable (net of tax) as a result of an April 2008 U.S. Supreme Court ruling (see Note 2 to the consolidated financial statements).

## OUTLOOK

### *Near-Term Outlook*

Global economies are showing signs of improvement, with 2010 economic forecasts estimating a 2.6 to 4.0% expansion – although slower than expected economic improvement could temper these estimates. The Asia-Pacific markets are expected to continue to outpace the U.S. and European markets in economic growth and therefore electricity generation and steel production. For 2009, China and India were the only steel producing 'majors' to outpace prior-year levels, with all other nations 23% lower on average. For 2010, the World Steel Association estimates global steel production will increase 9 percent over 2009. Globally, 72 gigawatts of new coal-fueled generation are under construction and expected to come on line during 2010, more than 70% of which are new units in China and India. New global coal-fueled generation for 2010 is estimated to require approximately 300 million tons of new annual coal demand.

In the U.S., higher coal use caused by colder winter weather lowered utility stockpiles an estimated 25 to 30 million tons between December 2009 and mid-January 2010. As of February 15, 2010, utility stockpiles were approximately 150 to 155 million tons, 24% above the 10-year average and 6% above the year-ago level. We believe U.S. coal demand could rise 60 to 80 million tons based on economic growth, increasing industrial production and an expected reduction of coal-to-gas switching due to rising natural gas prices. Conversely, the Energy Information Administration (EIA) estimates coal production will be 43 million tons lower in 2010, in part due to production declines initiated in 2009. With rising demand and lower production, utility coal inventories are likely to be reduced.

As of January 26, 2010, we are targeting full-year 2010 production of approximately 185 to 195 million tons in the U.S. and 26 to 28 million tons in Australia. Total 2010 sales are expected to be in a range of 240 to 260 million tons. We may continue to adjust our production levels in response to changes in market demand.

We are fully contracted for 2010 at planned production levels in the U.S. As of January 26, 2010 we had 4.5 to 5.5 million tons of Australian metallurgical coal unpriced for 2010, along with 6.5 to 7.0 million tons of unpriced export thermal coal. Unpriced 2010 volumes are primarily planned for deliveries over the last three quarters of 2010.

We continue to manage costs and operating performance to mitigate external cost pressures, geologic conditions and potential shipping delays resulting from adverse port and rail performance. To mitigate the external cost pressures, we have an ongoing company-wide initiative to instill best practices at all operations. We may have higher per ton costs as a result of below-optimal production levels due to market-driven changes in demand. We may also encounter poor geologic conditions, lower third-party contract miner or brokerage performance or unforeseen equipment problems that limit our ability to produce at forecasted levels. To the extent upward pressure on costs exceeds our ability to realize sales increases, or if we experience unanticipated operating or transportation difficulties, our operating margins would be negatively impacted. See Cautionary Notice Regarding Forward-Looking Statements and Item 1A. of this report for additional considerations regarding our outlook.

We rely on ongoing access to the worldwide financial markets for capital, insurance, hedging and investments through a wide variety of financial instruments and contracts. To the extent these markets are not available or increase significantly in cost, this could have a negative impact on our ability to meet our business goals. Similarly, many of our customers and suppliers rely on the availability of the financial markets to secure the necessary financing and financial surety (letters of credit, performance bonds, etc.) to complete transactions with us. To the extent customers and suppliers are not able to secure this financial support, it could have a negative impact on our results of operations and/or counterparty credit exposure.

### *Long-Term Outlook*

Our long-term global outlook remains positive. Coal has been the fastest-growing fuel in the world for each of the past six years, with consumption growing nearly twice as fast as total energy use.

The International Energy Agency's (IEA) World Energy Outlook estimates world primary energy demand will grow 40% between 2007 and 2030, with demand for coal rising 53%. China and India alone account for more than half of the expected incremental energy demand.

Coal is expected to retain its strong presence as a fuel for the power sector worldwide, with its share of the power generation mix projected to rise to 44% in 2030. Currently, 217 gigawatts of coal-fueled electricity generating plants are under construction around the world, representing more than 800 million tons of annual coal demand expected to come online in the next several years. In the U.S., 16 gigawatts of new coal-based generating capacity have been completed in 2009 or are under construction, representing approximately 65 million tons of annual coal demand when they come online over the next three to five years as expected.

We believe that Btu Conversion applications such as coal-to-gas (CTG) and coal-to-liquids (CTL) plants represent an avenue for potential long-term industry growth. The EIA continues to project an increase in demand for unconventional sources of transportation fuel such as CTL, which is estimated to add nearly 70 million tons of annual U.S. coal demand by 2035. In addition, China and India are developing CTG and CTL facilities.

The IEA projects natural gas demand will grow 1.5% per year to just under 4,310 billion cubic meters in 2030. The biggest increase in absolute terms occurs in the Middle East, which holds the majority of the world's proven reserves, and non-OECD Asia. North America and Eastern Europe/Eurasia are expected to remain the leading gas consumers in 2030, even though their demand is expected to rise less in percentage terms than almost anywhere else globally. Globally, the share of renewables is projected to rise four percentage points to 22% between 2007 and 2030, with most of the growth coming from non-hydro sources. Nuclear power is expected to grow in all major regions with the exception of Europe, but its share in total generation is expected to fall between 2007 and 2030.

We continue to support clean coal technology development and other initiatives addressing global climate change through our participation in a number of projects in the U.S., China and Australia. In addition, clean coal technology development in the U.S. is being accelerated by funding under the American Recovery and Reinvestment Act of 2009 and by the formation of an Interagency Task Force on Carbon Capture and Storage to develop a comprehensive and coordinated federal strategy to speed the commercial development of clean coal technologies.

Enactment of laws or passage of regulations regarding emissions from the combustion of coal by the U.S. or some of its states or by other countries, or other actions to limit such emissions, could result in electricity generators switching from coal to other fuel sources. The potential financial impact on us of future laws or regulations will depend upon the degree to which any such laws or regulations forces electricity generators to diminish their reliance on coal as a fuel source. That, in turn, will depend on a number of factors, including the specific requirements imposed by any such laws or regulations, the time periods over which those laws or regulations would be phased in and the state of commercial development and deployment of carbon capture and storage technologies. In view of the significant uncertainty surrounding each of these factors, it is not possible for us to reasonably predict the impact that any such laws or regulations may have on our results of operations, financial condition or cash flows.

## LIQUIDITY AND CAPITAL RESOURCES

Our primary sources of cash include sales of our coal production to customers, cash generated from our trading and brokerage activities, sales of non-core assets and financing transactions, including the sale of our accounts receivable (through our securitization program). Our primary uses of cash include our cash costs of coal production, capital expenditures, federal coal lease payments, interest costs and costs related to past mining obligations as well as acquisitions. Our ability to pay dividends, service our debt (interest and principal) and acquire new productive assets or businesses is dependent upon our ability to continue to generate cash from the primary sources noted above in excess of the primary uses. Future dividends and share repurchases, among other restricted items, are subject to limitations imposed in the covenants of our 5.875% and 6.875% Senior Notes and Convertible Junior Subordinated Debentures (the Debentures). We generally fund all of our capital expenditure requirements with cash generated from operations.

We believe our available borrowing capacity and operating cash flows will be sufficient in the near term. As of December 31, 2009, we had cash and cash equivalents of $988.8 million and $1.5 billion of available borrowing capacity under our Senior Unsecured Credit Facility, net of outstanding letters of credit. The Senior Unsecured Credit Facility matures on September 15, 2011.

The Pension Protection Act of 2006 (the Pension Protection Act), which was effective January 1, 2008, increased the long-term funding targets for single employer pension plans from 90% to 100%. "At risk" plans, as defined by the Pension Protection Act, are restricted from making full lump sum payments and from increasing benefits unless they are funded immediately, and also requires that the plan give participants notice regarding the at-risk status of the plan. If a plan falls below 60%, lump sum payments are prohibited and participant benefit accruals cease. As of December 31, 2009, our pension plans were approximately 77% funded, before considering planned 2010 contributions. Our minimum funding requirement for 2010 is approximately $3 million, and the qualified plans would not be considered at-risk. Using current assumptions, our 2011 minimum funding requirement would be approximately $98 million.

We also have a share repurchase program that has an available capacity of $700.4 million at December 31, 2009. While no repurchases were made in 2009 under the program, repurchases may be made from time to time based on an evaluation of our outlook and general business conditions, as well as alternative investment and debt repayment options. The repurchase program does not have an expiration date and may be discontinued at any time.

Net cash provided by operating activities from continuing operations for 2009 decreased $356.3 million compared to the prior year primarily due to the decline in operating cash flows generated from our Australian mining operations on lower volumes and lower average pricing and the timing of cash flows from our working capital, primarily driven by foreign income tax payments related to prior year earnings.

The decrease in cash used in discontinued operations of $117.4 million was primarily due to approximately $59 million of cash received related to coal excise tax refunds in 2009 (see Note 2 to the consolidated financial statements for more information related to the excise tax refund) and lower current year payments related to Patriot discontinued operations.

Net cash used in investing activities from continuing operations decreased $11.1 million in 2009 compared to the prior year. The decrease primarily reflects lower federal coal lease expenditures of $54.9 million in 2009, partially offset by higher spending for our share of the Prairie State construction costs and additional investments in equity affiliates and joint venture projects in the prior year. Capital expenditures in 2009 were consistent with prior year as current year spending related to the development of our Bear Run Mine was offset by prior year spending related to the completion of our El Segundo Mine and expenditures for our blending and loadout facility at our North Antelope Rochelle Mine in the Western U.S.

Net cash used in financing activities decreased $384.7 million, primarily due to 2008 payments related to the repurchase of common stock ($199.8 million), the acquisition of noncontrolling interests relating to our Millennium Mine ($110.1 million) and payments on our revolving line of credit ($97.7 million). During 2009, we purchased $10.0 million face value of our 6.84% Series A bonds and $10.0 million face value of our 6.84% Series C bonds for a combined total of $19.0 million.

Our total indebtedness as of December 31, 2009 and 2008 consisted of the following:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Term Loan under Senior Unsecured Credit Facility | **$ 490.3** | $ 490.3 |
| Convertible Junior Subordinated Debentures due December 2066 | **371.5** | 369.9 |
| 7.375% Senior Notes due November 2016 | **650.0** | 650.0 |
| 6.875% Senior Notes due March 2013 | **650.0** | 650.0 |
| 7.875% Senior Notes due November 2026 | **247.1** | 247.0 |
| 5.875% Senior Notes due March 2016 | **218.1** | 218.1 |
| 6.84% Series C Bonds due December 2016 | **33.0** | 43.0 |
| 6.34% Series B Bonds due December 2014 | **15.0** | 18.0 |
| 6.84% Series A Bonds due December 2014 | **–** | 10.0 |
| Capital lease obligations | **67.5** | 81.2 |
| Fair value hedge adjustment | **8.4** | 15.1 |
| Other | **1.4** | 1.0 |
| Total | **$2,752.3** | $2,793.6 |

We were in compliance with all of the covenants of the Senior Unsecured Credit Facility, the 6.875% Senior Notes, the 5.875% Senior Notes, the 7.375% Senior Notes, the 7.875% Senior Notes and the Debentures as of December 31, 2009.

### *Senior Unsecured Credit Facility*

Our Senior Unsecured Credit Facility provides a $1.8 billion Revolving Credit Facility and a $950.0 million Term Loan Facility. The Revolving Credit Facility is intended to accommodate working capital needs, letters of credit, the funding of capital expenditures and other general corporate purposes. The Revolving Credit Facility also includes a $50.0 million sub-facility available for same-day swingline loan borrowings.

Loans under the facility are available in U.S. dollars, with a sub-facility under the Revolving Credit Facility available in Australian dollars, pounds sterling and euros. Letters of credit under the Revolving Credit Facility are available to us in U.S. dollars with a sub-facility available in Australian dollars, pounds sterling and euros. The interest rate payable on the Revolving Credit Facility and the Term Loan Facility is based on a pricing grid tied to our leverage ratio, as defined in the Third Amended and Restated Credit Agreement. At December 31, 2009, the interest rate payable on the Revolving Credit Facility and the Term Loan Facility was LIBOR plus 0.75%, or a total of 1.0%.

We must comply with certain financial covenants on a quarterly basis including a minimum interest coverage ratio and a maximum leverage ratio, as defined in the Third Amended and Restated Credit Agreement. The financial covenants also place limitations on our investments in joint ventures, unrestricted subsidiaries, indebtedness of non-loan parties, and the imposition of liens on our assets. The Senior Unsecured Credit Facility matures on September 15, 2011.

As of December 31, 2009, we had no borrowings and $315.7 million letters of credit outstanding under our Revolving Credit Facility.

### *Other Long-Term Debt*

A description of our other debt instruments is described in Note 12 to the consolidated financial statements.

### *Third-party Security Ratings*

The ratings for our Senior Unsecured Credit Facility and our Senior Unsecured Notes are as follows: Moody's has issued a Ba1 rating, Standard & Poor's a BB+ rating, and Fitch has issued a BB+ rating. The ratings on the Debentures are as follows: Moody's has issued a Ba3 rating, Standard & Poor's a B+ rating, and Fitch has issued a BB- rating. These security ratings reflected the views of the rating agency only. An explanation of the significance of these ratings may be obtained from the rating agency. Such ratings are not a recommendation to buy, sell or hold securities, but rather an indication of creditworthiness. Any rating can be revised upward or downward or withdrawn at any time by a rating agency if it decides that the circumstances warrant the change. Each rating should be evaluated independently of any other rating.

### *Shelf Registration Statement*

On August 7, 2009, we filed an automatic shelf registration statement on Form S-3 as a well-known seasoned issuer with the Securities and Exchange Commission (SEC). The registration was for an indeterminate number of securities and is effective for three years, at which time we expect to be able to file an automatic shelf registration statement that would become immediately effective for another three-year term. Under this universal shelf registration statement, we have the capacity to offer and sell from time to time securities, including common stock, preferred stock, debt securities, warrants and units.

### *Capital Expenditures*

Capital expenditures for 2010 are anticipated to be between $600 million to $650 million. The planned expenditures include sustaining capital at our existing mines, completion of our Bear Run Mine in western Indiana, expansion of our metallurgical and thermal coal export platform in Australia to serve the growth markets in Asia and funding of our Prairie State investment.

## CONTRACTUAL OBLIGATIONS

The following is a summary of our contractual obligations as of December 31, 2009:

| | Payments Due By Year | | | | |
|---|---|---|---|---|---|
| *(Dollars in millions)* | *Total* | *Less Than 1 Year* | *1 - 3 Years* | *3 - 5 Years* | *More Than 5 Years* |
| Long-term debt obligations (principal and interest) | $5,219.5 | $203.4 | $ 884.8 | $ 964.8 | $3,166.5 |
| Capital lease obligations (principal and interest) | 80.3 | 15.1 | 30.2 | 35.0 | – |
| Operating lease obligations | 468.1 | 96.4 | 153.6 | 100.3 | 117.8 |
| Unconditional purchase obligations [1] | 70.4 | 70.4 | – | – | – |
| Coal reserve lease and royalty obligations | 79.9 | 11.3 | 16.8 | 15.0 | 36.8 |
| Take or pay obligations [2] | 1,864.4 | 110.7 | 297.4 | 310.4 | 1,145.9 |
| Other long-term liabilities [3] | 1,485.5 | 151.0 | 300.3 | 292.6 | 741.6 |
| Total contractual cash obligations | $9,268.1 | $658.3 | $1,683.1 | $1,718.1 | $5,208.6 |

*[1] We have purchase agreements with approved vendors for most types of operating expenses. However, our specific open purchase orders (which have not been recognized as a liability) under these purchase agreements, combined with any other open purchase orders, are not material. The commitments in the table above relate to capital purchases.*

*[2] Represents various long- and short-term take or pay arrangements associated with rail and port commitments for the delivery of coal, some of which extend to 2040, including amounts relating to export facilities currently under construction which are expected to be completed in 2010.*

*[3] Represents long-term liabilities relating to our postretirement benefit plans, work-related injuries and illnesses, defined benefit pension plans and mine reclamation and end of mine closure costs.*

As of December 31, 2009, we had $70.4 million of purchase obligations for capital expenditures and $0.9 million of obligations related to federal coal reserve lease payments due over the next five years. The purchase obligations for capital expenditures primarily relate to the replacement and improvement of equipment and facilities at existing mines.

We do not expect any of the $113.2 million of gross unrecognized tax benefits reported in our consolidated financial statements to require cash settlement within the next year. Beyond that, we are unable to make reasonably reliable estimates of periodic cash settlements with respect to such unrecognized tax benefits.

## OFF-BALANCE SHEET ARRANGEMENTS

In the normal course of business, we are a party to certain off-balance sheet arrangements. These arrangements include guarantees, indemnifications, financial instruments with off-balance sheet risk, such as bank letters of credit and performance or surety bonds and our accounts receivable securitization. Assets and liabilities related to these arrangements are not reflected in our consolidated balance sheets, and we do not expect any material adverse effects on our financial condition, results of operations or cash flows to result from these off-balance sheet arrangements.

We use a combination of surety bonds, corporate guarantees (such as self bonds) and letters of credit to secure our financial obligations for reclamation, workers' compensation, and coal lease obligations as follows as of December 31, 2009:

| *(Dollars in millions)* | *Reclamation Obligations* | *Lease Obligations* | *Workers' Compensation Obligations* | *Other [1]* | *Total* |
|---|---|---|---|---|---|
| Self Bonding | $ 821.9 | $ – | $ – | $ – | $ 821.9 |
| Surety Bonds | 772.3 | 116.3 | 8.7 | 57.3 | 954.6 |
| Letters of Credit | 34.9 | – | 43.0 | 237.8 | 315.7 |
| | $1,629.1 | $116.3 | $51.7 | $295.1 | $2,092.2 |

*[1] Other includes the six letter of credit obligations described below and an additional $61.1 million in letters of credit and surety bonds related to collateral for surety companies, road maintenance, performance guarantees and other operations.*

We own a 37.5% interest in Dominion Terminal Associates, a partnership that operates a coal export terminal in Newport News, Virginia under a 30-year lease that permits the partnership to purchase the terminal at the end of the lease term for a nominal amount. The partners have severally (but not jointly) agreed to make payments under various agreements which in the aggregate provide the partnership with sufficient funds to pay rents and to cover the principal and interest payments on the floating-rate industrial revenue bonds issued by the Peninsula Ports Authority, and which are supported by letters of credit from a commercial bank. As of December 31, 2009, our maximum reimbursement obligation to the commercial bank was in turn supported by four letters of credit totaling $42.7 million.

We are party to an agreement with the Pension Benefit Guaranty Corporation (PBGC) and TXU Europe Limited, an affiliate of our former parent corporation, under which we are required to make special contributions to two of our defined benefit pension plans and to maintain a $37.0 million letter of credit in favor of the PBGC. If we or the PBGC give notice of an intent to terminate one or more of the covered pension plans in which liabilities are not fully funded, or if we fail to maintain the letter of credit, the PBGC may draw down on the letter of credit and use the proceeds to satisfy liabilities under the Employee Retirement Income Security Act of 1974, as amended. The PBGC, however, is required to first apply amounts received from a $110.0 million guarantee in place from TXU Europe Limited in favor of the PBGC before it draws on our letter of credit. On November 19, 2002 TXU Europe Limited was placed under the administration process in the United Kingdom (a process similar to bankruptcy proceedings in the U.S.) and continues under this process as of December 31, 2009. As a result of these proceedings, TXU Europe Limited may be liquidated or otherwise reorganized in such a way as to relieve it of its obligations under its guarantee.

At December 31, 2009, we have a $154.3 million letter of credit for collateral for bank guarantees issued with respect to certain reclamation and performance obligations related to some of our Australian mines.

### *Other Guarantees*

See the "Other Guarantees" section of Note 19 to our consolidated financial statements for a description of our other guarantees.

### *Accounts Receivable Securitization Program*

Under our accounts receivable securitization program in place at December 31, 2009, a pool of eligible trade receivables contributed to our wholly-owned, bankruptcy-remote subsidiary were sold, without recourse, to a multi-seller, asset-backed commercial paper conduit (Conduit). Purchases by the Conduit are financed with the sale of highly rated commercial paper. We utilize proceeds from the sale of our accounts receivable as an alternative to other forms of debt, effectively reducing our overall borrowing costs. The funding cost of the securitization program was $4.0 million for the year ended December 31, 2009 and $10.8 million for the year ended December 31, 2008. The securitization program was renewed in May 2009 and amended in December 2009, and extends to May 2012, while the letter of credit commitment that supports the commercial paper facility underlying the securitization program must be renewed annually. The securitization transactions have been recorded as sales, with receivables sold to the Conduit removed from our consolidated balance sheets. The amount of interests in accounts receivable sold to the Conduit was $254.6 million as of December 31, 2009 and $275.0 million as of December 31, 2008 (see Note 6 to our consolidated financial statements for additional information on our accounts receivable securitization program). On January 25, 2010, the receivables purchase agreement for the accounts receivable securitization program was amended and restated to add a second multi-seller asset-backed commercial paper conduit as a purchaser.

## CRITICAL ACCOUNTING POLICIES AND ESTIMATES

Our discussion and analysis of our financial condition, results of operations, liquidity and capital resources is based upon our financial statements, which have been prepared in accordance with U.S. generally accepted accounting principles (GAAP). GAAP requires that we make estimates and judgments that affect the reported amounts of assets, liabilities, revenues and expenses, and related disclosure of contingent assets and liabilities. On an ongoing basis, we evaluate our estimates. We base our estimates on historical experience and on various other assumptions that we believe are reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates.

*Employee-Related Liabilities*

We have long-term liabilities for our employees' postretirement benefit costs and defined benefit pension plans. Detailed information related to these liabilities is included in Notes 14 and 15 to our consolidated financial statements. Liabilities for postretirement benefit costs and workers' compensation obligations are not funded. Our pension obligations are funded in accordance with the provisions of applicable law. Expense for the year ended December 31, 2009 for the pension and postretirement liabilities totaled $76.8 million, while funding payments were $110.3 million.

Each of these liabilities are actuarially determined and we use various actuarial assumptions, including the discount rate and future cost trends, to estimate the costs and obligations for these items. Our discount rate is determined by utilizing a hypothetical bond portfolio model which approximates the future cash flows necessary to service our liabilities.

We make assumptions related to future trends for medical care costs in the estimates of retiree health care and work-related injuries and illnesses obligations. Our medical trend assumption is developed by annually examining the historical trend of our cost per claim data. In addition, we make assumptions related to future compensation increases and rates of return on plan assets in the estimates of pension obligations.

If our assumptions do not materialize as expected, actual cash expenditures and costs that we incur could differ materially from our current estimates. Moreover, regulatory changes could increase our obligation to satisfy these or additional obligations. For our postretirement health care liability, assumed discount rates and health care cost trend rates have a significant effect on the expense and liability amounts reported for health care plans. Below we have provided two separate sensitivity analyses to demonstrate the significance of these assumptions in relation to reported amounts.

| (Dollars in millions) | One Percentage-Point Increase | One Percentage-Point Decrease |
|---|---|---|
| Healthcare cost trend rate: | | |
| Effect on total service and interest cost components [1] | $ 6.7 | $ (5.7) |
| Effect on total postretirement benefit obligation [1] | $ 98.3 | $(84.6) |

| (Dollars in millions) | One-Half Percentage-Point Increase | One-Half Percentage-Point Decrease |
|---|---|---|
| Discount rate: | | |
| Effect on total service and interest cost components [1] | $ 0.6 | $ (0.6) |
| Effect on total postretirement benefit obligation [1] | $(46.1) | $ 52.2 |

[1] In addition to the effect on total service and interest cost components of expense, changes in trend and discount rates would also increase or decrease the actuarial gain or loss amortization expense component. The gain or loss amortization would approximate the increase or decrease in the obligation divided by 10.92 years at December 31, 2009.

*Asset Retirement Obligations*

Our asset retirement obligations primarily consist of spending estimates for surface land reclamation and support facilities at both surface and underground mines in accordance with applicable reclamation laws in the U.S. and Australia as defined by each mining permit. Asset retirement obligations are determined for each mine using various estimates and assumptions including, among other items, estimates of disturbed acreage as determined from engineering data, estimates of future costs to reclaim the disturbed acreage and the timing of these cash flows, discounted using a credit-adjusted, risk-free rate. As changes in estimates occur (such as mine plan revisions, changes in estimated costs, or changes in timing of the reclamation activities), the obligation and asset are revised to reflect the new estimate after applying the appropriate credit-adjusted, risk-free rate. If our assumptions do not materialize as expected, actual cash expenditures and costs that we incur could be materially different than currently estimated. Moreover, regulatory changes could increase our obligation to perform reclamation and mine closing activities. Asset retirement obligation expense for the year ended December 31, 2009 was $40.1 million, and payments totaled $12.4 million. See Note 13 to our consolidated financial statements for additional details regarding our asset retirement obligations.

*Income Taxes*

We account for income taxes in accordance with accounting guidance which requires deferred tax assets and liabilities be recognized using enacted tax rates for the effect of temporary differences between the book and tax bases of recorded assets and liabilities. The guidance also requires that deferred tax assets be reduced by a valuation allowance if it is "more likely than not" that some portion or all of the deferred tax asset will not be realized. In our annual evaluation of the need for a valuation allowance, we take into account various factors, including the expected level of future taxable income and available tax planning strategies. If actual results differ from the assumptions made in our annual evaluation of our valuation allowance, we may record a change in valuation allowance through income tax expense in the period such determination is made.

Our liability for unrecognized tax benefits contains uncertainties because management is required to make assumptions and to apply judgment to estimate the exposures associated with our various filing positions. We recognize the tax benefit from an uncertain tax position only if it is "more likely than not" that the tax position will be sustained on examination by the taxing authorities, based on the technical merits of the position. The tax benefits recognized in the financial statements from such a position must be measured based on the largest benefit that has a greater than 50% likelihood of being realized upon ultimate settlement. We believe that the judgments and estimates are reasonable; however, actual results could differ.

*Level 3 Fair Value Measurements*

In accordance with the "Fair Value Measurements and Disclosures" topic of the Financial Accounting Standards Board Accounting Standards Codification, we evaluate the quality and reliability of the assumptions and data used to measure fair value in the three hierarchy Levels 1, 2 and 3 (see Note 3 to our consolidated financial statements for additional information). Commodity swaps and options and physical commodity purchase/sale contracts transacted in less liquid markets or contracts, such as long-term arrangements, with limited price availability were classified in Level 3. Indicators of less liquid markets are those with periods of low trade activity or when broker quotes reflect wide pricing spreads. Generally, these instruments or contracts are valued using internally generated models that include forward pricing curve quotes from one to three reputable brokers. Our valuation techniques also include basis adjustments for heat rate, sulfur and ash content, port and freight costs, and credit and nonperformance risk. We validate our valuation inputs with third-party information and settlement prices from other sources where available. We also consider credit and nonperformance risk in the fair value measurement by analyzing the counterparty's exposure balance, credit rating and average default rate, net of any counterparty credit enhancements (e.g., collateral), as well as our own credit rating for financial derivative liabilities.

We have consistently applied these valuation techniques in all periods presented, and believe we have obtained the most accurate information reasonably available for the types of derivative contracts held. Valuation changes from period to period for each level will increase or decrease depending on: (i) the relative change in fair value for positions held, (ii) new positions added, (iii) realized amounts for completed trades, and (iv) transfers between levels. Our coal trading strategies utilize various swaps and derivative physical contracts. Periodic changes in fair value for purchase and sale positions, which are executed to lock in coal trading spreads, occur in each level and therefore the overall change in value of our coal-trading platform requires consideration of valuation changes across all levels.

At December 31, 2009, 5% of our net financial assets were categorized as Level 3. At December 31, 2008, the percentage of Level 3 net financial assets compared to the total net financial liabilities is not meaningful due to the overall liability position at December 31, 2008. See Note 3 to our consolidated financial statements for additional information regarding fair value measurements.

## NEWLY ADOPTED ACCOUNTING STANDARDS AND ACCOUNTING STANDARDS NOT YET IMPLEMENTED

See Note 1 to our consolidated financial statements for a discussion of newly adopted accounting pronouncements and accounting pronouncements not yet implemented.

## QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The potential for changes in the market value of our coal and freight trading, emission allowances, crude oil, diesel fuel, natural gas, explosives, interest rate and currency portfolios is referred to as "market risk." Market risk related to our coal trading and freight portfolio is evaluated using a value at risk (VaR) analysis. VaR analysis is not used to evaluate our non-trading interest rate, diesel fuel, explosives or currency hedging portfolios. A description of each market risk category is set forth below. We attempt to manage market risks through diversification, controlling position sizes and executing hedging strategies. Due to lack of quoted market prices and the long-term, illiquid nature of the positions, we have not quantified market risk related to our non-trading, long-term coal supply agreement portfolio.

*Coal Trading Activities and Related Commodity Price Risk*

We engage in over-the-counter, direct and brokered trading of coal, ocean freight and fuel-related commodities to support our coal trading related activities (coal trading). These activities give rise to commodity price risk, which represents the potential loss that can be caused by an adverse change in the market value of a particular commitment. We actively measure, monitor and adjust traded position levels to remain within risk limits prescribed by management. For example, we have policies in place that limit the amount of total exposure, as measured by VaR, that we may assume at any point in time.

We account for coal trading using the fair value method, which requires us to reflect financial instruments with third parties at market value in our consolidated financial statements. Our trading portfolio included forwards, swaps and options as of December 31, 2009 and 2008.

We perform a VaR analysis on our coal trading portfolio, which includes bilaterally-settled and exchange-settled over-the-counter and brokerage coal trading. The use of VaR allows us to quantify in dollars, on a daily basis, a measure of price risk inherent in our trading portfolio. VaR represents the potential loss in value of our mark-to-market portfolio due to adverse market movements over a defined time horizon (liquidation period) within a specified confidence level. Our VaR model is based on a variance/co-variance approach. This captures our exposure related to forwards, swaps and options positions. Our VaR model assumes a 5 to 15-day holding period and a 95%

one-tailed confidence interval. This means that there is a one in 20 statistical chance that the portfolio would lose more than the VaR estimates during the liquidation period. Our volatility calculation incorporates an exponentially weighted moving average algorithm based on the previous 60 market days, which makes our volatility more representative of recent market conditions, while still reflecting an awareness of historical price movements. VaR does not capture the loss expected in the 5% of the time the portfolio value exceeds measured VaR.

The use of VaR allows us to aggregate pricing risks across products in the portfolio, compare risk on a consistent basis and identify the drivers of risk. We use historical data to estimate price volatility as an input to VaR. Given our reliance on historical data, we believe VaR is reasonably effective in characterizing risk exposures in markets in which there are not sudden fundamental changes or shifts in market conditions. Due to the subjectivity in the choice of the liquidation period, reliance on historical data to calibrate the models and the inherent limitations in the VaR methodology, we perform regular stress and scenario analyses to estimate the impacts of market changes on the value of the portfolio. Additionally, back-testing is regularly performed to monitor the effectiveness of our VaR measure. The results of these analyses are used to supplement the VaR methodology and identify additional market-related risks. An inherent limitation of VaR is that past changes in market risk factors may not produce accurate predictions of future market risk.

During the year ended December 31, 2009, the actual low, high, and average VaR for our coal trading portfolio were $2.7 million, $15.9 million, and $8.7 million, respectively. Our VaR decreased over the prior year due to less price volatility and lower overall prices in the U.S. and international coal markets.

As of December 31, 2009, the timing of the estimated future realization of the value of our trading portfolio was as follows:

| *Year of Expiration* | *Percentage of Portfolio Total* |
|---|---|
| 2010 | 46% |
| 2011 | 51% |
| 2012 | 3% |
| | 100% |

We also monitor other types of risk associated with our coal trading activities, including credit, market liquidity and counterparty nonperformance.

### *Nonperformance and Credit Risk*

The fair value of our assets and liabilities reflect adjustments for nonperformance and credit risk. Our concentration of nonperformance and credit risk is substantially with electric utilities, steel producers, energy producers and energy marketers. Our policy is to independently evaluate each customer's creditworthiness prior to entering into transactions and to regularly monitor the credit extended. If we engage in a transaction with a counterparty that does not meet our credit standards, we seek to protect our position by requiring the counterparty to provide an appropriate credit enhancement. Also, when appropriate (as determined by our credit management function), we have taken steps to reduce our exposure to customers or counterparties whose credit has deteriorated and who may pose a higher risk of failure to perform under their contractual obligations. These steps include obtaining letters of credit or cash collateral, requiring prepayments for shipments or the creation of customer trust accounts held for our benefit to serve as collateral in the event of a failure to pay or perform. To reduce our credit exposure related to trading and brokerage activities, we seek to enter into netting agreements with counterparties that permit us to offset receivables and payables with such counterparties and, to the extent required, will post or receive margin amounts associated with exchange-cleared positions.

We conduct our various hedging activities related to foreign currency, interest rate, and fuel and explosives exposures with a variety of highly-rated commercial banks. In light of the recent turmoil in the financial markets, we continue to closely monitor counterparty creditworthiness.

### *Foreign Currency Risk*

We utilize currency forwards and options to hedge currency risk associated with anticipated Australian dollar expenditures. The accounting for these derivatives is discussed in Note 3 to our consolidated financial statements. Assuming we had no hedges in place, our exposure in operating costs and expenses due to a $0.05 change in the Australian dollar/U.S. dollar exchange rate is approximately $82 million for 2010. However, taking into consideration hedges currently in place, our net exposure to the same rate change is approximately $17 million for 2010. The chart in the section "Notional Amounts and Fair Value" shows the notional amount of our hedge contracts as of December 31, 2009.

### *Interest Rate Risk*

Our objectives in managing exposure to interest rate changes are to limit the impact of interest rate changes on earnings and cash flows and to lower overall borrowing costs. To achieve these objectives, we manage fixed-rate debt as a percent of net debt through the use of various hedging instruments, which are discussed in detail in Note 3 to our consolidated financial statements. As of December 31, 2009, after taking into consideration the effects of interest rate swaps, we had $2.4 billion of fixed-rate borrowings and $0.4 billion of variable-rate borrowings outstanding. A one percentage point increase in interest rates would result in an annualized increase to interest expense of approximately $4.2 million on our variable-rate borrowings. With respect to our fixed-rate borrowings, a one percentage point increase in interest rates would result in a decrease of approximately $130 million in the estimated fair value of these borrowings.

## OTHER NON-TRADING ACTIVITIES – COMMODITY PRICE RISK

### *Long-term Coal Contracts*

We manage our commodity price risk for our non-trading, long-term coal contract portfolio through the use of long-term coal supply agreements (those with terms longer than one year), rather than through the use of derivative instruments. We sold 93% and 90% of our worldwide sales volume under long-term coal supply agreements during 2009 and 2008, respectively. We are fully contracted for 2010 at planned production levels in the U.S. We had 11 to 12.5 million tons remaining to be priced for 2010 in Australia at January 26, 2010.

### *Diesel Fuel and Explosives Hedges*

We manage commodity price risk of the diesel fuel and explosives used in our mining activities through the use of fixed price contracts, cost-plus contracts and a combination of forward contracts with our suppliers and financial derivative contracts, which are primarily swap contracts with financial institutions.

Notional amounts outstanding under fuel-related, derivative swap contracts are noted in the chart in the section "Notional Amounts and Fair Value." We expect to consume 130 to 135 million gallons of diesel fuel in 2010. Assuming we had no hedges in place, a $10 per barrel change in the price of crude oil (the primary component of a refined diesel fuel product) would increase or decrease our annual diesel fuel costs by approximately $31 million based on our expected usage. However, taking into consideration hedges currently in place, our net exposure to changes in the price of crude oil is approximately $14 million.

Notional amounts outstanding under explosives-related swap contracts are noted in the section "Notional Amounts and Fair Value." We expect to consume 345,000 to 355,000 tons of explosives during 2010 in the U.S. Explosives costs in Australia are generally included in the fees paid to our contract miners. Assuming we had no hedges in place, a price change in natural gas (often a key component in the production of explosives) of one dollar per million MMBtu would result in an increase or decrease in our annual explosives costs of approximately $6 million based on our expected usage. However, taking into consideration hedges currently in place, our net exposure to changes in the price of natural gas is approximately $3 million.

### *Notional Amounts and Fair Value*

The following summarizes our interest rate, foreign currency and commodity positions at December 31, 2009:

| | *Notional Amount by Year of Maturity* | | | | | | |
|---|---|---|---|---|---|---|---|
| | *Total* | *2010* | *2011* | *2012* | *2013* | *2014* | *2015 and thereafter* |
| **Interest Rate Swaps** | | | | | | | |
| Fixed-to-floating (dollars in millions) | $ 50.0 | $ – | $ – | $ – | $ 50.0 | $ – | $ – |
| Floating-to-fixed (dollars in millions) | $ 120.0 | $ – | $120.0 | $ – | $ – | $ – | $ – |
| **Foreign Currency** | | | | | | | |
| A$:US$ hedge contracts (A$ millions) | $3,291.7 | $1,299.3 | $994.8 | $742.6 | $120.0 | $135.0 | $ – |
| **Commodity Contracts** | | | | | | | |
| Diesel fuel hedge contracts (million gallons) | 177.8 | 71.1 | 65.3 | 41.4 | – | – | – |
| U.S. explosives hedge contracts (million MMbtu) | 3.0 | 3.0 | – | – | – | – | – |

| | *Account Classification by* | | | *Fair Value Asset (Liability) (Dollars in millions)* |
|---|---|---|---|---|
| | *Cash flow hedge* | *Fair value hedge* | *Economic hedge* | |
| **Interest Rate Swaps** | | | | |
| Fixed-to-floating (dollars in millions) | $ – | $50.0 | $ – | $ 1.5 |
| Floating-to-fixed (dollars in millions) | $ 120.0 | $ – | $ – | $ (9.8) |
| **Foreign Currency** | | | | |
| A$:US$ hedge contracts (A$ millions) | $3,291.7 | $ – | $ – | $206.1 |
| **Commodity Contracts** | | | | |
| Diesel fuel hedge contracts (million gallons) | 177.8 | – | – | $ (22.2) |
| U.S. explosives hedge contracts (million MMbtu) | 3.0 | – | – | $ (4.8) |

# Management Report

## OVERVIEW

Management of Peabody Energy Corporation is responsible for the preparation and presentation of the financial statements included in this annual report. Management is also responsible for the reasonableness of estimates and judgments inherent in the preparation of the financial statements. These statements have been prepared in conformity with U.S. generally accepted accounting principles and include amounts based on management's best estimates and judgments.

The financial statements have been audited by Ernst & Young LLP, an independent registered public accounting firm. Their audit was conducted in accordance with the standards of the Public Company Accounting Oversight Board (United States). Ernst & Young also audited the effectiveness of our internal control over financial reporting.

Management maintains a strong awareness of the importance of full and open presentation of our financial position and results of operations and utilizes a system of disclosure controls and procedures to ensure such presentation. To facilitate this, the Company maintains a Disclosure Committee, which includes senior executives who possess in-depth knowledge of the Company's business.

The Audit Committee of the Board of Directors, composed of independent directors, meets periodically with the independent registered public accountants, our internal auditors and management to review accounting, auditing, internal accounting controls and financial reporting matters. The independent certified public accountants and our internal auditors have access to and separately meet on a periodic basis with the Audit Committee.

## EVALUATION OF DISCLOSURE CONTROLS AND PROCEDURES

Our disclosure controls and procedures are designed to, among other things, provide reasonable assurance that material information, both financial and non-financial, and other information required under the securities laws to be disclosed is accumulated and communicated to senior management, including the principal executive officer and principal financial officer, on a timely basis. As of December 31, 2009, the end of the period covered by this Annual Report on Form 10-K, we carried out an evaluation of the effectiveness of the design and operation of our disclosure controls and procedures. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have evaluated our disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934) as of December 31, 2009, and concluded that such controls and procedures are effective to provide reasonable assurance that the desired control objectives were achieved.

## CHANGES IN INTERNAL CONTROL OVER FINANCIAL REPORTING

We periodically review our internal control over financial reporting as part of our efforts to ensure compliance with the requirements of Section 404 of the Sarbanes-Oxley Act of 2002. In addition, we routinely review our system of internal control over financial reporting to identify potential changes to our processes and systems that may improve controls and increase efficiency, while ensuring that we maintain an effective internal control environment. Changes may include such activities as implementing new systems, consolidating the activities of acquired business units, migrating certain processes to our shared services organizations, formalizing and refining policies and procedures, improving segregation of duties and adding monitoring controls. In addition, when we acquire new businesses, we incorporate our controls and procedures into the acquired business as part of our integration activities. There have been no changes in our internal control over financial reporting that occurred during the quarter ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

## MANAGEMENT'S REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING

Management is responsible for maintaining and establishing adequate internal control over financial reporting. Our internal control framework and processes were designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of our consolidated financial statements for external purposes in accordance with U.S. generally accepted accounting principles.

Because of inherent limitations, any system of internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Management conducted an assessment of the effectiveness of our internal control over financial reporting using the criteria set by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) in *Internal Control – Integrated Framework*. Based on this assessment, management concluded that the Company's internal control over financial reporting were effective to provide reasonable assurance that the desired control objectives were achieved as of December 31, 2009.

Our Independent Registered Public Accounting Firm, Ernst & Young LLP, has audited our internal control over financial reporting, as stated in their unqualified opinion report included herein.

Gregory H. Boyce
Chairman and Chief Executive Officer

Michael C. Crews
Executive Vice President and Chief Financial Officer

February 24, 2010

## Reports of Independent Registered Public Accounting Firm

**THE BOARD OF DIRECTORS AND STOCKHOLDERS**
**PEABODY ENERGY CORPORATION**

We have audited Peabody Energy Corporation's (the Company's) internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control – Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission (the COSO criteria). Peabody Energy Corporation's management is responsible for maintaining effective internal control over financial reporting and for its assessment of the effectiveness of internal control over financial reporting included in the accompanying Management's Report on Internal Control Over Financial Reporting. Our responsibility is to express an opinion on the Company's internal control over financial reporting based on our audit.

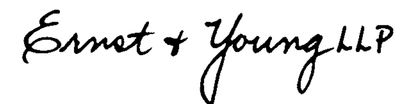
We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether effective internal control over financial reporting was maintained in all material respects. Our audit included obtaining an understanding of internal control over financial reporting, assessing the risk that a material weakness exists, testing and evaluating the design and operating effectiveness of internal control based on the assessed risk, and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion.

A company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that (1) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the company; (2) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the company; and (3) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use, or disposition of the company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions or that the degree of compliance with the policies or procedures may deteriorate.

In our opinion, Peabody Energy Corporation maintained, in all material respects, effective internal control over financial reporting as of December 31, 2009, based on the COSO criteria.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheets of Peabody Energy Corporation as of December 31, 2009 and 2008, and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2009, and our report dated February 24, 2010, expressed an unqualified opinion thereon.



St. Louis, Missouri
February 24, 2010

**THE BOARD OF DIRECTORS AND STOCKHOLDERS**
**PEABODY ENERGY CORPORATION**

We have audited the accompanying consolidated balance sheets of Peabody Energy Corporation (the Company) as of December 31, 2009 and 2008, and the related consolidated statements of operations, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 2009. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Peabody Energy Corporation at December 31, 2009 and 2008, and the consolidated results of its operations and its cash flows for each of the three years in the period ended December 31, 2009, in conformity with U.S. generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, on January 1, 2009, the Company changed its method for accounting for noncontrolling interests, its method for accounting for convertible debt that may be settled in cash upon conversion, and its method for accounting for earnings per share under the two-class method, and on January 1, 2008, the Company changed its method of accounting for the recognition of derivative positions with the same counterparty.

We also have audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), Peabody Energy Corporation's internal control over financial reporting as of December 31, 2009, based on criteria established in *Internal Control – Integrated Framework*, issued by the Committee of Sponsoring Organizations of the Treadway Commission, and our report dated February 24, 2010, expressed an unqualified opinion thereon.

St. Louis, Missouri
February 24, 2010

## Consolidated Statements of Operations

| *Years Ended December 31 (Dollars in millions, except per share data)* | ***2009*** | *2008* | *2007* |
|---|---|---|---|
| **Revenues** | | | |
| Sales | **$5,468.1** | $6,004.0 | $4,313.9 |
| Other revenues | **544.3** | 557.0 | 209.9 |
| Total revenues | **6,012.4** | 6,561.0 | 4,523.8 |
| **Costs and Expenses** | | | |
| Operating costs and expenses | **4,467.7** | 4,585.2 | 3,510.1 |
| Depreciation, depletion and amortization | **405.2** | 402.4 | 346.3 |
| Asset retirement obligation expense | **40.1** | 48.2 | 23.7 |
| Selling and administrative expenses | **208.7** | 201.8 | 147.1 |
| Other operating (income) loss: | | | |
| Net gain on disposal or exchange of assets | **(23.2)** | (72.9) | (88.6) |
| (Income) loss from equity affiliates | **69.1** | – | (14.5) |
| **Operating Profit** | **844.8** | 1,396.3 | 599.7 |
| Interest expense | **201.2** | 227.0 | 235.8 |
| Interest income | **(8.1)** | (10.0) | (7.0) |
| **Income From Continuing Operations Before Income Taxes** | **651.7** | 1,179.3 | 370.9 |
| Income tax provision (benefit) | **193.8** | 191.4 | (70.7) |
| **Income From Continuing Operations, Net of Income Taxes** | **457.9** | 987.9 | 441.6 |
| Income (loss) from discontinued operations, net of income taxes | **5.1** | (28.8) | (180.1) |
| **Net Income** | **463.0** | 959.1 | 261.5 |
| Less: Net income (loss) attributable to noncontrolling interests | **14.8** | 6.2 | (2.3) |
| **Net Income Attributable to Common Stockholders** | **$ 448.2** | $ 952.9 | $ 263.8 |
| **Income From Continuing Operations** | | | |
| Basic earnings per share | **$ 1.66** | $ 3.63 | $ 1.67 |
| Diluted earnings per share | **$ 1.64** | $ 3.60 | $ 1.64 |
| **Net Income Attributable to Common Stockholders** | | | |
| Basic earnings per share | **$ 1.68** | $ 3.52 | $ 0.99 |
| Diluted earnings per share | **$ 1.66** | $ 3.50 | $ 0.97 |
| **Dividends declared per share** | **$ 0.25** | $ 0.24 | $ 0.24 |

*See accompanying notes to consolidated financial statements*

## Consolidated Balance Sheets

| *December 31 (Amounts in millions, except share and per share data)* | ***2009*** | *2008* |
|---|---|---|
| **Assets** | | |
| Current assets | | |
| Cash and cash equivalents | **$ 988.8** | $ 449.7 |
| Accounts receivable, net of allowance for doubtful accounts of $18.3 at December 31, 2009 and $24.8 at December 31, 2008 | **303.0** | 382.2 |
| Inventories | **325.1** | 276.2 |
| Assets from coal trading activities, net | **276.8** | 662.8 |
| Deferred income taxes | **40.0** | 1.7 |
| Other current assets | **255.3** | 198.7 |
| Total current assets | **2,189.0** | 1,971.3 |
| Property, plant, equipment and mine development | | |
| Land and coal interests | **7,557.3** | 7,349.4 |
| Buildings and improvements | **908.0** | 858.1 |
| Machinery and equipment | **1,391.2** | 1,245.1 |
| Less: accumulated depreciation, depletion and amortization | **(2,595.0)** | (2,155.3) |
| Property, plant, equipment and mine development, net | **7,261.5** | 7,297.3 |
| Investments and other assets | **504.8** | 427.0 |
| Total assets | **$ 9,955.3** | $ 9,695.6 |
| **Liabilities and Stockholders' Equity** | | |
| Current liabilities | | |
| Current maturities of long-term debt | **$ 14.1** | $ 17.0 |
| Liabilities from coal trading activities, net | **110.6** | 304.2 |
| Accounts payable and accrued expenses | **1,187.7** | 1,535.0 |
| Total current liabilities | **1,312.4** | 1,856.2 |
| Long-term debt, less current maturities | **2,738.2** | 2,776.6 |
| Deferred income taxes | **299.1** | 20.8 |
| Asset retirement obligations | **452.1** | 418.7 |
| Accrued postretirement benefit costs | **914.1** | 766.1 |
| Other noncurrent liabilities | **483.5** | 737.7 |
| Total liabilities | **6,199.4** | 6,576.1 |
| Stockholders' equity | | |
| Preferred Stock – $0.01 per share par value; 10,000,000 shares authorized, no shares issued or outstanding as of December 31, 2009 or December 31, 2008 | **–** | – |
| Series A Junior Participating Preferred Stock – 1,500,000 shares authorized, no shares issued or outstanding as of December 31, 2009 or December 31, 2008 | **–** | – |
| Perpetual Preferred Stock – 750,000 shares authorized, no shares issued or outstanding as of December 31, 2009 or 2008 | **–** | – |
| Series Common Stock – $0.01 per share par value; 40,000,000 shares authorized, no shares issued or outstanding as of December 31, 2009 or December 31, 2008 | **–** | – |
| Common Stock – $0.01 per share par value; 800,000,000 shares authorized, 276,848,279 shares issued and 268,203,815 shares outstanding as of December 31, 2009 and 275,211,240 shares issued and 266,644,979 shares outstanding as of December 31, 2008 | **2.8** | 2.8 |
| Additional paid-in capital | **2,067.7** | 2,020.2 |
| Retained earnings | **2,183.8** | 1,802.4 |
| Accumulated other comprehensive loss | **(183.5)** | (388.5) |
| Treasury shares, at cost: 8,644,464 shares as of December 31, 2009 and 8,566,261 shares as of December 31, 2008 | **(321.1)** | (318.8) |
| Peabody Energy Corporation's stockholders' equity | **3,749.7** | 3,118.1 |
| Noncontrolling interests | **6.2** | 1.4 |
| Total stockholders' equity | **3,755.9** | 3,119.5 |
| Total liabilities and stockholders' equity | **$ 9,955.3** | $ 9,695.6 |

*See accompanying notes to consolidated financial statements*

## Consolidated Statements of Cash Flows

| *Years Ended December 31* *(Dollars in millions)* | **2009** | 2008 | 2007 |
|---|---|---|---|
| **Cash Flows From Operating Activities** | | | |
| Net income | **$ 463.0** | $ 959.1 | $ 261.5 |
| (Income) loss from discontinued operations, net of income taxes | **(5.1)** | 28.8 | 180.1 |
| Income from continuing operations, net of income taxes | **457.9** | 987.9 | 441.6 |
| Adjustments to reconcile income from continuing operations, net of income taxes to net cash provided by operating activities: | | | |
| Depreciation, depletion and amortization | **405.2** | 402.4 | 346.3 |
| Deferred income taxes | **131.1** | (33.3) | (196.5) |
| Share-based compensation | **38.8** | 34.9 | 20.1 |
| Amortization of debt discount and debt issuance costs | **7.8** | 7.7 | 8.0 |
| Net gain on disposal or exchange of assets | **(23.2)** | (72.9) | (88.6) |
| (Income) loss from equity affiliates | **69.1** | – | (14.5) |
| Revenue recovery on coal supply agreement | **–** | (56.9) | – |
| Dividends received from equity affiliates | **–** | 19.9 | 12.9 |
| Changes in current assets and liabilities: | | | |
| Accounts receivable, including securitization | **81.4** | (114.7) | 65.6 |
| Inventories | **(48.9)** | (13.2) | (60.9) |
| Net assets from coal trading activities | **70.9** | (43.0) | (77.6) |
| Other current assets | **(3.3)** | 1.9 | (57.1) |
| Accounts payable and accrued expenses | **(123.8)** | 235.1 | 52.6 |
| Asset retirement obligations | **27.7** | 32.9 | 13.6 |
| Workers' compensation obligations | **3.0** | 10.3 | 2.7 |
| Accrued postretirement benefit costs | **7.2** | 13.6 | 13.1 |
| Contributions to pension plans | **(38.7)** | (21.3) | (5.4) |
| Other, net | **(8.7)** | 18.5 | (15.2) |
| **Net cash provided by continuing operations** | **1,053.5** | 1,409.8 | 460.7 |
| Net cash used in discontinued operations | **(5.6)** | (123.0) | (141.3) |
| Net cash provided by operating activities | **1,047.9** | 1,286.8 | 319.4 |
| **Cash Flows From Investing Activities** | | | |
| Additions to property, plant, equipment and mine development | **(260.6)** | (264.1) | (438.8) |
| Investment in Prairie State Energy Campus | **(56.8)** | (40.9) | (28.8) |
| Federal coal lease expenditures | **(123.6)** | (178.5) | (178.2) |
| Proceeds from disposal of assets, net of notes receivable | **53.9** | 72.8 | 119.6 |
| Additions to advance mining royalties | **(6.1)** | (6.0) | (8.1) |
| Investments in equity affiliates and joint ventures | **(15.0)** | (2.6) | (4.6) |
| **Net cash used in continuing operations** | **(408.2)** | (419.3) | (538.9) |
| Net cash provided by (used in) discontinued operations | **1.7** | 23.9 | (36.4) |
| Net cash used in investing activities | **(406.5)** | (395.4) | (575.3) |
| **Cash Flows From Financing Activities** | | | |
| Change in revolving line of credit | **–** | (97.7) | 97.7 |
| Payments of long-term debt | **(37.1)** | (32.7) | (117.8) |
| Common stock repurchase | **–** | (199.8) | – |
| Dividends paid | **(66.8)** | (64.9) | (63.7) |
| Payment of debt issuance costs | **–** | – | (0.8) |
| Excess tax benefit related to stock options exercised | **–** | – | 96.7 |
| Proceeds from stock options exercised | **3.6** | 14.1 | 26.2 |
| Net proceeds from borrowing | **0.8** | – | – |
| Acquisition of noncontrolling interests (Millennium Mine) | **–** | (110.1) | – |
| Other, net | **(2.8)** | 4.1 | 3.4 |
| **Net cash provided by (used in) continuing operations** | **(102.3)** | (487.0) | 41.7 |
| Net cash used in discontinued operations | **–** | – | (67.0) |
| Net cash used in financing activities | **(102.3)** | (487.0) | (25.3) |
| Net change in cash and cash equivalents | **539.1** | 404.4 | (281.2) |
| Cash and cash equivalents at beginning of year | **449.7** | 45.3 | 326.5 |
| Cash and cash equivalents at end of year | **$ 988.8** | $ 449.7 | $ 45.3 |

*See accompanying notes to consolidated financial statements*

## Consolidated Statements of Changes in Stockholders' Equity

| | *Peabody Energy Corporation's Stockholders' Equity* | | | | | | |
|---|---|---|---|---|---|---|---|
| *(Dollars in millions)* | *Common Stock* | *Additional Paid-in Capital* | *Treasury Stock* | *Retained Earnings* | *Accumulated Other Comprehensive Loss* | *Noncontrolling Interests* | *Total Stockholders' Equity* |
| December 31, 2006 | $2.7 | $ 1,788.0 | $ (103.7) | $ 1,115.9 | $ (249.2) | $ 33.3 | $ 2,587.0 |
| Comprehensive income: | | | | | | | |
| Net income | – | – | – | 263.8 | – | (2.3) | 261.5 |
| Increase in fair value of cash flow hedges (net of $14.5 tax provision) | – | – | – | – | 21.9 | – | 21.9 |
| Postretirement plans and workers' compensation obligations (net of $50.2 tax provision): | – | – | – | – | 87.2 | – | 87.2 |
| Comprehensive income | | | | 263.8 | 109.1 | (2.3) | 370.6 |
| Dividends paid | – | – | – | (63.7) | – | – | (63.7) |
| Patriot Coal Corporation spin-off | – | – | – | (375.1) | 73.0 | (14.1) | (316.2) |
| Share-based compensation | – | 48.8 | – | – | – | – | 48.8 |
| Stock options exercised | – | 26.2 | – | – | – | – | 26.2 |
| Employee stock purchases | – | 6.4 | – | – | – | – | 6.4 |
| Shares relinquished | – | – | (4.3) | – | – | – | (4.3) |
| Income tax benefits from stock options exercised | – | 96.7 | – | – | – | – | 96.7 |
| Noncontrolling interests activity related to discontinued operations | – | – | – | – | – | (6.2) | (6.2) |
| Acquisition of noncontrolling interests associated with Excel Coal Limited – purchase accounting adjustment | – | – | – | – | – | (7.0) | (7.0) |
| Distributions to noncontrolling interests | – | – | – | – | – | (3.0) | (3.0) |
| December 31, 2007 | $2.7 | $ 1,966.1 | $ (108.0) | $ 940.9 | $ (67.1) | $ 0.7 | $ 2,735.3 |
| Comprehensive income: | | | | | | | |
| Net income | – | – | – | 952.9 | – | 6.2 | 959.1 |
| Decrease in fair value of cash flow hedges (net of $178.2 tax benefit) | – | – | – | – | (217.9) | – | (217.9) |
| Postretirement plans and workers' compensation obligations (net of $59.3 tax benefit) | – | – | – | – | (103.5) | – | (103.5) |
| Comprehensive income | | | | 952.9 | (321.4) | 6.2 | 637.7 |
| Dividends paid | – | – | – | (64.9) | – | – | (64.9) |
| Patriot Coal Corporation spin-off adjustment | – | – | – | (26.5) | – | – | (26.5) |
| Share-based compensation | – | 34.9 | – | – | – | – | 34.9 |
| Stock options exercised | 0.1 | 14.0 | – | – | – | – | 14.1 |
| Employee stock purchases | – | 5.2 | – | – | – | – | 5.2 |
| Shares relinquished | – | – | (11.0) | – | – | – | (11.0) |
| Common stock repurchased | – | – | (199.8) | – | – | – | (199.8) |
| Distributions to noncontrolling interests | – | – | – | – | – | (1.1) | (1.1) |
| Eliminations of noncontrolling interests due to acquisitions | – | – | – | – | – | (4.4) | (4.4) |
| December 31, 2008 | **$2.8** | **$2,020.2** | **$(318.8)** | **$1,802.4** | **$(388.5)** | **$ 1.4** | **$3,119.5** |
| Comprehensive income: | | | | | | | |
| Net income | **–** | **–** | **–** | **448.2** | **–** | **14.8** | **463.0** |
| Increase in fair value of cash flow hedges (net of $220.9 tax provision) | **–** | **–** | **–** | **–** | **319.8** | **–** | **319.8** |
| Postretirement plans and workers' compensation obligations (net of $71.8 tax benefit) | **–** | **–** | **–** | **–** | **(114.8)** | **–** | **(114.8)** |
| Comprehensive income | | | | **448.2** | **205.0** | **14.8** | **668.0** |
| Dividends paid | **–** | **–** | **–** | **(66.8)** | **–** | **–** | **(66.8)** |
| Share-based compensation | **–** | **38.8** | **–** | **–** | **–** | **–** | **38.8** |
| Stock options exercised | **–** | **3.6** | **–** | **–** | **–** | **–** | **3.6** |
| Employee stock purchases | **–** | **5.1** | **–** | **–** | **–** | **–** | **5.1** |
| Shares relinquished | **–** | **–** | **(2.3)** | **–** | **–** | **–** | **(2.3)** |
| Distributions to noncontrolling interests | **–** | **–** | **–** | **–** | **–** | **(10.0)** | **(10.0)** |
| **December 31, 2009** | **$2.8** | **$2,067.7** | **$(321.1)** | **$2,183.8** | **$(183.5)** | **$ 6.2** | **$3,755.9** |

*See accompanying notes to consolidated financial statements*

# Notes to Consolidated Financial Statements

Years Ended December 31

## (1) SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

### *Basis of Presentation*

The consolidated financial statements include the accounts of Peabody Energy Corporation (the Company) and its affiliates. All intercompany transactions, profits and balances have been eliminated in consolidation.

### *Description of Business*

The Company is engaged in the mining of thermal coal for sale primarily to electric utilities and metallurgical coal for sale to industrial customers. The Company's mining operations are located in the United States (U.S.) and Australia, and include an equity interest in a mining operation in Venezuela. In addition to the Company's mining operations, the Company markets, brokers and trades coal. The Company's other energy related commercial activities include participating in the development of mine-mouth coal-fueled generating plants, the management of its vast coal reserve and real estate holdings, and the development of Btu Conversion and clean coal technologies. The Company's Btu Conversion projects are designed to expand the uses of coal through various technologies such as coal-to-liquids and coal gasification.

### *Newly Adopted Accounting Standards*

In August 2009, the Financial Accounting Standards Board (FASB) issued accounting guidance that clarifies the fair value measurement of liabilities in circumstances in which a quoted price in an active market for the identical liability is not available. In those circumstances, an entity is required to measure fair value utilizing one or more of the following techniques: (1) a valuation technique that uses the quoted market price of an identical liability or similar liabilities when traded as assets; or (2) another valuation technique that is consistent with the principles of Accounting Standards Codification (ASC) Topic 820, such as a present value technique or market approach. The guidance also clarifies that when estimating the fair value liability, a reporting entity is not required to include a separate input or adjustment to other inputs relating to the existence of a restriction that prevents the transfer of a liability. Additionally, the guidance clarifies that both a quoted price in an active market for the identical liability at the measurement date and the quoted price for the identical liability when traded as an asset in an active market when no adjustments to the quoted price of the asset are required are Level 1 fair value measurements. The guidance, which became effective in the fourth quarter of 2009, did not have a material impact on the Company's results of operations or financial condition.

In May 2009, the FASB issued an accounting standard that was effective upon issuance that establishes accounting and disclosure guidance for subsequent events, which are events that occur after the balance sheet date but before financial statements are issued or are available to be issued. The Company evaluated subsequent events after the balance sheet date of December 31, 2009 through the filing of this report with the Securities and Exchange Commission on February 24, 2010.

In April 2009, the FASB issued an accounting standard which requires disclosures of the fair value of all financial instruments for which it is practicable to estimate that value, whether recognized or not on a company's balance sheet, in interim reporting periods and in financial statements for annual reporting periods. A related standard was also issued in April 2009 which requires entities to disclose the methods and significant assumptions used to estimate the fair value of financial instruments and describe changes in methods and significant assumptions, in both interim and annual financial statements. The Company adopted the standards on June 30, 2009. See Note 3 for further information.

In April 2009, the FASB issued an accounting standard which provides additional guidance for estimating fair value when the volume and level of activity for the asset or liability have significantly decreased. The standard also includes guidance on identifying circumstances that indicate a transaction is not orderly and requires that a reporting entity: (1) disclose in interim and annual periods the inputs and valuation technique(s) used to measure fair value and a discussion of changes in valuation techniques and related inputs, if any, during the period, and (2) define the "major category" for any equity securities and debt securities to be based on the "major security types" (nature and risk of the security). The Company adopted the standard on June 30, 2009. While adoption of the standard had an impact on the Company's disclosures, it did not affect the Company's results of operations or financial condition.

In December 2008, the FASB issued an accounting standard to provide for additional transparency on an employer's disclosures about plan assets of a defined benefit pension or other postretirement plan, including the concentrations of risk in those plans. The Company adopted the standard on December 31, 2009. While the adoption of this guidance had an impact on the Company's disclosures, it did not affect the Company's results of operations, financial condition or cash flows.

In June 2008, the FASB issued an accounting standard requiring share-based payment awards that entitle their holders to receive nonforfeitable dividends or dividend equivalents before vesting should be considered participating securities and need to be included in the earnings allocation in computing earnings per share (EPS) under the "two-class method." The two-class method is an earnings allocation formula that determines EPS for each class of common stock and participating security according to dividends declared (or accumulated) and participation rights in undistributed earnings. The Company's unvested restricted stock awards are considered participating securities because they entitle holders to receive nonforfeitable dividends during the vesting term. In applying the two-class method, undistributed earnings are allocated between common shares and unvested restricted stock awards. The standard was effective for the Company for the fiscal year beginning January 1, 2009 where the two-class method of computing basic and diluted EPS was applied for all periods presented. See Note 7 for additional information.

In May 2008, the FASB issued an accounting standard which clarifies that convertible debt instruments that may be settled in cash upon conversion, including partial cash settlement, are not within the scope of the "Debt" topic of the FASB ASC. Instead, issuers of such instruments should separately account for the liability and equity components in a manner that will reflect the issuer's nonconvertible debt borrowing rate when recognizing interest cost in subsequent periods. The standard was effective for the Company's Convertible Junior Subordinated Debentures for the fiscal year beginning January 1, 2009. Prior period balances in this report have been adjusted to conform with these provisions. See Note 12 for additional information.

In March 2008, the FASB issued an accounting standard which expands the disclosure requirements for derivative instruments and hedging activities. The standard specifically requires entities to provide enhanced disclosures addressing the following: (1) how and why an entity uses derivative instruments, (2) how derivative instruments and related hedged items are accounted for under the "Derivatives and Hedging" topic of the FASB ASC, and (3) how derivative instruments and related hedged items affect an entity's financial position, financial performance and cash flows. The standard was effective for the Company for the fiscal year beginning January 1, 2009. While the standard had an impact on the Company's disclosures, it did not affect the Company's results of operations or financial condition. These additional disclosures are included in Note 3.

In December 2007, the FASB issued an accounting standard which establishes accounting and reporting guidance for noncontrolling interests in partially-owned consolidated subsidiaries and the loss of control of subsidiaries. The standard requires noncontrolling interests (minority interests) to be reported as a separate component of equity. In addition, the standard requires that a parent recognize a gain or loss in net income when a subsidiary is deconsolidated. The standard was effective for the Company for the fiscal year beginning January 1, 2009. Prior period balances in this report have been adjusted to conform with these provisions.

In December 2007, the FASB issued an accounting standard which changes the principles and requirements for the recognition and measurement of identifiable assets acquired, liabilities assumed and any noncontrolling interest of an acquiree in the financial statements of an acquirer. This standard also provides for the recognition and measurement of goodwill acquired in a business combination and related disclosure. This standard applies prospectively to business combinations for which the acquisition date is on or after the beginning of the first annual reporting period beginning January 1, 2009. In April 2009, the FASB issued additional guidance on this topic, which amended and clarified the initial recognition and measurement, subsequent measurement and accounting and related disclosures arising from contingencies in a business combination. Under this guidance, assets acquired and liabilities assumed in a business combination that arise from contingencies should be recognized at fair value on the acquisition date if fair value can be determined during the measurement period. If fair value cannot be determined, companies should typically account for the acquired contingencies using existing guidance. This standard is effective for business combinations with an acquisition date that is on or after the beginning of the first annual reporting period beginning January 1, 2009.

In September 2006, the FASB issued an accounting standard which establishes a framework for measuring fair value under U.S. generally accepted accounting principles (GAAP) and expands disclosures about fair value measurements. The standard applies under accounting pronouncements that require or permit fair value measurements, but the standard does not require any new fair value measurements. In February 2008, the FASB amended the standard to exclude leasing transactions and to delay the effective date by one year for nonfinancial assets and liabilities that are recognized or disclosed at fair value in the financial statements on a nonrecurring basis. The Company adopted the standard on a prospective basis on January 1, 2008. In October 2008, the FASB issued additional guidance, which clarifies the application of the standard in an inactive market and demonstrated how the fair value of a financial asset is determined when the market for that financial asset is inactive. This guidance was effective upon issuance, including prior periods for which financial statements had not been issued. The adoption of the standard did not have a material impact on the Company's determination of fair value for financial assets. See Note 3 for additional details on fair value.

### *Accounting Standards Not Yet Implemented*

In June 2009, the FASB issued accounting guidance which modifies how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. The guidance clarifies that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance. The guidance also requires an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity, and additional disclosures about a company's involvement in variable interest entities and any associated changes in risk exposure. The guidance is applicable for annual periods beginning after November 15, 2009 (January 1, 2010 for the Company), at which time the Company will begin the monitoring and assessment of its business ventures in accordance with the guidance.

In June 2009, the FASB issued an accounting standard that seeks to improve the relevance, representational faithfulness and comparability of the information that a reporting entity provides in its financial statements about a transfer of financial assets; the effects of a transfer on its financial position, financial performance and cash flows; and a transferor's continuing involvement, if any, in transferred financial assets. The standard is effective for annual periods beginning after November 15, 2009 (January 1, 2010 for the Company). While the adoption of this guidance will have an impact on the Company's disclosures, it will not affect the Company's results of operations, financial condition or cash flows.

### Sales

The Company's revenue from coal sales is realized and earned when risk of loss passes to the customer. Under the typical terms of the Company's coal supply agreements, title and risk of loss transfer to the customer at the mine or port, where coal is loaded to the transportation source(s) that serves each of the Company's mines. The Company incurs certain "add-on" taxes and fees on coal sales. Reported coal sales include taxes and fees charged by various federal and state governmental bodies and the freight charges on destination customer contracts.

### Other Revenues

Other revenues include royalties related to coal lease agreements, sales agency commissions, farm income, property and facility rentals, generation development activities, net revenues from coal trading activities accounted for under the Derivatives and Hedging guidance of the ASC and contract termination or restructuring payments. Royalty income generally results from the lease or sublease of mineral rights to third parties, with payments based upon a percentage of the selling price or an amount per ton of coal produced.

### Discontinued Operations and Assets Held for Sale

The Company classifies items within discontinued operations in the consolidated statements of operations when the operations and cash flows of a particular component (defined as operations and cash flows that can be clearly distinguished, operationally and for financial reporting purposes, from the rest of the entity) of the Company have been (or will be) eliminated from the ongoing operations of the Company as a result of a disposal transaction, and the Company will no longer have any significant continuing involvement in the operations of that component. See Note 2 for additional details related to discontinued operations and assets held for sale.

### Cash and Cash Equivalents

Cash and cash equivalents are stated at cost, which approximates fair value. Cash equivalents consist of highly liquid investments with original maturities of three months or less.

### Inventories

Materials and supplies and coal inventory are valued at the lower of average cost or market. Raw coal represents coal stockpiles that may be sold in current condition or may be further processed prior to shipment to a customer. Coal inventory costs include labor, supplies, equipment, operating overhead and other related costs.

### Property, Plant, Equipment and Mine Development

Property, plant, equipment and mine development are recorded at cost. Interest costs applicable to major asset additions are capitalized during the construction period. Capitalized interest in 2009, 2008 and 2007 was immaterial.

Expenditures which extend the useful lives of existing plant and equipment assets are capitalized. Maintenance and repairs are charged to operating costs as incurred. Costs incurred to develop coal mines or to expand the capacity of operating mines are capitalized. Costs incurred to maintain current production capacity at a mine and exploration expenditures are charged to operating costs as incurred, including costs related to drilling and study costs incurred to convert or upgrade mineral resources to reserves. Costs to acquire computer hardware and the development and/or purchase of software for internal use are capitalized and depreciated over the estimated useful lives.

Coal reserves are recorded at cost, or at fair value in the case of acquired businesses. The net book value of coal reserves totaled $5.3 billion as of December 31, 2009 and $5.4 billion as of December 31, 2008. These coal reserves include mineral rights for leased coal interests and advance royalties that had a net book value of $4.0 billion as of December 31, 2009 and $4.1 billion as of December 31, 2008. The remaining net book value of coal reserves of $1.3 billion at December 31, 2009 and 2008 relates to coal reserves held by fee ownership. Amounts attributable to properties where the Company was not currently engaged in mining operations or leasing to third parties and, therefore, the coal reserves were not currently being depleted was $1.9 billion as of December 31, 2009 and 2008.

Depletion of coal reserves and amortization of advance royalties is computed using the units-of-production method utilizing only proven and probable reserves (as adjusted for recoverability factors) in the depletion base. Mine development costs are principally amortized over the estimated lives of the mines using the straight-line method. Depreciation of plant and equipment (excluding life of mine assets) is computed using the straight-line method over the estimated useful lives as follows:

| | Years |
|---|---|
| Building and improvements | 10 to 20 |
| Machinery and equipment | 3 to 37 |
| Leasehold improvements | Life of Lease |

In addition, certain plant and equipment assets associated with mining are depreciated using the straight-line method over the estimated life of the mine, which varies from one to 37 years.

### Investments in Joint Ventures

The Company accounts for its investments in less than majority owned corporate joint ventures under either the equity or cost method. The Company applies the equity method to investments in joint ventures when it has the ability to exercise significant influence over the operating and financial policies of the joint venture. Investments accounted for under the equity method are initially recorded at cost, and any difference between the cost of the Company's investment and the underlying equity in the net assets of the joint venture at the investment date is amortized over the lives of the related assets that gave rise to the difference. The Company's pro rata share of earnings from joint ventures and basis difference amortization is reported in the consolidated statements of operations in "(Income) loss from equity affiliates." Included in the Company's equity method investments is its joint venture interest in Carbones del Guasare, which owns and operates the Paso Diablo Mine in Venezuela. In 2009, the Company recognized an impairment loss of $34.7 million related to its interest in Carbones del Guasare based on the joint venture's deteriorating operating results (resulting in 2009 equity losses of $19.9 million), ongoing cash flow issues resulting in no dividend payments since January 2008, the Company's expectations concerning ongoing operating and cash flow issues for the joint venture and uncertainty impacting recoverability of this investment. The table below summarizes the book value of the Company's equity method investments, which is reported in "Investments and other assets" in the consolidated balance sheets, the income (loss) from its equity affiliates and dividends received from its equity investments:

| | Book value at December 31, | | Income (loss) from equity affiliates for the year ended December 31, | | |
|---|---|---|---|---|---|
| (Dollars in millions) | **2009** | 2008 | **2009** | 2008 | 2007 |
| Interest in Carbones del Guasare | **$ –** | $54.2 | **$(54.6)** | $5.7 | $21.2 |
| Other equity method investments | **14.1** | 7.0 | **(14.5)** | (5.7) | (6.7) |
| Total equity method investments | **$14.1** | $61.2 | **$(69.1)** | $ – | $14.5 |

### Asset Retirement Obligations

The Company's asset retirement obligation (ARO) liabilities primarily consist of spending estimates for surface land reclamation and support facilities at both surface and underground mines in accordance with applicable reclamation laws in the U.S. and Australia as defined by each mining permit.

The Company estimates its ARO liabilities for final reclamation and mine closure based upon detailed engineering calculations of the amount and timing of the future cash spending for a third-party to perform the required work. Spending estimates are escalated for inflation and then discounted at the credit-adjusted, risk-free rate. The Company records an ARO asset associated with the discounted liability for final reclamation and mine closure. The obligation and corresponding asset are recognized in the period in which the liability is incurred. The ARO asset is amortized on the units-of-production method over its expected life and the ARO liability is accreted to the projected spending date. As changes in estimates occur (such as mine plan revisions, changes in estimated costs or changes in timing of the performance of reclamation activities), the revisions to the obligation and asset are recognized at the appropriate historical credit-adjusted, risk-free rate. The Company also recognizes an obligation for contemporaneous reclamation liabilities incurred as a result of surface mining. Contemporaneous reclamation consists primarily of grading, topsoil replacement and re-vegetation of backfilled pit areas.

### Environmental Liabilities

Included in "Other noncurrent liabilities" are accruals for other environmental matters that are recorded in operating expenses when it is probable that a liability has been incurred and the amount of the liability can be reasonably estimated. Accrued liabilities are exclusive of claims against third parties and are not discounted. In general, costs related to environmental remediation are charged to expense.

### Income Taxes

Income taxes are accounted for using a balance sheet approach. The Company accounts for deferred income taxes by applying statutory tax rates in effect at the reporting date of the balance sheet to differences between the book and tax basis of assets and liabilities. A valuation allowance is established if it is "more likely than not" that the related tax benefits will not be realized. In determining the appropriate valuation allowance, the Company considers projected realization of tax benefits based on expected levels of future taxable income, available tax planning strategies, and the overall deferred tax position.

The Company recognized the tax benefit from uncertain tax positions only if it is "more likely than not" the tax position will be sustained on examination by the taxing authorities. The tax benefits recognized from such a position are measured based on the largest benefit that has a greater than fifty percent likelihood of being realized upon ultimate settlement. To the extent the Company's assessment of such tax positions changes, the change in estimate will be recorded in the period in which the determination is made. Tax-related interest and penalties are classified as a component of income tax expense.

***Postretirement Health Care and Life Insurance Benefits***

The Company accounts for postretirement benefits other than pensions by accruing the costs of benefits to be provided over the employees' period of active service. These costs are determined on an actuarial basis. The Company's consolidated balance sheets reflect the funded status of postretirement benefits.

***Pension Plans***

The Company sponsors non-contributory defined benefit pension plans accounted for by accruing the cost to provide the benefits over the employees' period of active service. These costs are determined on an actuarial basis. The Company's consolidated balance sheets reflect the funded status of the defined benefit pension plans.

***Derivatives***

The Company recognizes at fair value all derivatives as assets or liabilities on the consolidated balance sheets. Gains or losses from derivative financial instruments designated as fair value hedges are recognized immediately in the consolidated statements of operations, along with the offsetting gain or loss related to the underlying hedged item.

Non-derivative contracts and derivative contracts for which the Company has elected to apply the normal purchase/normal sale exception are accounted for on an accrual basis.

Gains or losses on derivative financial instruments designated as cash flow hedges are recorded as a separate component of stockholders' equity until the hedged transaction occurs (or until hedge ineffectiveness is determined), at which time gains or losses are reclassified to the consolidated statements of operations in conjunction with the recognition of the underlying hedged item. To the extent that the periodic changes in the fair value of the derivatives exceed the changes in the hedged item, the ineffective portion of the periodic non-cash changes are recorded in the consolidated statements of operations in the period of the change. If the hedge ceases to qualify for hedge accounting, the Company prospectively recognizes the mark-to-market movements in the consolidated statements of operations in the period of the change. The potential for hedge ineffectiveness is present in the design of the Company's cash flow hedge relationships and is discussed in detail in Note 3.

***Use of Estimates in the Preparation of the Consolidated Financial Statements***

The preparation of financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

***Impairment of Long-Lived Assets***

The Company records impairment losses on long-lived assets used in operations when events and circumstances indicate that assets might be impaired and the undiscounted cash flows estimated to be generated by those assets under various assumptions are less than the carrying amounts of the assets. Impairment losses are measured by comparing the estimated fair value of the impaired asset to its carrying amount. There were no impairment losses recorded during the years ended December 31, 2009, 2008 or 2007.

***Fair Value***

For assets and liabilities that are recognized or disclosed at fair value in the consolidated financial statements, the Company defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date.

The Company's asset and liability derivative positions are offset on a counterparty-by-counterparty basis if the contractual agreement provides for the net settlement of contracts with the counterparty in the event of default or termination of any one contract.

***Foreign Currency***

The Company's foreign subsidiaries utilize the U.S. dollar as their functional currency. As such, monetary assets and liabilities are remeasured at year-end exchange rates while non-monetary items are remeasured at historical rates. Income and expense accounts are remeasured at the average rates in effect during the year, except for those expenses related to balance sheet amounts that are remeasured at historical exchange rates. Gains and losses from foreign currency remeasurement related to tax balances are included as a component of income tax expense while all other remeasurement gains and losses are included in operating costs and expenses. The foreign currency remeasurement loss for the year ended December 31, 2009, was $55.4 million. The foreign currency remeasurement gain for the year ended December 31, 2008 was $71.1 million and the foreign currency remeasurement loss for the year ended December 31, 2007 was $61.2 million.

***Share-Based Compensation***

The Company accounts for share-based compensation at the grant date fair value of awards and recognizes the related expense over the vesting period of the award.

***Exploration and Drilling Costs***

Exploration expenditures are charged to operating costs as incurred, including costs related to drilling and study costs incurred to convert or upgrade mineral resources to reserves.

***Advance Stripping Costs***

Pre-production: At existing surface operations, additional pits may be added to increase production capacity in order to meet customer requirements. These expansions may require significant capital to purchase additional equipment, expand the workforce, build or improve existing haul roads and create the initial pre-production box cut to remove overburden (i.e., advance stripping costs) for new pits at existing operations. If these pits operate in a separate and distinct area of the mine, the costs associated with initially uncovering coal (i.e., advance stripping costs incurred for the initial box cuts) for production are capitalized and amortized over the life of the developed pit consistent with coal industry practices.

Post-production: Advance stripping costs related to post-production are expensed as incurred. Where new pits are routinely developed as part of a contiguous mining sequence, the Company expenses such costs as incurred. The development of a contiguous pit typically reflects the planned progression of an existing pit, thus maintaining production levels from the same mining area utilizing the same employee group and equipment.

***Reclassifications***

Certain amounts in prior periods have been reclassified to conform with the current year presentation, with no effect on previously reported net income or stockholders' equity.

**(2) DISCONTINUED OPERATIONS**

***Patriot Coal Corporation***

On October 31, 2007, the Company spun-off portions of its formerly Eastern U.S. Mining operations business segment through a dividend of all outstanding shares of Patriot Coal Corporation (Patriot), which is now an independent public company traded on the New York Stock Exchange (symbol PCX). The spin-off included eight company-operated mines, two joint venture mines, and numerous contractor operated mines serviced by eight coal preparation facilities along with 1.2 billion tons of proven and probable coal reserves.

Revenues from the spun-off operations are the result of supply agreements the Company entered into with Patriot to meet commitments under non-assignable pre-existing customer agreements sourced from Patriot mining operations. The Company makes no profit as part of these arrangements. The loss from discontinued operations for the year ended December 31, 2008 was primarily related to the write-off of a $19.4 million receivable related to excise taxes previously paid on export shipments produced from discontinued operations. As part of the Patriot spin-off, the Company retained a receivable for excise tax refunds on export shipments that had previously been ruled unconstitutional by the appellate court. The U.S. Supreme Court reversed the appellate court's ruling on April 15, 2008, and the Company recorded the charge to discontinued operations.

In October 2008, the Energy Improvement and Extension Act of 2008 was enacted, which contained provisions that allow for the refund of coal excise tax collected on coal exported from the U.S. between January 1, 1990 and the date of the legislation. The Company's claim for refund was approved by the Internal Revenue Service (IRS) in 2009. During the year ended December 31, 2009 the refund of approximately $35 million (net of income taxes) was recorded in "Income (loss) from discontinued operations, net of income taxes" in the consolidated statement of operations. Approximately $59 million was received during 2009 and is shown in "Net cash used in discontinued operations" as a component of cash flows from operating activities in the consolidated statements of cash flows.

***Baralaba***

In December 2008, the Company sold its Baralaba Mine, a non-strategic Australian mine, for $25.8 million of cash proceeds and an Australian dollar note receivable valued at approximately $8.7 million on December 31, 2008, resulting in a gain of $26.2 million. In 2008, the non-cash portion of this transaction was excluded from the investing section of the consolidated statement of cash flows.

### Chain Valley

In December 2009, the Company sold its Chain Valley Mine, a non-strategic Australian mine, and recorded a loss of $10.0 million in conjunction with the sale.

### Summary Financial Information

Operating results related to discontinued operations and assets held for sale were as follows:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Revenues: | | | |
| Patriot | **$275.7** | $431.2 | $1,024.5 |
| Baralaba | **–** | 18.8 | 22.1 |
| Chain Valley | **20.6** | 32.4 | 21.3 |
| Assets held for sale | **5.2** | 30.6 | 39.5 |
| Total | **$301.5** | $513.0 | $1,107.4 |
| Income (loss) before income taxes: | | | |
| Patriot | **$ 35.4** | $ (23.0) | $ (238.4) |
| Baralaba | **–** | 10.5 | (10.6) |
| Chain Valley | **(16.8)** | (3.5) | (6.9) |
| Assets held for sale | **(4.2)** | (44.6) | (13.5) |
| Total | **$ 14.4** | $ (60.6) | $ (269.4) |
| Income tax provision (benefit): | | | |
| Patriot | **$ 13.6** | $ (8.9) | $ (81.5) |
| Baralaba [1] | **–** | – | – |
| Chain Valley | **(2.8)** | (6.0) | (2.5) |
| Assets held for sale | **(1.5)** | (16.9) | (5.3) |
| Total | **$ 9.3** | $ (31.8) | $ (89.3) |
| Income (loss), net of income taxes: | | | |
| Patriot | **$ 21.8** | $ (14.1) | $ (156.9) |
| Baralaba | **–** | 10.5 | (10.6) |
| Chain Valley | **(14.0)** | 2.5 | (4.4) |
| Assets held for sale | **(2.7)** | (27.7) | (8.2) |
| Total | **$ 5.1** | $ (28.8) | $ (180.1) |

*(1) Income tax benefits associated with Baralaba's operating results were completely offset by valuation allowances recorded against the deferred tax assets created by the operating losses.*

Assets and liabilities related to discontinued operations were as follows:

| | 2009 | | | 2008 | | | |
|---|---|---|---|---|---|---|---|
| (Dollars in millions) | Patriot [1] | Assets held for sale | Total | Patriot [1] | Chain Valley | Assets held for sale | Total |
| **Assets** | | | | | | | |
| Current assets | | | | | | | |
| Other current assets | **$29.2** | **$ –** | **$29.2** | $51.0 | $ 3.1 | $ – | $ 54.1 |
| Total current assets | **29.2** | **–** | **29.2** | 51.0 | 3.1 | – | 54.1 |
| Noncurrent assets | | | | | | | |
| Investments and other assets | **–** | **11.4** | **11.4** | 4.9 | 17.8 | 12.6 | 35.3 |
| Total assets | **$29.2** | **$11.4** | **$40.6** | $55.9 | $20.9 | $12.6 | $ 89.4 |
| **Liabilities** | | | | | | | |
| Current liabilities | | | | | | | |
| Accounts payable and accrued expenses | **$40.6** | **$ –** | **$40.6** | $69.1 | $ 5.4 | $ – | $ 74.5 |
| Total current liabilities | **40.6** | **–** | **40.6** | 69.1 | 5.4 | – | 74.5 |
| Noncurrent liabilities | | | | | | | |
| Other noncurrent liabilities | **–** | **6.5** | **6.5** | 12.8 | 4.6 | 9.4 | 26.8 |
| Total liabilities | **$40.6** | **$ 6.5** | **$47.1** | $81.9 | $10.0 | $ 9.4 | $101.3 |

*(1) "Other current assets" included receivables from customers in relation to the supply agreements with Patriot and "Accounts payable and accrued expenses" included the amounts due to Patriot on these pass-through transactions.*

## (3) LABOR RELATIONS, RISK MANAGEMENT AND FAIR VALUE MEASUREMENTS

### Employees

As of December 31, 2009, the Company had approximately 7,300 employees, which included approximately 5,400 hourly employees. As of December 31, 2009, approximately 29% of the Company's hourly employees were represented by organized labor unions and generated 10% of its 2009 coal production. Relations with its employees and, where applicable, organized labor are important to the Company's success.

### U.S. Labor Relations

Hourly workers at the Company's Kayenta Mine in Arizona are represented by the United Mine Workers of America (UMWA) under the Western Surface Agreement, which is effective through September 2, 2013. This agreement covers approximately 7% of the Company's U.S. subsidiaries' hourly employees, who generated 4% of the Company's U.S. production during the year ended December 31, 2009.

Hourly workers at the Company's Willow Lake Mine in Illinois are represented by the International Brotherhood of Boilermakers under a labor agreement that expires April 15, 2011. This agreement covers approximately 9% of the Company's U.S. subsidiaries' hourly employees, who generated approximately 2% of the Company's U.S. production during the year ended December 31, 2009.

### Australian Labor Relations

The Australian coal mining industry is unionized and the majority of workers employed at the Company's Australian Mining operations are members of trade unions. The Construction Forestry Mining and Energy Union represents the Company's Australian subsidiary's hourly production and engineering employees, including those employed through contract mining relationships. All the Australian subsidiary's mine sites have enterprise bargaining agreements. The current labor agreement at the Company's Metropolitan Mine expires in June 2010; renegotiations for a new agreement will commence in the first quarter of 2010. The labor agreement for the Wambo Mine coal handling plant was renewed in 2008 and expires in 2011. The labor agreement for the Wambo Underground Mine was renewed in early 2009 and will expire in 2012. For the Wilkie Creek Mine (expired October 2009) and the North Goonyella Mine (expired May 2009), the Company has reached agreements in principle, with the vote of the unions and employees expected to take place in late February 2010.

### Risk Management - Non Coal Trading

The Company is exposed to various types of risk in the normal course of business, including fluctuations in commodity prices, interest rates and foreign currency exchange rates. These risks are actively monitored in an effort to ensure compliance with the risk management policies of the Company. In most cases, commodity price risk (excluding coal trading activities) related to the sale of coal is mitigated through the use of long-term, fixed-price contracts rather than financial instruments.

### Interest Rate Swaps

The Company is exposed to interest rate risk on its fixed rate and variable rate long-term debt. The interest rate risk associated with the fair value of the Company's fixed rate borrowings is managed using fixed-to-floating interest rate swaps to effectively convert a portion of the underlying cash flows on the debt into variable rate cash flows. The Company designates these swaps as fair value hedges, with the objective of hedging against changes in the fair value of the fixed rate debt that results from market interest rate changes. The interest rate risk associated with the Company's variable rate borrowings is managed using floating-to-fixed interest rate swaps. The Company designates these swaps as cash flow hedges, with the objective of reducing the variability of cash flows associated with market interest rate changes.

### Foreign Currency Risk

The Company is exposed to foreign currency exchange rate risk on Australian dollar expenditures made in its Australian Mining segment. This risk is managed by entering into forward contracts and options that the Company designates as cash flow hedges, with the objective of reducing the variability of cash flows associated with forecasted Australian dollar expenditures.

### Diesel Fuel and Explosives Hedges

The Company is exposed to commodity price risk associated with diesel fuel in the U.S. and Australia and explosives in the U.S. Explosives costs and a portion of the diesel fuel costs in Australia are included in the fees paid to the Company's contract miners. This risk is managed through the use of fixed price contracts, cost plus contracts and derivatives, primarily swaps. The Company has generally designated the swap contracts as cash flow hedges, with the objective of reducing the variability of cash flows associated with the forecasted purchase of diesel fuel and explosives.

### Notional Amounts and Fair Value

The following summarizes the Company's interest rate, foreign currency and commodity positions at December 31, 2009:

| | Notional Amount by Year of Maturity | | | | | | |
|---|---|---|---|---|---|---|---|
| | Total | 2010 | 2011 | 2012 | 2013 | 2014 | 2015 and thereafter |
| **Interest Rate Swaps** | | | | | | | |
| Fixed-to-floating (dollars in millions) | $ 50.0 | $ – | $ – | $ – | $ 50.0 | $ – | $ – |
| Floating-to-fixed (dollars in millions) | $ 120.0 | $ – | $120.0 | $ – | $ – | $ – | $ – |
| **Foreign Currency** | | | | | | | |
| A$:US$ hedge contracts (A$ millions) | $3,291.7 | $1,299.3 | $994.8 | $742.6 | $120.0 | $135.0 | $ – |
| **Commodity Contracts** | | | | | | | |
| Diesel fuel hedge contracts (million gallons) | 177.8 | 71.1 | 65.3 | 41.4 | – | – | – |
| U.S. explosives hedge contracts (million MMbtu) | 3.0 | 3.0 | – | – | – | – | – |

| | Account Classification by: Cash flow hedge | Fair value hedge | Economic hedge | Fair Value Asset (Liability) (Dollars in millions) |
|---|---|---|---|---|
| **Interest Rate Swaps** | | | | |
| Fixed-to-floating (dollars in millions) | $ – | $50.0 | $ – | $ 1.5 |
| Floating-to-fixed (dollars in millions) | $ 120.0 | $ – | $ – | $ (9.8) |
| **Foreign Currency** | | | | |
| A$:US$ hedge contracts (A$ millions) | $3,291.7 | $ – | $ – | $206.1 |
| **Commodity Contracts** | | | | |
| Diesel fuel hedge contracts (million gallons) | 177.8 | – | – | $ (22.2) |
| U.S. explosives hedge contracts (million MMbtu) | 3.0 | – | – | $ (4.8) |

### *Hedge Ineffectiveness*

The Company assesses both at inception and at least quarterly thereafter, whether the derivatives used in hedging activities are highly effective at offsetting the changes in the anticipated cash flows of the hedged item. The effective portion of the change in the fair value is recorded as a separate component of stockholders' equity until the hedged transaction impacts reported earnings, at which time gains and losses are reclassified to the consolidated statements of operations at the time of the recognition of the underlying hedged item. The ineffective portion of the derivative's change in fair value is recorded in the consolidated statements of operations. In addition, if the hedging relationship ceases to be highly effective, or it becomes probable that a forecasted transaction is no longer expected to occur, gains and losses on the derivative are recorded to the consolidated statements of operations.

A measure of ineffectiveness is inherent in hedging future diesel fuel purchases with derivative positions based on crude oil and refined petroleum products.

The Company's hedging of future explosives purchases also has an inherent measure of ineffectiveness as the derivative positions are primarily based on natural gas, which closely matches the contractual purchase price of explosives since price changes occur in a constant ratio of MMBtu per ton in the manufacture of explosives and generally carry a fixed surcharge.

With respect to the interest rate swaps, there was no hedge ineffectiveness recognized in the consolidated statements of operations for these instruments during the years ended December 31, 2009, 2008, or 2007.

The table below shows the classification and amounts of pre-tax gains and losses related to the Company's non-trading hedges during the year ended December 31, 2009:

| Financial Instrument (Dollars in millions) | Income Statement Classification Gains (Losses) - Realized | Gain (loss) recognized in income on non-designated derivatives [1] | Gain (loss) recognized in other comprehensive income on derivative (effective portion) | Gain (loss) reclassified from other comprehensive income into income (effective portion) | Gain (loss) reclassified from other comprehensive income into income (ineffective portion) |
|---|---|---|---|---|---|
| Interest rate swaps: | | | | | |
| Cash flow hedges | Interest expense | $ – | $ 0.2 | $ (5.5) | $ – |
| Diesel fuel hedge contracts: | | | | | |
| Cash flow hedges | Operating costs and expenses | – | 67.9 | (84.4) | 0.7 |
| Economic hedges | Operating costs and expenses | (0.6) | – | – | – |
| Explosives cash flow hedge contracts: | | | | | |
| Cash flow hedges | Operating costs and expenses | – | (2.4) | (13.9) | – |
| Economic hedges | Operating costs and expenses | (2.1) | – | – | – |
| Foreign currency cash flow hedge contracts | Operating costs and expenses | – | 458.0 | (30.8) | – |
| Total | | $(2.7) | $523.7 | $(134.6) | $0.7 |

[1] *Amounts relate to diesel fuel and explosives hedge derivatives that were de-designated in 2009.*

As of December 31, 2009, the classification and amount of derivatives presented on a gross basis are as follows:

| Financial Instrument (Dollars in millions) | Fair Value: Other Current Assets | Investments and Other Assets | Accounts Payable and Accrued Expenses | Other Noncurrent Liabilities |
|---|---|---|---|---|
| **Interest Rate Swaps:** | | | | |
| Fair value hedges | $ – | $ 1.5 | $ – | $ – |
| Cash flow hedges | – | – | – | 9.8 |
| Diesel fuel cash flow hedge contracts | 142.9 | 243.8 | 167.5 | 241.4 |
| Explosives cash flow hedge contracts | 15.9 | – | 20.7 | – |
| Foreign currency cash flow hedge contracts | 110.6 | 100.2 | 1.6 | 3.1 |
| Total | $269.4 | $345.5 | $189.8 | $254.3 |

The Company elected the trading exemption under GAAP for its coal trading transactions which allows for reduced disclosure since it is the Company's policy to include these instruments as a part of its trading book. For further information, see Risk Management - Coal Trading below.

### ***Risk Management - Coal Trading***

The Company engages in direct and brokered trading of coal, ocean freight and fuel-related commodities in over-the-counter markets (coal trading), some of which is subsequently exchange-cleared and some of which is bilaterally-cleared. Except those for which the Company has elected to apply a normal purchases and normal sales exception, all derivative coal trading contracts are accounted for on a fair value basis. For derivative trading contracts, the Company establishes fair values using bid/ask price quotations or other market assessments obtained from multiple, independent third-party brokers to value its trading positions from the over-the-counter market. Prices from these sources are then averaged to obtain trading position values. While the Company does not anticipate any decrease in the number of third-party brokers or market liquidity, such events could erode the quality of market information and therefore in valuing its market positions should the number of third-party brokers decrease or if market liquidity is reduced. For its exchange-cleared positions, the Company utilizes exchange-published settlement prices. See Note 5 for information related to the maturity and valuation of the Company's trading portfolio.

| *(Dollars in millions)* | ***2009*** |
|---|---|
| **Trading Revenue by Type of Instrument** | |
| Commodity swaps and options | **$176.5** |
| Physical commodity purchase/sale contracts | **85.0** |
| Total trading revenue | **$261.5** |

Trading revenues are recorded in "Other revenues" in the consolidated statements of operations and include realized and unrealized gains and losses on derivative instruments, including those under the normal purchases and normal sales exception.

### *Hedge Ineffectiveness – Coal Trading*

In some instances, the Company has designated an existing coal trading derivative as a hedge and, thus, the derivative has a non-zero fair value at hedge inception. The "off-market" nature of these derivatives, which is best described as an embedded financing element within the derivative, is a source of ineffectiveness. In other instances, the Company uses a coal trading derivative that settles at a different time or has a different location basis than the occurrence of the cash flow being hedged. These collectively yield ineffectiveness to the extent that the derivative hedge contract does not exactly offset changes in the fair value or expected cash flows of the hedged item.

### ***Nonperformance and Credit Risk***

The fair value of the Company's assets and liabilities reflect adjustments for nonperformance and credit risk. The concentration of nonperformance and credit risk is substantially with electric utilities, steel producers, energy producers and energy marketers. The Company's policy is to independently evaluate each customer's creditworthiness prior to entering into transactions and to regularly monitor the credit extended. If the Company engages in a transaction with a counterparty that does not meet its credit standards, the Company seeks to protect its position by requiring the counterparty to provide an appropriate credit enhancement. Also, when appropriate (as determined by its credit management function), the Company has taken steps to reduce its exposure to customers or counterparties whose credit has deteriorated and who may pose a higher risk of failure to perform under their contractual obligations. These steps include obtaining letters of credit or cash collateral, requiring prepayments for shipments or the creation of customer trust accounts held for the Company's benefit to serve as collateral in the event of a failure to pay or perform. To reduce its credit exposure related to trading and brokerage activities, the Company seeks to enter into netting agreements with counterparties that permit the Company to offset receivables and payables with such counterparties and, to the extent required, will post or receive margin amounts associated with exchange-cleared positions.

The Company conducts its various hedging activities related to foreign currency, interest rate, and fuel and explosives exposures with a variety of highly-rated commercial banks. In light of the recent turmoil in the financial markets the Company continues to closely monitor counterparty creditworthiness.

Certain of the Company's derivative instruments require the parties to provide additional performance assurances whenever a material adverse event jeopardizes one party's ability to perform under the instrument. In the event the Company were to sustain a material adverse event (using commercially reasonable standards), the counterparties could request collateralization on derivative instruments in net liability positions, which based on an aggregate fair value on December 31, 2009, could require the Company to post up to $83.8 million of collateral to its counterparties.

Certain of the Company's other derivative instruments require the parties to provide additional performance assurances whenever a credit downgrade occurs below a certain level as specified in each underlying contract. The terms of such instruments typically require additional collateralization on an incremental basis, which is commensurate with the severity of the credit downgrade. As of December 31, 2009, if a credit downgrade were to occur below a certain level, the Company's additional collateral requirements are estimated to be approximately $15.9 million (for which the Company currently has posted approximately $0.8 million) to its counterparties based on the aggregate fair value of all derivative instruments with such features that are in a net liability position.

The Company is required to post collateral on its exchange-settled positions for its entire net liability position, which was $18.1 million as of December 31, 2009. In addition, as of December 31, 2009, the Company has posted $29.7 million of collateral to meet the requirements of the respective exchanges (reflected in "Other current assets").

### *Fair Value Measurements*

The Company uses a three-level fair value hierarchy that categorizes assets and liabilities measured at fair value based on the observability of the inputs utilized in the valuation. These levels include: Level 1, inputs are quoted prices in active markets for the identical assets or liabilities; Level 2, inputs other than quoted prices included in Level 1 that are directly or indirectly observable through market-corroborated inputs; and Level 3, inputs are unobservable, or observable but cannot be market-corroborated, requiring the Company to make assumptions about pricing by market participants.

The following tables set forth the hierarchy of the Company's net financial asset (liability) positions for which fair value is measured on a recurring basis:

| | 2009 | | | |
|---|---|---|---|---|
| *(Dollars in millions)* | *Level 1* | *Level 2* | *Level 3* | *Total* |
| Commodity swaps and options – coal trading activities | **$(1.7)** | **$ 80.7** | **$ –** | **$ 79.0** |
| Commodity swaps and options – other than coal | **–** | **(27.0)** | **–** | **(27.0)** |
| Physical commodity purchase/sale contracts – coal trading activities | **–** | **70.2** | **17.0** | **87.2** |
| Interest rate swaps | **–** | **(8.3)** | **–** | **(8.3)** |
| Foreign currency hedge contracts | **–** | **206.1** | **–** | **206.1** |
| Total net financial assets (liabilities) | **$(1.7)** | **$321.7** | **$17.0** | **$337.0** |

| | 2008 | | | |
|---|---|---|---|---|
| *(Dollars in millions)* | *Level 1* | *Level 2* | *Level 3* | *Total* |
| Commodity swaps and options – coal trading activities | $(17.0) | $233.7 | $(1.1) | $215.6 |
| Commodity swaps and options – other than coal | – | (194.7) | – | (194.7) |
| Physical commodity purchase/sale contracts – coal trading activities | – | 104.1 | 38.9 | 143.0 |
| Interest rate swaps | – | (9.3) | – | (9.3) |
| Foreign currency hedge contracts | – | (283.8) | – | (283.8) |
| Total net financial assets (liabilities) | $(17.0) | $(150.0) | $37.8 | $(129.2) |

For Level 1 and 2 financial assets and liabilities, the Company utilizes both direct and indirect observable price quotes, including LIBOR yield curves, New York Mercantile Exchange and Intercontinental Exchange indices (ICE), broker quotes, published indices, and other market quotes. Below is a summary of the Company's valuation techniques for Level 1 and 2 financial assets and liabilities:

- Commodity swaps and options – coal trading activities: generally valued based on unadjusted quoted prices in active markets (Level 1) or a valuation that is corroborated by the use of market-based pricing (Level 2).
- Commodity swaps and options – other than coal: generally valued based on a valuation that is corroborated by the use of market-based pricing (Level 2).
- Physical commodity purchase/sale contracts – coal trading activities: purchases and sales at locations with significant market activity corroborated by market-based information (Level 2).
- Interest rate swaps: valued based on modeling observable market data and corroborated with statements from counterparties (Level 2).
- Foreign currency hedge contracts: valued utilizing inputs obtained in quoted public markets (Level 2).

Commodity swaps and options and physical commodity purchase/sale contracts transacted in less liquid markets or contracts, such as long-term arrangements with limited price availability were classified in Level 3. These instruments or contracts are valued based on quoted inputs from brokers or counterparties, or reflect methodologies that consider historical relationships among similar commodities to derive the Company's best estimate of fair value. The Company has consistently applied these valuation techniques in all periods presented, and believes it has obtained the most accurate information available for the types of derivative contracts held.

The following table summarizes the changes in the Company's recurring Level 3 net financial assets:

| *(Dollars in millions)* | *2009* | *2008* |
|---|---|---|
| Beginning of period | **$ 37.8** | $128.7 |
| Total gains or losses (realized/unrealized): | | |
| Included in earnings | **(2.9)** | (9.8) |
| Included in other comprehensive income | **(1.6)** | 3.4 |
| Purchases, issuances and settlements | **(20.5)** | (58.8) |
| Net transfers in (out) | **4.2** | (25.7) |
| End of period | **$ 17.0** | $ 37.8 |

The following table summarizes the changes in unrealized gains (losses) relating to Level 3 net financial assets held both as of the beginning and the end of the period:

| *(Dollars in millions)* | *2009* | *2008* |
|---|---|---|
| Changes in unrealized gains (losses) [(1)] | **$15.6** | $(34.8) |

*(1) Within the consolidated statements of operations for the periods presented, unrealized gains and losses from Level 3 items are combined with unrealized gains and losses on positions classified in Level 1 or 2, as well as other positions that have been realized during the applicable periods.*

### *Fair Value – Other Financial Instruments*

The following methods and assumptions were used by the Company in estimating fair values for other financial instruments as of December 31, 2009 and 2008:

- Cash and cash equivalents, accounts receivable and accounts payable and accrued expenses have carrying values which approximate fair value due to the short maturity or the financial nature of these instruments.
- Long-term debt fair value estimates are based on observed prices for securities with an active trading market when available, and otherwise on estimated borrowing rates to discount the cash flows to their present value. The carrying amounts of the 7.875% Senior Notes due 2026 and the Convertible Junior Subordinated Debentures due 2066 are net of the respective unamortized note discounts.

The carrying amounts and estimated fair values of the Company's debt are summarized as follows:

| | 2009 | | 2008 | |
|---|---|---|---|---|
| *(Dollars in millions)* | ***Carrying Amount*** | ***Estimated Fair Value*** | *Carrying Amount* | *Estimated Fair Value* |
| Long-term debt | **$2,752.3** | **$2,828.8** | $2,793.6 | $2,472.1 |

## (4) RESOURCE MANAGEMENT AND OTHER COMMERCIAL EVENTS

In 2008, the Company sold approximately 58 million tons of non-strategic coal reserves and surface lands located in Kentucky for $21.5 million cash proceeds and a note receivable of $54.9 million, and recognized a gain of $54.0 million. The note receivable was paid in two installments, $30.0 million of which was received in December 2008 with the balance received in June 2009. The non-cash portion of this transaction was excluded from the investing section of the consolidated statement of cash flows until the cash was received.

In 2007, the Company sold approximately 172 million tons of coal reserves and surface lands to the Prairie State Energy Campus (Prairie State) equity partners. The Company recognized a gain totaling $26.4 million and received $114.3 million in cash proceeds associated with this transaction. See Note 19 for additional information regarding Prairie State.

In 2007, the Company exchanged oil and gas rights and assets in more than 860,000 acres in the Illinois Basin, West Virginia, New Mexico and the Powder River Basin for coal reserves in West Virginia and Kentucky and $15.0 million in cash proceeds. The Company's subsidiaries, including one subsidiary now owned by Patriot, received approximately 40 million tons of coal reserves. Based on the fair value of the coal reserves received, the Company recognized a $50.5 million gain on the exchange. The non-cash portion of this transaction was excluded from the investing section of the consolidated statement of cash flows.

## (5) ASSETS AND LIABILITIES FROM COAL TRADING ACTIVITIES

The fair value of assets and liabilities from coal trading activities is set forth below:

| (Dollars in millions) | 2009 Gross Basis | 2009 Net Basis | 2008 Gross Basis | 2008 Net Basis |
|---|---|---|---|---|
| Assets from coal trading activities | **$ 949.8** | **$ 276.8** | $ 1,969.7 | $ 662.8 |
| Liabilities from coal trading activities | **(779.3)** | **(110.6)** | (1,548.5) | (304.2) |
| Subtotal | **170.5** | **166.2** | 421.2 | 358.6 |
| Net margin held | **(4.3)** | **–** | (62.6) | – |
| Net value of coal trading positions | **$ 166.2** | **$ 166.2** | $ 358.6 | $ 358.6 |

As of December 31, 2009, forward contracts made up 53% and 65% of the Company's trading assets and liabilities, respectively; financial swaps represent most of the remaining balances. The net fair value of coal trading positions designated as cash flow hedges of anticipated future sales was an asset of $93.0 million as of December 31, 2009 and an asset of $220.4 million as of December 31, 2008. The net value of trading positions, including those designated as hedges of future cash flows, represents the fair value of the trading portfolio.

As of December 31, 2009, the estimated future realization of the value of the Company's trading portfolio was as follows:

| Year of Expiration | Percentage of Portfolio Total |
|---|---|
| 2010 | 46% |
| 2011 | 51% |
| 2012 | 3% |
| | 100% |

At December 31, 2009, 73% of the Company's credit exposure related to coal trading activities with investment grade counterparties and 27% with non-investment grade counterparties.

## (6) ACCOUNTS RECEIVABLE SECURITIZATION

The Company has an accounts receivable securitization program (securitization program) through its wholly-owned, bankruptcy-remote subsidiary (Seller). Under the program, the Company contributes a pool of eligible trade receivables to the Seller, which then sells, without recourse, to a multi-seller, asset-backed commercial paper conduit (Conduit). Purchases by the Conduit are financed with the sale of highly rated commercial paper. The Company utilizes proceeds from the sale of its accounts receivable as an alternative to other forms of debt, effectively reducing its overall borrowing costs. The funding cost of the securitization program was $4.0 million, $10.8 million and $11.2 million for the years ended December 31, 2009, 2008 and 2007, respectively and is included in interest expense in the consolidated statements of operations. The Company continues to service the sold trade receivables but does not receive a servicing fee. The securitization program was renewed in May 2009, and amended in December 2009 and January 2010, and extends to May 2012, while the letter of credit commitment that supports the commercial paper facility underlying the securitization program must be renewed annually.

The securitization transactions have been recorded as sales, with those accounts receivable sold to the Conduit removed from the consolidated balance sheets. The amount of interests in accounts receivables sold to the Conduit was $254.6 million as of December 31, 2009 and $275.0 million as of December 31, 2008. The $20.4 million decrease in the securitization program for the year ended December 31, 2009 is reflected in cash flows from operating activities in the consolidated statements of cash flows. There was no change in the facility usage during the year ended December 31, 2008.

The Seller is a separate legal entity whose assets are available first and foremost to satisfy the claims of its creditors. Eligible receivables, as defined in the securitization agreement, consist of trade receivables from most of the Company's U.S. subsidiaries, and are reduced for certain items such as past due balances and concentration limits. Of the eligible pool of receivables contributed to the Seller, only a portion of the pool is sold to the Conduit. The Company continues to own $9.4 million of receivables as of December 31, 2009, which represents collateral supporting the securitization program. The Seller's interest in these receivables is subordinate to the Conduit's interest in the event of default under the securitization agreement. If the Company defaulted under the securitization agreement or if its pool of eligible trade receivables decreased significantly, the Company could be prohibited from selling any additional receivables in the future under the securitization agreement.

On January 25, 2010, the receivables purchase agreement for the accounts receivable securitization program was amended and restated to add a second multi-seller asset-backed commercial paper conduit as a purchaser.

## (7) EARNINGS PER SHARE

As discussed in Note 1, the Company uses the two-class method to compute basic and diluted EPS for all periods presented. The following illustrates the earnings allocation method utilized in the calculation of basic and diluted EPS.

| (In millions, except per share amounts) | 2009 | 2008 | 2007 |
|---|---|---|---|
| **Basic earnings per share:** | | | |
| Income from continuing operations, net of income taxes | **$457.9** | $987.9 | $ 441.6 |
| Less: Net income (loss) attributable to noncontrolling interests | **14.8** | 6.2 | (2.3) |
| Income from continuing operations attributable to common stockholders before allocation of earnings to participating securities | **443.1** | 981.7 | 443.9 |
| Less: Earnings allocated to participating securities | **(2.9)** | (5.5) | (1.2) |
| Income from continuing operations attributable to common stockholders | **440.2** | 976.2 | 442.7 |
| Income (loss) from discontinued operations, net of income taxes | **5.1** | (28.8) | (180.1) |
| Net income attributable to common stockholders | **$445.3** | $947.4 | $ 262.6 |
| **Diluted earnings per share:** | | | |
| Income from continuing operations attributable to common stockholders before allocation of earnings to participating securities | **$443.1** | $981.7 | $ 443.9 |
| Less: Earnings allocated to participating securities | **(2.9)** | (5.5) | (1.2) |
| Income from continuing operations attributable to common stockholders before the reallocation of the earnings of participating securities | **440.2** | 976.2 | 442.7 |
| Reallocation of the earnings of participating securities | **–** | – | – |
| Income from continuing operations attributable to common stockholders | **440.2** | 976.2 | 442.7 |
| Income (loss) from discontinued operations, net of income taxes | **5.1** | (28.8) | (180.1) |
| Net income attributable to common stockholders | **$445.3** | $947.4 | $ 262.6 |
| Weighted average shares outstanding - basic | **265.5** | 268.9 | 264.1 |
| Dilutive impact of share-based compensation (1) | **2.0** | 1.8 | 4.5 |
| Weighted average shares outstanding - diluted (2) | **267.5** | 270.7 | 268.6 |
| Basic earnings per share attributable to common stockholders: | | | |
| Income from continuing operations | **$ 1.66** | $ 3.63 | $ 1.67 |
| Income (loss) from discontinued operations | **0.02** | (0.11) | (0.68) |
| Net income | **$ 1.68** | $ 3.52 | $ 0.99 |
| Diluted earnings per share attributable to common stockholders: | | | |
| Income from continuing operations | **$ 1.64** | $ 3.60 | $ 1.64 |
| Income (loss) from discontinued operations | **0.02** | (0.10) | (0.67) |
| Net income | **$ 1.66** | $ 3.50 | $ 0.97 |

*(1) Includes the dilutive impact of stock options, restricted stock awards, deferred stock units, employee stock purchase plan and performance units.*

*(2) Weighted average shares outstanding excludes anti-dilutive shares totaling 0.2 million, 0.1 million and 0.2 million for the years ended December 31, 2009, 2008 and 2007, respectively.*

## (8) INVENTORIES

Inventories consisted of the following:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Materials and supplies | **$ 106.5** | $109.6 |
| Raw coal | **80.5** | 22.7 |
| Saleable coal | **138.1** | 143.9 |
| Total | **$325.1** | $276.2 |

## (9) LEASES

The Company leases equipment and facilities under various noncancelable lease agreements. Certain lease agreements require the maintenance of specified ratios and contain restrictive covenants which limit indebtedness, subsidiary dividends, investments, asset sales and other Company actions. Rental expense under operating leases was $127.8 million, $121.3 million and $104.6 million for the years ended December 31, 2009, 2008 and 2007, respectively. The gross value of property, plant, equipment and mine development assets under capital leases was $98.4 million and $108.6 million as of December 31, 2009 and 2008, respectively, related primarily to the leasing of mining equipment. The accumulated depreciation for these items was $31.0 million and $27.6 million at December 31, 2009 and 2008, respectively.

The Company also leases coal reserves under agreements that require royalties to be paid as the coal is mined. Certain agreements also require minimum annual royalties to be paid regardless of the amount of coal mined during the year. Total royalty expense was $439.4 million, $506.4 million and $338.6 million for the years ended December 31, 2009, 2008 and 2007, respectively.

A substantial amount of the coal mined by the Company is produced from mineral reserves leased from the owner. One of the major lessors is the U.S. government, from which the Company leases substantially all of the coal it mines in Wyoming and Colorado under terms set by Congress and administered by the U.S. Bureau of Land Management. These leases are generally for an initial term of ten years but may be extended by diligent development and mining of the reserves until all economically recoverable reserves are depleted. The Company has met the diligent development requirements for substantially all of these federal leases either directly through production or by including the lease as a part of a logical mining unit with other leases upon which development has occurred. Annual production on these federal leases must total at least 1.0% of the original amount of coal in the entire logical mining unit. In addition, royalties are payable monthly at a rate of 12.5% of the gross realization from the sale of the coal mined using surface mining methods and at a rate of 8.0% of the gross realization for coal produced using underground mining methods. The Company also leases coal reserves in Arizona from The Navajo Nation and the Hopi Tribe under leases that are administered by the U.S. Department of the Interior. These leases expire

upon exhaustion of the leased reserves or upon the permanent ceasing of all mining activities on the related reserves as a whole. The royalty rates are also generally based upon a percentage of the gross realization from the sale of coal. These rates are subject to redetermination every ten years under the terms of the leases. The remainder of the leased coal is generally leased from state governments, land holding companies and various individuals. The duration of these leases varies greatly. Typically, the lease terms are automatically extended as long as active mining continues. Royalty payments are generally based upon a specified rate per ton or a percentage of the gross realization from the sale of the coal.

Mining and exploration in Australia is generally carried on under leases or licenses granted by state governments. Mining leases are typically for an initial term of up to 21 years (but which may be renewed) and contain conditions relating to such matters as minimum annual expenditures, restoration and rehabilitation. Royalties are paid to the state government as a percentage of sale prices. Generally landowners do not own the mineral rights or have the ability to grant rights to mine those minerals. These rights are retained by state governments. Compensation is payable to landowners for loss of access to the land, and the amount of compensation can be determined by agreement or arbitration. Surface rights are typically acquired directly from landowners and, in the absence of agreement, there is an arbitration provision in the mining law.

Future minimum lease and royalty payments as of December 31, 2009 are as follows:

| *(Dollars in millions)* | *Capital Leases* | *Operating Leases* | *Coal Lease and Royalty Obligations* |
|---|---|---|---|
| 2010 | $15.1 | $ 96.4 | $11.3 |
| 2011 | 15.1 | 87.4 | 9.0 |
| 2012 | 15.1 | 66.2 | 7.8 |
| 2013 | 23.0 | 56.6 | 8.3 |
| 2014 | 12.0 | 43.7 | 6.7 |
| 2015 and thereafter | – | 117.8 | 36.8 |
| Total minimum lease payments | $80.3 | $468.1 | $79.9 |
| Less interest | 12.8 | | |
| Present value of minimum capital lease payments | $67.5 | | |

As of December 31, 2009, certain of the Company's lease obligations were secured by outstanding surety bonds totaling $116.3 million.

## (10) ACCOUNTS PAYABLE AND ACCRUED EXPENSES

Accounts payable and accrued expenses consisted of the following:

| *(Dollars in millions)* | **2009** | 2008 |
|---|---|---|
| Trade accounts payable | **$ 387.6** | $ 427.2 |
| Accrued taxes other than income | **172.3** | 170.7 |
| Other accrued expenses | **160.0** | 127.0 |
| Accrued payroll and related benefits | **135.0** | 120.1 |
| Income taxes payable | **80.7** | 142.7 |
| Accrued health care | **78.7** | 82.5 |
| Accrued royalties | **51.1** | 77.7 |
| Accrued interest | **31.7** | 31.1 |
| Commodity and foreign currency hedge contracts | **29.4** | 261.1 |
| Workers' compensation obligations | **8.7** | 8.7 |
| Accrued environmental | **7.9** | 7.6 |
| Other accrued benefits | **4.0** | 4.1 |
| Liabilities associated with discontinued operations | **40.6** | 69.1 |
| Current liabilities associated with assets held for sale | **–** | 5.4 |
| Total accounts payable and accrued expenses | **$1,187.7** | $1,535.0 |

## (11) INCOME TAXES

Income from continuing operations before income taxes consisted of the following:

| *(Dollars in millions)* | **2009** | 2008 | 2007 |
|---|---|---|---|
| U.S. | **$281.4** | $ 185.2 | $296.1 |
| Non U.S. | **370.3** | 994.1 | 74.8 |
| Total | **$651.7** | $1,179.3 | $370.9 |

Total income tax provision (benefit) consisted of the following:

| *(Dollars in millions)* | **2009** | 2008 | 2007 |
|---|---|---|---|
| Current: | | | |
| U.S. federal | **$ (0.7)** | $ – | $ – |
| Non U.S. | **61.7** | 224.7 | 28.9 |
| State | **1.7** | – | 0.2 |
| Total current | **62.7** | 224.7 | 29.1 |
| Deferred: | | | |
| U.S. federal | **56.0** | 47.1 | (139.3) |
| Non U.S. | **74.4** | (81.7) | 46.7 |
| State | **0.7** | 1.3 | (7.2) |
| Total deferred | **131.1** | (33.3) | (99.8) |
| Total provision (benefit) | **$193.8** | $191.4 | $ (70.7) |

The income tax rate differed from the U.S. federal statutory rate as follows:

| *(Dollars in millions)* | **2009** | 2008 | 2007 |
|---|---|---|---|
| Federal statutory rate | **$228.1** | $412.7 | $ 129.8 |
| Excess depletion | **(44.0)** | (40.1) | (55.3) |
| Foreign earnings rate differential | **(83.6)** | (119.7) | (13.5) |
| Remeasurement of foreign deferred taxes | **74.4** | (65.2) | 56.0 |
| State income taxes, net of U.S. federal tax benefit | **3.4** | (1.6) | 0.3 |
| Tax credits | **(12.2)** | (12.6) | (24.3) |
| Changes in valuation allowance | **17.3** | (44.2) | (175.7) |
| Changes in tax reserves | **5.9** | 34.4 | 4.1 |
| Other, net | **4.5** | 27.7 | 7.9 |
| Total provision (benefit) | **$193.8** | $191.4 | $ (70.7) |

The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and liabilities consisted of the following:

| *(Dollars in millions)* | **2009** | 2008 |
|---|---|---|
| Deferred tax assets: | | |
| Tax credits and loss carryforwards | **$ 557.1** | $ 785.9 |
| Postretirement benefit obligations | **474.7** | 403.9 |
| Intangible tax asset and purchased contract rights | **30.9** | 58.1 |
| Accrued reclamation and mine closing liabilities | **57.0** | 46.1 |
| Accrued long-term workers' compensation liabilities | **23.1** | 12.6 |
| Employee benefits | **80.3** | 56.2 |
| Financial guarantee | **20.1** | 23.9 |
| Others | **39.5** | 56.5 |
| Total gross deferred tax assets | **1,282.7** | 1,443.2 |
| Deferred tax liabilities: | | |
| Property, plant, equipment and mine development, leased coal interests and advance royalties, principally due to differences in depreciation, depletion and asset writedowns | **1,221.0** | 1,154.2 |
| Unamortized discount on Convertible Junior Subordinated Debentures | **139.6** | 139.9 |
| Hedge activities | **29.2** | 35.3 |
| Investments and other assets | **64.8** | 75.9 |
| Total gross deferred tax liabilities | **1,454.6** | 1,405.3 |
| Valuation allowance | **(87.2)** | (57.0) |
| Net deferred tax liability | **$ (259.1)** | $ (19.1) |
| Deferred taxes are classified as follows: | | |
| Current deferred income taxes | **$ 40.0** | $ 1.7 |
| Noncurrent deferred income taxes | **(299.1)** | (20.8) |
| Net deferred tax liability | **$ (259.1)** | $ (19.1) |

The Company's tax credits and loss carryforwards included alternative minimum tax (AMT) and general business credits of $73.3 million and $62.4 million, U.S. net operating loss (NOL) carryforwards of $392.1 million and $653.5 million and foreign loss carryforwards of $91.7 million and $70.0 million as of December 31, 2009 and 2008, respectively. The AMT credits and foreign NOL and capital loss carryforwards have no expiration date and the U.S. NOL carryforwards begin to expire in the year 2025. The Company evaluated and assessed the expected near-term utilization of NOLs, future book and taxable income,

available tax strategies and the overall deferred tax position to determine the appropriate amount and timing of valuation allowance adjustments. Of the $17.3 million change in the valuation allowance, the largest component of the 2009 assessment was a $15.7 million increase of a valuation allowance on AMT credits. Significant reductions of valuation allowance were made to foreign NOLs during the 2008 assessment and on U.S. NOL carryforwards during the 2007 assessments. The remaining valuation allowance at December 31, 2009 of $87.2 million represents a reserve for AMT credits and certain foreign deferred tax assets.

The total amount of the net unrecognized tax benefits was $109.2 million ($113.2 million gross) at December 31, 2009 and was $176.9 million ($186.3 million gross) at December 31, 2008. The amount of the Company's gross unrecognized tax benefits has decreased by $73.1 million since January 1, 2009 primarily as a result of the Company's IRS audit for the 2005 and 2006 tax years. The corresponding adjustment was a reduction of the deferred tax asset associated with net operating losses. A reconciliation of the beginning and ending amount of gross unrecognized tax benefits is as follows (dollars in millions):

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Balance at beginning of period | **$186.3** | $152.6 | $144.0 |
| Additions for current year tax positions | **2.7** | 30.3 | 4.0 |
| Additions for prior year positions | **15.7** | 3.4 | 4.6 |
| Reductions for settlements with tax authorities | **(88.5)** | – | – |
| Reductions for expirations of statute of limitations | **(3.0)** | – | – |
| Balance at end of period | **$113.2** | $186.3 | $152.6 |

The amount of the net unrecognized tax benefits that, if recognized, would directly affect the effective tax rate is $109.2 million. However, $10.4 million would generate a deferred tax asset for state NOL carryforwards that would more likely than not be offset by a valuation allowance. The Company does not expect any significant changes to its net unrecognized tax benefits within 12 months of this reporting date.

The Company's federal income tax returns are under examination by the IRS for the 2005 and 2006 income tax years. The IRS has issued the Company notices of proposed adjustments to decrease the Company's net operating losses associated with the liquidation of an insolvent subsidiary and interest income accrued by a foreign subsidiary. The Company believes its position regarding these matters is supported by applicable valuation methodology, tax laws and existing Treasury regulations. The Company and the IRS have agreed to proceed to an alternative dispute resolution program (Fast Track Settlement) which could facilitate a settlement within 120 days (expected to be May 2010); and, provided a settlement is reached in this process, additional changes could occur to the amount of unrecognized tax benefits. However, the Company does not expect any changes to have a material impact on its financial position or results of operations.

If a settlement is not reached under the Fast Track Settlement process, the Company will begin the formal IRS appeals process to resolve any outstanding issues which could take two or more years to complete. Should the IRS positions ultimately be sustained at the conclusion of the appeals process, additional income tax charges would be required to the extent the Company's net operating loss carryforwards are reduced.

The Company recognizes interest and penalties accrued related to unrecognized tax benefits in its income tax provision. The Company has recognized $2.8 million of interest for the year ended December 31, 2009. The Company had $6.4 million and $3.6 million of accrued interest related to uncertain tax positions at December 31, 2009 and 2008, respectively. The Company has considered the application of penalties on its unrecognized tax benefits and determined, based upon several factors, including the existence of NOL carryforwards, that no accrual of penalties is required.

The Company's federal income tax returns for 1999 through 2001, 2003 through 2004 and 2007 through 2008 remain subject to examination by the IRS. The Company's state income tax returns for the tax years 1991 and beyond remain subject to examination by various state taxing authorities. The Company's foreign income tax returns for the tax years 2003 and beyond remain subject to examination by various foreign taxing authorities.

The total amount of undistributed earnings of foreign subsidiaries for income tax purposes was approximately $1.4 billion at December 31, 2009 and $1.2 billion at December 31, 2008. The Company has not provided deferred taxes on foreign earnings of $1.3 billion for 2009 and $1.1 billion for 2008 because such earnings were intended to be indefinitely reinvested outside the U.S. Should the Company repatriate all of these earnings, a one-time income tax charge to the Company's consolidated results of operations of up to $466.0 million could occur.

The following table summarizes the Company's tax payments:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| U.S. – federal | **$ –** | $ – | $ 3.0 |
| U.S. – state and local | **0.9** | – | 1.2 |
| Non U.S. | **169.7** | 65.8 | 80.0 |
| Total tax payments | **$170.6** | $65.8 | $84.2 |

## (12) LONG-TERM DEBT

The Company's total indebtedness as of December 31, 2009 and 2008 consisted of the following:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Term Loan under Senior Unsecured Credit Facility | **$ 490.3** | $ 490.3 |
| Convertible Junior Subordinated Debentures due December 2066 | **371.5** | 369.9 |
| 7.375% Senior Notes due November 2016 | **650.0** | 650.0 |
| 6.875% Senior Notes due March 2013 | **650.0** | 650.0 |
| 7.875% Senior Notes due November 2026 | **247.1** | 247.0 |
| 5.875% Senior Notes due March 2016 | **218.1** | 218.1 |
| 6.84% Series C Bonds due December 2016 | **33.0** | 43.0 |
| 6.34% Series B Bonds due December 2014 | **15.0** | 18.0 |
| 6.84% Series A Bonds due December 2014 | **–** | 10.0 |
| Capital lease obligations | **67.5** | 81.2 |
| Fair value hedge adjustment | **8.4** | 15.1 |
| Other | **1.4** | 1.0 |
| Total | **$2,752.3** | $2,793.6 |

### *Senior Unsecured Credit Facility*

The Senior Unsecured Credit Facility provides a $1.8 billion Revolving Credit Facility (the Revolver) and a $950.0 million Term Loan Facility (the Term Loan) and matures on September 15, 2011. The Revolver is intended to accommodate working capital needs, letters of credit, and other general corporate purposes, and includes a $50.0 million sub-facility available for same-day swingline loan borrowings. As of December 31, 2009, the Company had $315.7 million of letters of credit outstanding under the Revolver, with a remaining available borrowing capacity of approximately $1.5 billion.

Loans under the facility are available to the Company in U.S. dollars, with a sub-facility under the Revolver available in Australian dollars, pounds sterling and euros. Letters of credit under the Revolver are available to the Company in U.S. dollars with a sub-facility available in Australian dollars, pounds sterling and euros. The interest rate payable on the Revolver and the Term Loan is based on a pricing grid tied to the Company's leverage ratio, as defined in the Third Amended and Restated Credit Agreement. The interest rate payable on the Revolver and the Term Loan is currently LIBOR plus 0.75%, which was 1.0% at December 31, 2009.

Under the Senior Unsecured Credit Facility, the Company must comply with certain financial covenants on a quarterly basis including a minimum interest coverage ratio and a maximum leverage ratio. The financial covenants also place limitations on the Company's investments in joint ventures, unrestricted subsidiaries, indebtedness of non-loan parties and the imposition of liens on Company assets.

### *Convertible Junior Subordinated Debentures*

As of December 31, 2009, the Company had $732.5 million aggregate principal outstanding of Convertible Junior Subordinated Debentures (the Debentures) that generally require interest to be paid semiannually at a rate of 4.75% per year. The Company may elect to, and to the extent that a mandatory trigger event (as defined in the indenture governing the Debentures) has occurred and is continuing will be required to, defer interest payments on the Debentures. After five years of deferral at the Company's option, or upon the occurrence of a mandatory trigger event, the Company generally must sell warrants or preferred stock with specified characteristics and use the funds from that sale to pay deferred interest, subject to certain limitations. In no event may the Company defer payments of interest on the Debentures for more than 10 years.

The Debentures are convertible at any time on or prior to December 15, 2036 if any of the following conditions occur: (i) the Company's closing common stock price exceeds 140% of the then applicable conversion price for the Debentures (currently $81.75 per share) for at least 20 of the final 30 trading days in any quarter; (ii) a notice of redemption is issued with respect to the Debentures; (iii) a change of control, as defined in the indenture governing the Debentures; (iv) satisfaction of certain trading price conditions; and (v) other specified corporate transactions described in the indenture governing the Debentures. In addition, the Debentures are convertible at any time after December 15, 2036 to December 15, 2041, the scheduled maturity date. In the case of conversion following a notice of redemption or upon a non-stock change of control, as defined in the indenture governing the Debentures, holders may convert their Debentures into cash in the amount of the principal amount of their Debentures and shares of the Company's common stock for any conversion value in excess of the principal amount. In all other conversion circumstances, holders will receive perpetual preferred stock (see Note 16) with a liquidation preference equal to the principal amount of their Debentures, and any conversion value in excess of the principal amount will be settled with the Company's common stock. As a result of the Patriot spin-off and a change in the Company's dividend distribution rate, the conversion rate was adjusted. The current conversion rate is 17.1244 shares of common stock per $1,000 principal amount of Debentures effective February 8, 2010. This adjusted conversion rate represents a conversion price of approximately $58.40.

The Debentures are not subject to redemption prior to December 20, 2011. Between December 20, 2011 and December 19, 2036 the Company may redeem the Debentures, in whole or in part, if for at least 20 out of the 30 consecutive trading days immediately prior to the date on which notice of redemption is given, the Company's closing common stock price has exceeded 130% of the then applicable conversion price for the Debentures. On or after December 20, 2036, whether or not the redemption condition is satisfied, the Company may redeem the Debentures, in whole or in part. The Company may not redeem any Debentures unless (i) all accrued

and unpaid interest on the Debentures has been paid in full on or prior to the redemption date and (ii) if any perpetual preferred stock is outstanding, the Company has first given notice to redeem the perpetual preferred stock in the same proportion as the redemption of the Debentures. Any redemption of the Debentures will be at a cash redemption price of 100% of the principal amount of the Debentures to be redeemed, plus accrued and unpaid interest to the date of redemption.

On December 15, 2041, the scheduled maturity date, the Company will use commercially reasonable efforts, subject to the occurrence of a market disruption event, as defined in the indenture governing the Debentures, to issue securities of equivalent equity content in an amount sufficient to pay the principal amount of the Debentures, together with accrued and unpaid interest. At the final maturity date of the Debentures on December 15, 2066, the entire principal amount will become due and payable, together with accrued and unpaid interest.

In connection with the issuance of the Debentures, the Company entered into a Capital Replacement Covenant (the CRC). Pursuant to the CRC, the Company covenanted for the benefit of holders of covered debt, as defined in the CRC (currently the Company's 7.875% Senior Notes, issued in the aggregate principal amount of $250.0 million), that neither the Company nor any of its subsidiaries shall repay, redeem or repurchase all or any part of the Debentures on or after December 15, 2041 and prior to December 15, 2046, except to the extent that the total repayment, redemption or repurchase price does not exceed the sum of: (i) 400% of the Company's net cash proceeds from the sale of its common stock and rights to acquire its common stock (including common stock issued pursuant to the Company's dividend reinvestment plan or employee benefit plans); (ii) the Company's net cash proceeds from the sale of its mandatorily convertible preferred stock, as defined in the CRC, or debt exchangeable for equity, as defined in the CRC; and (iii) the Company's net cash proceeds from the sale of other replacement capital securities, as defined in the CRC, in each case, during the six months prior to the notice date for the relevant payment, redemption or repurchase.

The Debentures are unsecured obligations of the Company, ranking junior to all existing and future senior and subordinated debt (excluding trade accounts payable or accrued liabilities arising in the ordinary course of business) except for any future debt that ranks equal to or junior to the Debentures. The Debentures will rank equal in right of payment with the Company's obligations to trade creditors. Substantially all of the Company's existing indebtedness is senior to the Debentures. In addition, the Debentures will be effectively subordinated to all indebtedness of the Company's subsidiaries. The indenture governing the Debentures places no limitation on the amount of additional indebtedness that the Company or any of the Company's subsidiaries may incur.

As discussed in Note 1, the Company adopted an accounting standard such that the Company separately accounts for the liability and equity components of the Debentures in a manner that reflects the nonconvertible debt borrowing rate when recognizing interest cost in subsequent periods. The following table illustrates the carrying amount of the equity and debt components of the Debentures:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Carrying amount of the equity component | **$ 215.4** | $ 215.4 |
| Principal amount of the liability component | **732.5** | 732.5 |
| Unamortized discount | **(361.0)** | (362.6) |
| Net carrying amount | **$ 371.5** | $ 369.9 |

The following table illustrates the effective interest rate and the interest expense related to the Debentures:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Effective interest rate | **4.9%** | 4.9% | 4.9% |
| Interest expense – contractual interest coupon | **$34.8** | $34.5 | $34.9 |
| Interest expense – amortization of debt discount | **1.6** | 1.5 | 1.3 |

The remaining period over which the discount will be amortized is 32 years as of December 31, 2009.

### 7.375% Senior Notes and 7.875% Senior Notes

The notes are general unsecured obligations of the Company and rank senior in right of payment to any subordinated indebtedness of the Company; equally in right of payment with any senior indebtedness of the Company; effectively junior in right of payment to the Company's existing and future secured indebtedness, to the extent of the value of the collateral securing that indebtedness; and effectively junior to all the indebtedness and other liabilities of the Company's subsidiaries that do not guarantee the notes. Interest payments are scheduled to occur on May 1 and November 1 of each year.

The notes are guaranteed by the Company's Subsidiary Guarantors, as defined in the note indenture. The note indenture contains covenants that, among other things, limit the Company's ability to create liens and enter into sale and leaseback transactions. The notes are redeemable at a redemption price equal to 100% of the principal amount of the notes being redeemed plus a make-whole premium, if applicable, and any accrued unpaid interest to the redemption date.

### 6.875% Senior Notes

The notes are senior unsecured obligations of the Company and rank equally with all of the Company's other senior unsecured indebtedness. Interest payments are scheduled to occur on March 15 and September 15 of each year. The notes are guaranteed by the Company's Subsidiary Guarantors as defined in the note indenture. The note indenture contains covenants which, among other things, limit the Company's ability to incur additional indebtedness and issue preferred stock, pay dividends or make other distributions, make other restricted payments and investments, create liens, sell assets and merge or consolidate with other entities. The notes are redeemable at fixed redemption prices as set forth in the indenture.

### 5.875% Senior Notes

The notes are senior unsecured obligations of the Company and rank equally with all of the Company's other senior unsecured indebtedness. Interest payments are scheduled to occur on April 15 and October 15 of each year. The notes are guaranteed by the Company's Subsidiary Guarantors as defined in the note indenture. The note indenture contains covenants which, among other things, limit the Company's ability to incur additional indebtedness and issue preferred stock, pay dividends or make other distributions, make other restricted payments and investments, create liens, sell assets and merge or consolidate with other entities. The notes are redeemable at fixed redemption prices as set forth in the indenture.

### Series Bonds

The Series Bonds were assumed as part of the Excel Coal Limited acquisition. In December 2009, the Company purchased $20.0 million of the bonds in an open market transaction for $19.0 million resulting in a $1.0 million gain that was recorded as a component of interest expense. The purchase included $10.0 million of the 6.84% Series A Bonds and $10.0 million of the 6.84% Series C Bonds. Based on this purchase, the 6.84% Series A Bonds were paid in full. The 6.34% Series B Bonds are payable in installments. The first scheduled payment occurred in December 2008. The 6.84% Series C Bonds are payable in installments beginning December 2012. Interest payments are scheduled to occur in June and December of each year. The notes are redeemable at a redemption price equal to 100% of the principal amount of the notes being redeemed plus a make-whole premium, if applicable, and any accrued unpaid interest to the redemption date.

### Interest Rate Swaps

As of December 31, 2009, the Company had the following fixed-to-floating and floating-to-fixed interest rate swaps:

| (Dollars in millions) | Notional Amount | Benefit Received | Amount Paid | Termination Date | Fair Value |
|---|---|---|---|---|---|
| **Fixed-to-Floating** | | | | | |
| 6 7/8 $650 Senior Notes | $25.0 | 6.875% sa | 6-M LIBOR + 299.75 bps sa | 3/15/2013 | $ 0.8 |
| 6 7/8 $650 Senior Notes | $ 25.0 | 6.875% sa | 6-M LIBOR + 307 bps sa | 3/15/2013 | $ 0.7 |
| **Floating-to-Fixed** | | | | | |
| Senior Unsecured Term Loan | $120.0 | 3-M LIBOR + 100 bps qt | 6.25% sa | 9/15/2011 | $ (9.8) |

*Legend: M = month; bps = basis points; qt = quarterly; sa = semi-annually*

Because the critical terms of the swaps and the respective debt instruments they hedge coincide, there was no hedge ineffectiveness recognized in the consolidated statements of operations during the years ended December 31, 2009, 2008, or 2007. At December 31, 2009 and 2008, there was an unrealized loss related to the cash flow hedge of $9.8 million and $21.8 million, respectively. At December 31, 2009 and 2008, there was a net unrealized gain on the fair value hedges of $8.4 million and $15.1 million, respectively. The fair value hedge adjustment, which includes the unamortized portion of terminated fair value hedges ($6.9 million and $2.6 million at December 31, 2009 and 2008, respectively), is reflected as an adjustment to the carrying value of the 6.875% Senior Notes.

### Capital Lease Obligations

Capital lease obligations are primarily for mining equipment (see Note 9 for additional information on the Company's capital lease obligations).

### Debt Maturities, Interest Paid, and Financing Costs

The aggregate amounts of long-term debt maturities (excluding unamortized debt discounts) subsequent to December 31, 2009, including capital lease obligations, were as follows:

| Year of Maturity (Dollars in millions) | |
|---|---|
| 2010 | $ 14.1 |
| 2011 | 505.2 |
| 2012 | 22.1 |
| 2013 | 689.5 |
| 2014 | 21.5 |
| 2015 and thereafter | 1,863.8 |
| Total | $3,116.2 |

Interest paid on long-term debt was $201.6 million, $226.0 million and $191.9 million for the years ended December 31, 2009, 2008 and 2007, respectively.

Financing costs incurred with the issuance of the Company's debt are being amortized to interest expense over the remaining term of the associated debt. The remaining balance at December 31, 2009 was $30.6 million, of which $17.9 million will be amortized to interest expense over the next five years.

## (13) ASSET RETIREMENT OBLIGATIONS

Reconciliations of the Company's ARO liability are as follows:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Balance at beginning of year | $418.7 | $360.7 |
| Liabilities incurred or acquired | 0.4 | – |
| Liabilities settled or disposed | (8.1) | (6.1) |
| Accretion expense | 24.0 | 20.5 |
| Revisions to estimates | 17.1 | 43.6 |
| Balance at end of year | $452.1 | $418.7 |
| Balance at end of year – active locations | $422.0 | $383.3 |
| Balance at end of year – closed or inactive locations | $ 30.1 | $ 35.4 |

The credit-adjusted, risk-free interest rates were 7.92% at December 31, 2009 and 7.91% at December 31, 2008 and 7.85% at January 1, 2008.

As of December 31, 2009 and 2008, the Company had $772.3 million and $740.6 million, respectively, in surety bonds outstanding to secure reclamation obligations or activities. The amount of reclamation self-bonding in certain states in which the Company qualifies was $821.9 million and $773.4 million as of December 31, 2009 and 2008, respectively. Additionally, the Company had $34.9 million and $0.1 million of letters of credit in support of reclamation obligations or activities as of December 31, 2009 and 2008, respectively.

## (14) PENSION AND SAVINGS PLANS

One of the Company's subsidiaries, Peabody Investments Corp. (PIC), sponsors a defined benefit pension plan covering certain U.S. salaried employees and eligible hourly employees at certain PIC subsidiaries (the Peabody Plan). A PIC subsidiary also has a defined benefit pension plan covering eligible employees who are represented by the UMWA under the Western Surface Agreement (the Western Plan). PIC also sponsors an unfunded supplemental retirement plan to provide senior management with benefits in excess of limits under the federal tax law. These plans are collectively referred to as The Plans.

Effective June 1, 2008 the Peabody Plan was frozen in its entirety for both participation and benefit accrual purposes. The Company adopted an enhanced savings plan contribution structure in lieu of benefits formerly accrued under the Peabody Plan.

Net periodic pension cost included the following components:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Service cost for benefits earned | $ 1.4 | $ 2.0 | $ 12.7 |
| Interest cost on projected benefit obligation | 51.3 | 51.0 | 49.0 |
| Expected return on plan assets | (60.9) | (60.6) | (57.4) |
| Amortization of prior service cost | 1.4 | 1.3 | 0.4 |
| Amortization of actuarial (gains) losses | 1.9 | (0.5) | 15.3 |
| Net periodic pension cost | (4.9) | (6.8) | 20.0 |
| Curtailment gain | – | (0.6) | (0.4) |
| Total net periodic pension (benefit) cost | $ (4.9) | $ (7.4) | $ 19.6 |

The following includes amounts recognized in accumulated other comprehensive loss:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Net actuarial (gain) loss arising during year | $46.1 | $199.2 | $(89.6) |
| Prior service cost arising during year | – | – | 7.9 |
| Amortizations: | | | |
| Actuarial gain (loss) | (1.9) | 0.5 | (15.3) |
| Prior service cost | (1.4) | (0.7) | – |
| Total recognized in other comprehensive loss | 42.8 | 199.0 | (97.0) |
| Net periodic pension (benefit) costs | (4.9) | (6.8) | 20.0 |
| Total recognized in net periodic pension cost and other comprehensive loss | $37.9 | $192.2 | $(77.0) |

The Company amortizes actuarial gains and losses using a 5% corridor with a five-year amortization period. The estimated net actuarial loss and prior service cost that will be amortized from accumulated other comprehensive loss into net periodic pension costs during the year ended December 31, 2010 are $21.9 million and $1.4 million, respectively.

The following summarizes the change in benefit obligation, change in plan assets and funded status of the Company's plans:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Change in benefit obligation: | | |
| Projected benefit obligation at beginning of period | $ 768.6 | $ 778.2 |
| Service cost | 1.4 | 2.0 |
| Interest cost | 51.3 | 51.0 |
| Benefits paid | (48.3) | (46.7) |
| Actuarial (gain) loss | 71.9 | (15.9) |
| Projected benefit obligation at end of period | 844.9 | 768.6 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of period | 552.6 | 732.4 |
| Actual return on plan assets | 86.6 | (154.4) |
| Employer contributions | 38.7 | 21.3 |
| Benefits paid | (48.3) | (46.7) |
| Fair value of plan assets at end of period | 629.6 | 552.6 |
| Funded status at end of year | $(215.3) | $(216.0) |
| Amounts recognized in the consolidated balance sheets: | | |
| Current obligation (included in Accounts payable and accrued expenses) | $ (1.8) | $ (1.6) |
| Noncurrent obligation (included in Other noncurrent liabilities) | (213.5) | (214.4) |
| Net amount recognized | $(215.3) | $(216.0) |

The weighted-average assumptions used to determine the benefit obligations as of the end of each year were as follows:

| | 2009 | 2008 |
|---|---|---|
| Discount rate | 6.19% | 6.90% |
| Rate of compensation increase | N/A | N/A |
| Measurement date | Dec. 31, 2009 | Dec. 31, 2008 |

The weighted-average assumptions used to determine net periodic benefit cost were as follows:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Discount rate | 6.90% | 6.75% | 6.00% |
| Expected long-term return on plan assets | 8.75% | 8.75% | 8.75% |
| Rate of compensation increase | N/A | N/A | 3.50% |
| Measurement date | Dec. 31, 2008 | Dec. 31, 2007 | Dec. 31, 2006 |

The expected rate of return on plan assets is determined by taking into consideration expected long-term returns associated with each major asset class (net of inflation) based on long-term historical ranges, inflation assumptions and the expected net value from active management of the assets based on actual results. Effective January 1, 2010, the Company lowered its expected rate of return on plan assets from 8.75% to 8.25% given the decline in asset performance due to the global recession and disruption in the financial markets, as well as management's reevaluation of the ongoing impact of active management of assets by outside investment advisors.

The projected benefit obligation and the accumulated benefit obligation exceeded plan assets for all plans as of December 31, 2009 and 2008. The accumulated benefit obligation for all pension plans was $844.9 million and $768.6 million as of December 31, 2009, and 2008, respectively.

### *Assets of the Plans*

Assets of the Peabody Plan and the Western Plan are commingled in the PIC Master Trust (the Master Trust) and are invested in accordance with investment guidelines that have been established by the Company's Retirement Committee (the Retirement Committee) after consultation with outside investment advisors and actuaries.

The asset allocation targets have been set with the expectation that the Plans' assets will be managed with an appropriate level of risk so that they can fund each Plan's expected liabilities. To determine the appropriate target asset allocations, the Retirement Committee considers the demographics of each Plan's participants, the funding status of each Plan, the business and financial profile of the Company and other associated risk preferences. These allocation targets are reviewed by the Retirement Committee on a regular basis and revised as necessary. The current target allocations for plan assets are 55% equity securities, 35% fixed income investments and 10% real estate investments. The Company plans to transition to 60% equity securities and 40% fixed income investments over time.

Assets of the Plans are either under active management by third-party investment advisors or in index funds, all selected and monitored by the Retirement Committee. The Retirement Committee has established specific investment guidelines for each major asset class including performance benchmarks, allowable and prohibited investment types and concentration limits. In general, the Plans' investment guidelines do not permit leveraging the assets held in the Master Trust. Equity investment guidelines do not permit entering into put or call options (except as deemed appropriate to manage currency risk), and futures contracts are permitted only to the extent necessary to equitize cash holdings.

The following table presents the fair value of assets in the Master Trust by category and by fair value valuation hierarchy:

| (Dollars in millions) | 2009 Level 1 | Level 2 | Level 3 | Total |
|---|---|---|---|---|
| U.S. equity securities | $68.1 | $200.2 | $ – | $268.3 |
| International equity securities | – | 102.2 | – | 102.2 |
| Mortgage-backed debt securities | – | 77.5 | – | 77.5 |
| U.S. debt securities | 10.5 | 35.3 | – | 45.8 |
| International debt securities | – | 19.2 | – | 19.2 |
| Corporate debt securities | – | 37.2 | – | 37.2 |
| Short-term investments | – | 32.0 | – | 32.0 |
| Interests in real estate | – | – | 47.4 | 47.4 |
| Total assets at fair value | $78.6 | $503.6 | $47.4 | $629.6 |

A financial instrument's level within the valuation hierarchy is based upon the lowest level of input that is significant to the fair value measurement. Following is a description of the valuation methodologies used for investments measured at fair value, including the general classification of such investments pursuant to the valuation hierarchy.

### *U.S. equity securities*

Investment vehicles include various small-cap publicly traded common stocks, an exchange-traded fund and a common collective trust. Publicly traded common stocks and the exchange-traded fund are traded on a national securities exchange and are valued at quoted market prices in active markets and are classified within Level 1 of the valuation hierarchy. While the common collective trust invests in various large-cap publicly traded common stocks that are traded on a national securities exchange, it is classified within Level 2 of the valuation hierarchy since the net asset value (NAV) is based on a derived price in an active market and it is not publicly traded on a national securities exchange.

### *International equity securities*

Investment vehicles include a common collective trust and an investment entity that primarily invest in various large-cap international equity securities that are valued on the basis of quotations from the primary market in which they are traded and translated at each valuation date from the local currency into U.S. dollars using the mean between the bid and asked market rates for such currencies. The NAV of the fund and the calculation of the NAV of each underlying investment is determined in U.S. dollars by the custodial trustee or at the direction of the investment manager as of the end of each month. These investments are classified within the Level 2 valuation hierarchy since the NAV is based on a derived price in an active market and neither the common collective trust nor the investment entity are publicly traded on a national securities exchange.

### *Debt securities*

Investment vehicles for U.S debt securities, mortgage-backed debt securities, international debt securities and corporate debt securities (collectively, debt securities) primarily consist of mutual funds, which are invested in various diversified portfolios of fixed-income instruments. NAV for each debt security is calculated daily in actively traded markets by an independent custodian for the investment manager. For purposes of calculating NAV, portfolio securities and other assets for which market quotes are readily available are valued at market value. Market value is generally determined on the basis of last reported sales prices, or if no sales are reported, based on quotes obtained from a quotation reporting system, established market makers, or pricing services. Investments initially valued in currencies other than the U.S. dollar are converted to the U.S. dollar using exchange rates obtained from pricing services. Since the fair value inputs are derived prices in active markets and the mutual funds are not publicly traded on a national securities exchange, the debt securities are classified within the Level 2 valuation hierarchy.

### *Short-term investments*

Investments primarily consist of a common collective trust that invests in commercial paper, repurchase agreements, time deposits and agency discount notes. Units in the common collective trust are valued at NAV at year-end. These investments are classified within Level 2 of the valuation hierarchy as the NAV for these investments is a derived price in an active market and the common collective trust is not publicly traded on a national securities exchange.

### *Interests in real estate*

Investments in real estate represent interests in real estate pooled funds and limited partnerships, which consist of net partnership interests in properties. They are valued using various methodologies including independent third party appraisals. For some investments little market activity may exist and determination of fair value is then based on the best information available in the circumstances. This involves a significant degree of judgment by taking into consideration a combination of internal and external factors. Based on the above factors, the real estate funds are classified within the Level 3 valuation hierarchy.

The methods described above may produce a fair value calculation that may not be indicative of net realizable value or reflective of future fair values. Furthermore, while the Company believes the valuation methods are appropriate and consistent with other market participants, the use of different methodologies or assumptions to determine the fair value of certain financial instruments could result in a different fair value measurement at the reporting date. The inputs or methodology used for valuing investments are not necessarily an indication of the risk associated with investing in those investments.

The table below sets forth a summary of changes in the fair value of the Master Trust's Level 3 investments.

| (Dollars in millions) | 2009 |
|---|---|
| **Interests in Real Estate** | |
| Beginning of year | $ 62.2 |
| Assets held at the reporting date: | |
| Realized gains | 1.5 |
| Unrealized losses | (21.5) |
| Purchases, sales and settlements, net | 6.2 |
| Transfers out of Level 3 | (1.0) |
| End of year | $ 47.4 |

### *Contributions*

Annual contributions to the Plans are made as determined by consulting actuaries based upon the Employee Retirement Income Security Act of 1974 minimum funding standard. In May 1998, the Company entered into an agreement with the Pension Benefit Guaranty Corporation (PBGC) which requires the Company to maintain certain minimum funding requirements. Effective January 1, 2008, new minimum funding standards were required by the Pension Protection Act of 2006 (the Pension Protection Act) that increased the long-term funding targets for single employer pension plans from 90% to 100%. "At risk" plans, as defined by the Pension Protection Act, are restricted from making full lump sum payments and from increasing benefits unless they are funded immediately, and also requires that the plan give participants notice regarding the at-risk status of the plan. If a plan falls below 60%, lump sum payments are prohibited and benefit accruals cease.

As of December 31, 2009, the Company's qualified pension plans were approximately 77% funded (on a GAAP accounting basis), before considering planned 2010 contributions of $3.4 million, which represents the 2010 minimum funding requirement for the qualified Plans.

### *Estimated Future Benefit Payments*

The following benefit payments (net of retiree contributions), which reflect expected future service, as appropriate, are expected to be paid by the Master Trust:

| (Dollars in millions) | Pension Benefits |
|---|---|
| 2010 | $53.9 |
| 2011 | 55.4 |
| 2012 | 56.9 |
| 2013 | 58.8 |
| 2014 | 61.0 |
| Years 2015-2019 | 327.1 |

### *Defined Contribution Plans*

The Company sponsors employee retirement accounts under three 401(k) plans for eligible U.S. employees. The Company matches voluntary contributions to each plan up to specified levels. The expense for these plans was $47.9 million, $50.5 million and $21.7 million for the years ended December 31, 2009, 2008 and 2007, respectively. A performance contribution feature allows for additional contributions from the Company based upon meeting specified Company performance targets. Performance contributions related to the years ended December 31, 2009, 2008, and 2007 were $20.3 million, $18.7 million and $4.9 million, respectively.

### *Multi-Employer Pension Plan – Discontinued Operations*

Certain subsidiaries that were part of the Patriot spin-off participate in multi-employer pension plans (the 1950 Plan and the 1974 Plan), which provide defined benefits to substantially all hourly coal production workers represented by the UMWA under the 2007 NBCWA. During 2007, contributions of $5.9 million made to the 1974 Plan were expensed as paid, and are reflected in "Discontinued operations." There were no contributions to the multi-employer pension plans during the years ended December 31, 2009 and 2008.

## (15) POSTRETIREMENT HEALTH CARE AND LIFE INSURANCE BENEFITS

The Company currently provides health care and life insurance benefits to qualifying salaried and hourly retirees and their dependents from defined benefit plans established by the Company. Plan coverage for health and life insurance benefits is provided to future hourly retirees in accordance with the applicable labor agreement.

Net periodic postretirement benefit cost included the following components:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Service cost for benefits earned | **$10.5** | $10.1 | $ 9.4 |
| Interest cost on accumulated postretirement benefit obligation | **55.2** | 54.0 | 50.6 |
| Amortization of prior service cost (credit) | **1.5** | 0.4 | (0.2) |
| Amortization of actuarial losses | **14.5** | 17.3 | 22.8 |
| Net periodic postretirement benefit cost | **$81.7** | $81.8 | $82.6 |

Net periodic postretirement benefit cost related to the spin-off of Patriot was $46.6 million for the year ended December 31, 2007 and was included in "Discontinued operations."

The following includes amounts recognized in accumulated other comprehensive loss:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Net actuarial (gain) loss arising during year | **$165.2** | $(18.3) | $(24.5) |
| Prior service cost arising during year | **(10.5)** | – | 13.8 |
| Amortizations: | | | |
| Actuarial loss | **(14.5)** | (17.3) | (22.8) |
| Prior service (cost) credit | **(1.5)** | (0.4) | 0.2 |
| Total recognized in other comprehensive loss | **138.7** | (36.0) | (33.3) |
| Net periodic postretirement benefit cost | **81.7** | 81.8 | 82.6 |
| Total recognized in net periodic postretirement benefit costs and other comprehensive loss | **$220.4** | $ 45.8 | $ 49.3 |

The Company amortizes actuarial gains and losses using a 0% corridor with an amortization period that covers the average remaining service period of active employees (10.92 years and 10.68 years at January 1, 2009 and 2008, respectively). The estimated net actuarial loss and prior service cost that will be amortized from accumulated other comprehensive loss into net periodic postretirement benefit cost during the year ended December 31, 2010 are $25.4 million and $2.0 million, respectively.

The following table sets forth the plan's funded status reconciled with the amounts shown in the consolidated balance sheets:

| (Dollars in millions) | 2009 | 2008 |
|---|---|---|
| Change in benefit obligation: | | |
| Accumulated postretirement benefit obligation at beginning of period | **$ 833.4** | $ 855.8 |
| Service cost | **10.5** | 10.1 |
| Interest cost | **55.2** | 54.0 |
| Participant contributions | **1.2** | 1.5 |
| Plan amendments [(1)] | **(10.5)** | – |
| Benefits paid | **(72.8)** | (69.7) |
| Actuarial (gain) loss | **165.2** | (18.3) |
| Accumulated postretirement benefit obligation at end of period | **982.2** | 833.4 |
| Change in plan assets: | | |
| Fair value of plan assets at beginning of period | **–** | – |
| Employer contributions | **71.6** | 68.2 |
| Participant contributions | **1.2** | 1.5 |
| Benefits paid and administrative fees (net of Medicare Part D reimbursements) | **(72.8)** | (69.7) |
| Fair value of plan assets at end of period | **–** | – |
| Funded status at end of year | **(982.2)** | (833.4) |
| Less current portion (included in Accounts payable and accrued expenses) | **68.1** | 67.3 |
| Noncurrent obligation (included in Accrued postretirement benefit costs) | **$(914.1)** | $(766.1) |

(1) Effective January 1, 2010, the benefits provided to certain salaried retirees are capped at a fixed level, which resulted in a decrease to the retiree health care liability of $7.3 million. The Company will begin realizing the effect of this plan amendment over 13.54 years beginning January 1, 2010.

The weighted-average assumptions used to determine the benefit obligations as of the end of each year were as follows:

| | 2009 | 2008 |
|---|---|---|
| Discount rate | **6.14%** | 6.85% |
| Rate of compensation increase | **3.50%** | 3.50% |
| Measurement date | **Dec. 31, 2009** | Dec. 31, 2008 |

The weighted-average assumptions used to determine net periodic benefit cost were as follows:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Discount rate | **6.85%** | 6.60% | 6.00% |
| Rate of compensation increase | **3.50%** | 3.50% | 3.50% |
| Measurement date | **Dec. 31, 2008** | Dec. 31, 2007 | Dec. 31, 2006 |

The following presents information about the assumed health care cost trend rate:

| | 2009 | 2008 |
|---|---|---|
| Health care cost trend rate assumed for next year | **7.50%** | 7.50% |
| Rate to which the cost trend is assumed to decline (the ultimate trend rate) | **5.00%** | 4.75% |
| Year that the rate reaches the ultimate trend rate | **2016** | 2014 |

Assumed health care cost trend rates have a significant effect on the amounts reported for health care plans. A one-percentage-point change in the assumed health care cost trend would have the following effects:

| (Dollars in millions) | One Percentage-Point Increase | One Percentage-Point Decrease |
|---|---|---|
| Effect on total service and interest cost components | $6.7 | $(5.7) |
| Effect on total postretirement benefit obligation | $98.3 | $(84.6) |

### *Plan Assets*

The Company's postretirement benefit plans are unfunded.

### *Estimated Future Benefit Payments*

The following benefit payments (net of retiree contributions), which reflect expected future service as appropriate, are expected to be paid by the Company:

| (Dollars in millions) | Postretirement Benefits |
|---|---|
| 2010 | $68.1 |
| 2011 | 70.7 |
| 2012 | 74.5 |
| 2013 | 75.9 |
| 2014 | 77.1 |
| Years 2015-2019 | 398.3 |

### *Multi-Employer Benefit Plans – Discontinued Operations*

Multi-employer benefit obligations related to the Combined Fund, the 1992 Benefit Plan and 1993 Benefit Plan became the responsibility of Patriot in conjunction with the spin-off. The Surface Mining Control and Reclamation Act Amendments of 2006 amended the federal laws establishing the Combined Fund and the 1992 Benefit Plan and include the 1993 Benefit Plan. To the extent that (i) the annual federal funding is less than benefits paid, (ii) Congress does not allocate additional funds to cover the shortfall and (iii) Patriot's subsidiaries do not pay for their share of the shortfall, some of the Company's subsidiaries would be responsible for the additional costs. The total expense for the Combined Fund, the 1992 Benefit Plan and 1993 Benefit Plan was $14.5 million for the year ended December 31, 2007 and was included in "Discontinued operations."

## (16) STOCKHOLDERS' EQUITY

### *Common Stock*

The Company has 800.0 million authorized shares of $0.01 par value common stock. Holders of common stock are entitled to one vote per share on all matters to be voted upon by the stockholders and vote together, as one class, with the holders of the Company's Series A Junior Participating Preferred Stock, if any such shares were issued and outstanding. The holders of common stock do not have cumulative voting rights in the election of directors. Holders of common stock are entitled to receive ratably dividends if, as and when dividends are declared from time to time by the Company's Board of Directors out of funds legally available for that purpose, after payment of dividends required to be paid on outstanding preferred stock or series common stock, as described below. Upon liquidation, dissolution or winding up, any business combination or a sale or disposition of all or substantially all of the assets, the holders of common stock are entitled to receive ratably the assets available for distribution to the stockholders after payment of liabilities and accrued but unpaid dividends and liquidation preferences on any outstanding preferred stock or series common stock. The common stock has no preemptive or conversion rights and is not subject to further calls or assessment by the Company. There are no redemption or sinking fund provisions applicable to the common stock.

The following table summarizes common stock activity from December 31, 2006 to December 31, 2009:

| | *Shares Outstanding* |
|---|---|
| **December 31, 2006** | 263,846,839 |
| Stock options exercised | 5,222,074 |
| Stock grants to employees | 937,795 |
| Employee stock purchases | 185,646 |
| Stock grants to non-employee directors | 11,892 |
| Shares relinquished | (137,625) |
| **December 31, 2007** | 270,066,621 |
| Stock options exercised | 1,388,174 |
| Stock grants to employees | 788,895 |
| Employee stock purchases | 119,737 |
| Stock grants to non-employee directors | 2,870 |
| Shares repurchased | (5,524,574) |
| Shares relinquished | (196,744) |
| **December 31, 2008** | **266,644,979** |
| Stock options exercised | **463,490** |
| Stock grants to employees | **794,213** |
| Employee stock purchases | **374,548** |
| Stock grants to non-employee directors | **4,788** |
| Shares relinquished | **(78,203)** |
| **December 31, 2009** | **268,203,815** |

### *Preferred Stock and Series Common Stock*

The Board of Directors is authorized to issue up to 10.0 million shares of preferred stock and up to 40.0 million shares of series common stock. The Board of Directors can determine the terms and rights of each series, whether dividends (if any) will be cumulative or non-cumulative and the dividend rate of the series, redemption or sinking fund provisions, conversion terms, prices and rates, and amounts payable on shares of the series in the event of any voluntary or involuntary liquidation, dissolution or winding up of the affairs of the Company. The Board of Directors may also determine restrictions on the issuance of shares of the same series or of any other class or series, and the voting rights (if any) of the holders of the series. There were no outstanding shares of preferred stock or series common stock as of December 31, 2009.

### *Perpetual Preferred Stock*

As discussed in Note 12, the Company had $732.5 million aggregate principal amount of Debentures outstanding as of December 31, 2009. Perpetual preferred stock issued upon a conversion of the Debentures will be fully paid and nonassessable, and holders will have no preemptive or preferential right to purchase any of the Company's other securities. The perpetual preferred stock has a liquidation preference of $1,000 per share, is not convertible and is redeemable at the Company's option at any time at a cash redemption price per share equal to the liquidation preference plus any accumulated dividends. Holders are entitled to receive cumulative dividends at an annual rate of 3.0875% if and when declared by the Company's Board of Directors. If the Company fails to pay dividends on the perpetual preferred stock for five years, or upon the occurrence of a mandatory trigger event, as defined in the certificate of designations governing the perpetual preferred stock, the Company generally must sell warrants or preferred stock with specified characteristics and use the funds from that sale to pay accumulated dividends after the payment in full of any deferred interest on the Debentures, subject to certain limitations. In the event of a mandatory trigger event, the Company may not declare dividends on the perpetual preferred stock other than those funded through the sale of warrants or preferred stock as described above. Any deferred interest on the Debentures at the time of notice of conversion will be reflected as accumulated dividends on the perpetual preferred stock at issuance. Additionally, holders of the perpetual preferred stock are entitled to elect two additional members to serve on the Company's Board of Directors if (i) prior to any remarketing of the perpetual preferred stock, the Company fails to declare and pay dividends with respect to the perpetual stock for 10 consecutive years or (ii) after any successful remarketing or any final failed remarketing of the perpetual preferred stock, the Company fails to declare and pay six dividends thereon, whether or not consecutive. The perpetual preferred stock may be remarketed at the holder's election after December 15, 2046 or earlier, upon the first occurrence of a change of control if the Company does not redeem the perpetual preferred stock. There were no outstanding shares of perpetual preferred stock as of December 31, 2009.

### *Preferred Share Purchase Rights Plan and Series A Junior Participating Preferred Stock*

Each outstanding share of common stock, par value $0.01 per share, of the Company carries one preferred share purchase right (a Right). The Rights are governed by a plan that expires in August 2012.

The Rights have certain anti-takeover effects. The Rights will cause substantial dilution to a person or group that attempts to acquire the Company on terms not approved by the Company's Board of Directors, except pursuant to any offer conditioned on a substantial number of Rights being acquired. The Rights should not interfere with any merger or other business combination approved by the Board of Directors since the Rights may be redeemed by the Company at a redemption price of $0.001 per Right prior to the time that a person or group has acquired beneficial ownership of 15% or more of the common stock of the Company. In addition, the Board of Directors is authorized to reduce the 15% threshold to not less than 10%.

Each Right entitles the holder to purchase one quarter of one-hundredth of a share of Series A Junior Participating Preferred Stock from the Company at an exercise price of $27.50, which in turn provides rights to receive the number of common stock shares having a market value of two times the exercise price of the Right. The Right is exercisable only if a person or group acquires 15% or more of the Company's common stock. The Board of Directors is authorized to issue up to 1.5 million shares of Series A Junior Participating Preferred Stock. There were no outstanding shares of Series A Junior Participating Preferred Stock as of December 31, 2009.

### *Treasury Stock*

The Company has a share repurchase program for its common stock with an authorized amount of $1 billion in which repurchases may be made from time to time based on an evaluation of the Company's outlook and general business conditions, as well as alternative investment and debt repayment options. The Company's Chairman and Chief Executive Officer also has authority to direct the Company to repurchase up to $100 million of common stock outside the share repurchase program. The repurchase program does not have an expiration date and may be discontinued at any time. Through December 31, 2009, the Company has made repurchases of 7.7 million shares at a cost of $299.6 million, leaving $700.4 million available for share repurchase under the program.

During the year ended December 31, 2009, the Company received 78,203 shares of common stock to pay estimated taxes as consideration for the exercise of stock options, the payout of performance units and the vesting of restricted stock. The value of the common stock tendered by employees was based upon the closing price on the dates of the respective transactions.

## (17) SHARE-BASED COMPENSATION

The Company recognizes share-based compensation expense in accordance with the fair value recognition provisions of "Compensation" topic of the ASC, which it adopted on January 1, 2006. The Company has four equity incentive plans for employees and non-employee directors that in the aggregate allow for the issuance of share-based compensation in the form of stock appreciation rights, restricted stock, performance awards, incentive stock options, nonqualified stock options and deferred stock units. These plans made 47.4 million shares of the Company's common stock available for grant, with 14.6 million shares available for grant as of December 31, 2009. The Company has two employee stock purchase plans that provide for the purchase of up to 6.0 million shares of the Company's common stock, with 5.0 million shares authorized for purchase by U.S. employees and 1.0 million shares authorized for purchase by the Australian employees.

Share-based compensation expense, which is recorded in "Selling and administrative expenses" in the consolidated statements of operations, was as follows:

| *(Dollars in millions)* | *Total Expense* | *Tax Benefit* | *Expense, Net of Tax Benefit* |
|---|---|---|---|
| **2009** | **$38.8** | **$15.0** | **$23.8** |
| 2008 | 34.9 | 13.5 | 21.4 |
| 2007 | 20.1 | 2.9 | 17.2 |

As of December 31, 2009, the total unrecognized compensation cost related to nonvested awards was $28.0 million, net of taxes, which is expected to be recognized over 3.2 years with a weighted-average period of 0.7 years.

In 2009 and 2008, the Company granted deferred stock units to each of its non-employee directors. The fair value of these units are equal to the market price of the Company's common stock at the date of grant and generally vest after one year. In 2007, the Company granted stock options and restricted stock to each of its non-employee directors.

### *Restricted Stock Awards*

Restricted stock awards are typically granted in January of each year and generally cliff vest after three years of service. The fair value of restricted stock is equal to the market price of the Company's common stock at the date of grant and is amortized to expense ratably over the vesting period.

A summary of restricted stock award activity is as follows:

| | 2009 | Weighted Average Grant-Date Fair Value |
|---|---|---|
| Nonvested at January 1, 2009 | **1,788,333** | $38.13 |
| Granted | **769,229** | 30.09 |
| Vested | **(308,760)** | 36.43 |
| Forfeited | **(103,937)** | 37.49 |
| Nonvested at December 31, 2009 | **2,144,865** | $35.51 |

### *Stock Options*

Employee and director stock options granted since the Company's initial public offering (IPO) of common stock in May 2001 generally vest ratably over three years and expire after 10 years from the date of the grant, subject to earlier termination upon discontinuation of an employee's service. Options granted prior to the IPO generally cliff vest in 2010 and represented 0.8 million options of the 3.2 million options outstanding at December 31, 2009. Option grants are typically made in January of each year or following the inception of employment for employees hired during the year who are eligible to participate in the plan.

The Company used the Black-Scholes option pricing model to determine the fair value of stock options. The Company utilized U.S. Treasury yields as of the grant date for its risk-free interest rate assumption, matching the treasury yield terms to the expected life of the option. The Company utilized historical company data to develop its dividend yield, expected volatility and expected option life assumptions.

A summary of outstanding option activity under the plans is as follows:

| | 2009 | Weighted Average Exercise Price | Weighted Average Remaining Contractual Life | Aggregate Intrinsic Value (in millions) |
|---|---|---|---|---|
| Options Outstanding at January 1, 2009 | **3,250,857** | $17.84 | | |
| Granted | **481,498** | 26.84 | | |
| Exercised | **(463,490)** | 7.73 | | |
| Forfeited | **(22,835)** | 43.37 | | |
| Options Outstanding at December 31, 2009 | **3,246,030** | $20.44 | 4.7 | $85.1 |
| Vested and Exercisable | **1,715,557** | $20.78 | 4.6 | $43.1 |

During the years ended December 31, 2009, 2008 and 2007, the total intrinsic value of options exercised, defined as the excess fair value of the underlying stock over the exercise price of the options, was $14.7 million, $72.8 million and $248.7 million, respectively. The weighted-average fair values of the Company's stock options and the assumptions used in applying the Black-Scholes option pricing model (for grants during the years ended December 31, 2009, 2008 and 2007) were as follows:

| | 2009 | 2008 | 2007 |
|---|---|---|---|
| Weighted-average fair value | **$26.84** | $64.31 | $37.93 |
| Risk-free interest rate | **1.5%** | 3.3% | 4.6% |
| Expected option life | **5.0 years** | 5.0 years | 5.0 years |
| Expected volatility | **60%** | 40% | 43% |
| Dividend yield | **0.9%** | 0.5% | 0.6% |

### *Performance Units*

Performance units are typically granted annually in January and vest over a three-year measurement period. Prior to 2009, the performance units were usually subject to the achievement of two goals, 50% based on stock price performance compared to both an industry peer group and a S&P index (market condition) and 50% based on a return on capital target (performance condition). For 2009, the units granted were only subject to the achievement of the market condition. Three performance unit grants are outstanding for any given year. The payouts related to all active grants will be settled in the Company's common stock.

A summary of performance unit activity is as follows:

| | 2009 | Weighted Average Remaining Contractual Life |
|---|---|---|
| Nonvested at January 1, 2009 | **250,691** | 1.5 |
| Granted | **248,263** | |
| Forfeited | **(9,195)** | |
| Vested | **(133,315)** | |
| Nonvested at December 31, 2009 | **356,444** | 1.5 |

As of December 31, 2009, there were 133,315 performance units vested that had an aggregate intrinsic value of $8.7 million and a conversion price per share of $44.49.

The awards settled are accounted for based on their grant date fair value. The performance condition awards were valued utilizing the grant date fair values of the Company's stock adjusted for dividends foregone during the vesting period. The market condition awards were valued utilizing a Monte Carlo simulation which incorporates the total stockholder return hurdles set for each grant. The assumptions used in the valuations for grants during the years ended December 31, 2009 and 2008 were as follows:

| | 2009 | 2008 |
|---|---|---|
| Risk-free interest rate | **1.3%** | 2.9% |
| Expected volatility | **60%** | 40% |
| Dividend yield | **0.9%** | 0.5% |

### *Employee Stock Purchase Plans*

The Company's eligible full-time and part-time employees are able to contribute up to 15% of their base compensation into the employee stock purchase plans, subject to a limit of $25,000 per person per year. Employees are able to purchase Company common stock at a 15% discount to the lower of the fair market value of the Company's common stock on the initial or final trading dates of each six-month offering period. Offering periods begin on January 1 and July 1 of each year. The Company uses the Black-Scholes option pricing model to determine the fair value of employee stock purchase plans share-based payments. The fair value of the six-month "look-back" option in the Company's employee stock purchase plans is estimated by adding the fair value of 0.15 of one share of stock to the fair value of 0.85 of an option on one share of stock. The Company utilized U.S. Treasury yields as of the grant date for its risk-free interest rate assumption, matching the treasury yield terms to the six-month offering period. The Company utilized historical company data to develop its dividend yield and expected volatility assumptions.

Shares purchased under the plans were 0.3 million for the year ended December 31, 2009, 0.1 million for the year ended December 31, 2008 and 0.2 million for the year ended December 31, 2007.

## (18) ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

The following table sets forth the after-tax components of comprehensive income (loss):

| (Dollars in millions) | Foreign Currency Translation Adjustment | Net Actuarial Loss Associated with Postretirement Plans and Workers' Compensation Obligations | Prior Service Cost Associated with Postretirement Plans | Cash Flow Hedges | Total Accumulated Other Comprehensive Loss |
|---|---|---|---|---|---|
| **December 31, 2006** | $3.1 | $(288.8) | $(7.0) | $43.5 | $(249.2) |
| Net increase in value of cash flow hedges | – | – | – | 83.7 | 83.7 |
| Reclassification from other comprehensive income to earnings: | | | | | |
| Continuing operations | – | 24.3 | (0.1) | (61.8) | (37.6) |
| Discontinued operations | – | 17.9 | (6.1) | – | 11.8 |
| Current period change | – | 64.2 | (13.0) | – | 51.2 |
| Patriot spin-off | – | 65.7 | 7.3 | – | 73.0 |
| **December 31, 2007** | 3.1 | (116.7) | (18.9) | 65.4 | (67.1) |
| Net decrease in value of cash flow hedges | – | – | – | (194.5) | (194.5) |
| Reclassification from other comprehensive income to earnings | – | 14.1 | 0.2 | (23.4) | (9.1) |
| Current period change | – | (117.8) | – | – | (117.8) |
| **December 31, 2008** | **3.1** | **(220.4)** | **(18.7)** | **(152.5)** | **(388.5)** |
| Net increase in value of cash flow hedges | **–** | **–** | **–** | **235.2** | **235.2** |
| Reclassification from other comprehensive income to earnings | **–** | **11.8** | **1.8** | **84.6** | **98.2** |
| Current period change | **–** | **(128.4)** | **–** | **–** | **(128.4)** |
| **December 31, 2009** | **$3.1** | **$(337.0)** | **$(16.9)** | **$167.3** | **$(183.5)** |

Comprehensive income (loss) differs from net income by the amount of unrealized gain or loss resulting from valuation changes of the Company's cash flow hedges (which include fuel and explosives hedges, currency forwards, traded coal index contracts and interest rate swaps) and the change in actuarial loss and prior service cost during the periods. The values of the Company's cash flow hedging instruments are affected by changes in interest rates, crude oil, diesel fuel, natural gas and coal prices and the U.S. dollar/Australian dollar exchange rate. The change in the value of the cash flow hedges during 2009 was primarily due to the strengthening of the Australian dollar against the U.S. dollar.

## (19) GUARANTEES AND FINANCIAL INSTRUMENTS WITH OFF-BALANCE-SHEET RISK

In the normal course of business, the Company is a party to guarantees and financial instruments with off-balance-sheet risk, such as bank letters of credit, performance or surety bonds and other guarantees and indemnities, which are not reflected in the accompanying consolidated balance sheets. Such financial instruments are valued based on the amount of exposure under the instrument and the likelihood of required performance. In the Company's past experience, virtually no claims have been made against these financial instruments. Management does not expect any material losses to result from these guarantees or off-balance-sheet instruments.

### *Letters of Credit and Bonding*

The Company has letters of credit, surety bonds and corporate guarantees (such as self bonds) in support of the Company's reclamation, coal lease obligations, and workers' compensation as follows as of December 31, 2009:

| *(Dollars in millions)* | *Reclamation Obligations* | *Lease Obligations* | *Workers' Compensation Obligations* | *Other [1]* | *Total* |
|---|---|---|---|---|---|
| Self Bonding | **$ 821.9** | **$ –** | **$ –** | **$ –** | **$ 821.9** |
| Surety Bonds | **772.3** | **116.3** | **8.7** | **57.3** | **954.6** |
| Letters of Credit | **34.9** | **–** | **43.0** | **237.8** | **315.7** |
| | **$1,629.1** | **$116.3** | **$51.7** | **$295.1** | **$2,092.2** |

[1] *Other includes the six letter of credit obligations described below and an additional $61.1 million in letters of credit and surety bonds related to collateral for surety companies, road maintenance, performance guarantees and other operations.*

The Company owns a 37.5% interest in Dominion Terminal Associates, a partnership that operates a coal export terminal in Newport News, Virginia under a 30-year lease that permits the partnership to purchase the terminal at the end of the lease term for a nominal amount. The partners have severally (but not jointly) agreed to make payments under various agreements which in the aggregate provide the partnership with sufficient funds to pay rents and to cover the principal and interest payments on the floating-rate industrial revenue bonds issued by the Peninsula Ports Authority, and which are supported by letters of credit from a commercial bank. As of December 31, 2009, the Company's maximum reimbursement obligation to the commercial bank was in turn supported by four letters of credit totaling $42.7 million.

The Company is party to an agreement with the PBGC and TXU Europe Limited, an affiliate of the Company's former parent corporation, under which the Company is required to make special contributions to two of the Company's defined benefit pension plans and to maintain a $37.0 million letter of credit in favor of the PBGC. If the Company or the PBGC gives notice of an intent to terminate one or more of the covered pension plans in which liabilities are not fully funded, or if the Company fails to maintain the letter of credit, the PBGC may draw down on the letter of credit and use the proceeds to satisfy liabilities under the Employee Retirement Income Security Act of 1974, as amended. The PBGC, however, is required to first apply amounts received from a $110.0 million guarantee in place from TXU Europe Limited in favor of the PBGC before it draws on the Company's letter of credit. On November 19, 2002 TXU Europe Limited was placed under the administration process in the United Kingdom (a process similar to bankruptcy proceedings in the U.S.) and continues under this process as of December 31, 2009. As a result of these proceedings, TXU Europe Limited may be liquidated or otherwise reorganized in such a way as to relieve it of its obligations under its guarantee.

At December 31, 2009, the Company has a $154.3 million letter of credit for collateral for bank guarantees issued with respect to certain reclamation and performance obligations related to some of the Company's Australian mines.

### *Other Guarantees*

The Company has a liability recorded of $52.3 million as of December 31, 2009 and $61.8 million as of December 31, 2008 related to reclamation and bonding commitments associated with the purchase of approximately 427 million tons of coal reserves and surface lands in the Illinois Basin in 2007.

The Company is the lessee under numerous equipment and property leases. It is common in such commercial lease transactions for the Company, as the lessee, to agree to indemnify the lessor for the value of the property or equipment leased, should the property be damaged or lost during the course of the Company's operations. The Company expects that losses with respect to leased property would be covered by insurance (subject to deductibles). The Company and certain of its subsidiaries have guaranteed other subsidiaries' performance under their various lease obligations. Aside from indemnification of the lessor for the value of the property leased, the Company's maximum potential obligations under its leases are equal to the respective future minimum lease payments as presented in Note 9, and the Company assumes that no amounts could be recovered from third parties.

A subsidiary of the Company owns a 5.06% undivided interest in Prairie State, which is currently under construction. In connection with the development of Prairie State, each owner, including the Company's subsidiary, has a guarantee for its proportionate share of obligations to pay its percentage of the construction costs under the Target Price Engineering, Procurement and Construction Agreement with Bechtel Power Corporation. The Company has capitalized development costs of $126.5 million and $69.7 million that were recorded as part of "Investments and other assets" in the consolidated balance sheets as of December 31, 2009 and 2008, respectively. The Company spent $56.8 million during the year ended December 31, 2009 representing its 5.06% share of the construction costs. Total construction costs for Prairie State are expected to be approximately $4 billion.

The Company has provided financial guarantees under certain long-term debt agreements entered into by its subsidiaries, and substantially all of the Company's subsidiaries provide financial guarantees under long-term debt agreements entered into by the Company. The maximum amounts payable under the Company's debt agreements are equal to the respective principal and interest payments. See Note 12 for the descriptions of the Company's (and its subsidiaries') debt. Supplemental guarantor/non-guarantor financial information is provided in Note 23.

As part of the Patriot spin-off, the Company agreed to maintain in force several letters of credit that secured Patriot obligations for certain employee benefits and workers' compensation obligations. As of December 31, 2009, these letters of credit were released as Patriot satisfied the beneficiaries with alternate letters of credit or insurance.

A discussion of the Company's accounts receivable securitization program is included in Note 6 to the consolidated financial statements.

## (20) COMMITMENTS AND CONTINGENCIES

### *Commitments*

As of December 31, 2009, purchase commitments for capital expenditures were $70.4 million. Commitments for expenditures to be made under coal leases are reflected in Note 9. The Company has also various long- and short-term take or pay arrangements associated with rail and port commitments for the delivery of coal, some of which extend to 2040, including amounts relating to export facilities currently under construction which are expected to be completed in 2010. As of December 31, 2009, these commitments totaled $1,864.4 million with $718.5 million obligated within the next five years and $110.7 million obligated within the next year.

From time to time, the Company or its subsidiaries are involved in legal proceedings arising in the ordinary course of business or related to indemnities or historical operations. The Company believes it has recorded adequate reserves for these liabilities and that there is no individual case pending that is likely to have a material adverse effect on the Company's financial condition, results of operations or cash flows. The Company discusses its significant legal proceedings below.

### *Litigation Relating to Continuing Operations*

#### *Navajo Nation Litigation*

On June 18, 1999, the Navajo Nation served three of the Company's subsidiaries, including Peabody Western Coal Company (Peabody Western), with a complaint that had been filed in the U.S. District Court for the District of Columbia. The Navajo Nation has alleged 16 claims, including Civil Racketeer Influenced and Corrupt Organizations Act (RICO) violations and fraud. The complaint alleges that the defendants jointly participated in unlawful activity to obtain favorable coal lease amendments. The plaintiff is seeking various remedies including actual damages of at least $600 million, which could be trebled under the RICO counts, punitive damages of at least $1 billion, a determination that Peabody Western's two coal leases have terminated due to Peabody Western's breach of these leases and a reformation of these leases to adjust the royalty rate to 20%. Subsequently, the court allowed the Hopi Tribe to intervene in this lawsuit and the Hopi Tribe is also seeking unspecified actual damages, punitive damages and reformation of its coal lease. One of the Company's subsidiaries named as a defendant is now a subsidiary of Patriot. However, the Company is responsible for this litigation under the Separation Agreement entered into with Patriot in connection with the spin-off. On April 6, 2009, the U.S. Supreme Court ruled against the Navajo Nation in a related case against the U.S. government, and remanded that case to the lower court to dismiss the complaint. The U.S. Supreme Court said that none of the sources relied on by the Navajo Nation provided a basis for its breach-of-trust lawsuit against the U.S. government, which undermines some of the claims the Navajo Nation asserts in its litigation against the Company.

The outcome of this litigation is subject to numerous uncertainties. Based on the Company's evaluation of the issues and their potential impact, the amount of any future loss cannot be reasonably estimated. However, based on current information, the Company believes this matter is likely to be resolved without a material adverse effect on the Company's financial condition, results of operations or cash flows.

#### *Gulf Power Company Litigation*

On June 22, 2006, Gulf Power Company (Gulf Power) filed a breach of contract lawsuit against a Company subsidiary in the U.S. District Court, Northern District of Florida, contesting the force majeure declaration by the Company's subsidiary under a coal supply agreement with Gulf Power and seeking damages for alleged past and future tonnage shortfalls of nearly 5 million tons under the agreement, which expired on December 31, 2007. In February 2008, the court denied the Company's motion to dismiss the Florida lawsuit or to transfer it to Illinois and retained jurisdiction over the case. Gulf Power filed a motion for partial summary judgment on liability, and the Company subsidiary filed a motion for summary judgment seeking complete dismissal. On September 30, 2009, the court granted Gulf Power's motion for partial summary judgment and denied the Company subsidiary's motion for summary judgment. In October 2009, the Company subsidiary filed a motion for reconsideration which the court denied. The damages portion of the trial was held in February 2010; however, the court has not yet rendered its decision in the case.

The outcome of this litigation is subject to numerous uncertainties. Based on the Company's evaluation of the issues and their potential impact, the amount of any future loss cannot reasonably be estimated. However, based on current information, the Company believes this matter is likely to be resolved without a material adverse effect on its financial condition, results of operations or cash flows.

***Claims and Litigation Relating to Indemnities or Historical Operations***

*Oklahoma Lead Litigation*

Gold Fields Mining, LLC (Gold Fields) is a dormant, non-coal producing entity that was previously managed and owned by Hanson PLC, the Company's predecessor owner. In a February 1997 spin-off, Hanson PLC transferred ownership of Gold Fields to the Company, despite the fact that Gold Fields had no ongoing operations and the Company had no prior involvement in its past operations. Gold Fields is currently one of the Company's subsidiaries. The Company indemnified TXU Group with respect to certain claims relating to a former affiliate of Gold Fields. A predecessor of Gold Fields formerly operated two lead mills near Picher, Oklahoma prior to the 1950s and mined, in accordance with lease agreements and permits, approximately 0.15% of the total amount of the crude ore mined in the county.

Gold Fields and several other companies are defendants in two property damage lawsuits arising from past operations near Picher, Oklahoma. The plaintiffs are seeking compensatory damages for diminution in property values and punitive damages. These cases were originally filed as putative class actions, but the court has denied class certification and the cases were subsequently amended to include a number of individual plaintiffs. In December 2003, the Quapaw Indian tribe and certain Quapaw land owners filed a lawsuit against Gold Fields, five other companies and the U.S. The plaintiffs are seeking compensatory and punitive damages based on a variety of theories. In December 2007, the court dismissed the tribe's medical monitoring claim. In July 2008, the court dismissed the tribe's claim for interim and lost use damages under the Comprehensive Environmental Response, Compensation and Liability Act without prejudice to refile at the point the U.S. Environmental Protection Agency (EPA) selects a final remedy for the site. Gold Fields has filed a third-party complaint against the U.S. and other parties. In February 2005, the state of Oklahoma on behalf of itself and several other parties sent a notice to Gold Fields and other companies regarding a possible natural resources damage claim. All of the lawsuits are pending in the U.S. District Court for the Northern District of Oklahoma.

The outcome of litigation and these claims are subject to numerous uncertainties. Based on the Company's evaluation of the issues and their potential impact, the amount of any future loss cannot be reasonably estimated. However, based on current information, the Company believes this matter is likely to be resolved without a material adverse effect on its financial condition, results of operations or cash flows.

***Environmental Claims and Litigation***

Environmental claims have been asserted against Gold Fields related to activities of Gold Fields or a former affiliate. Gold Fields or the former affiliate has been named a potentially responsible party (PRP) at five national priority list sites based on the Superfund Amendments and Reauthorization Act of 1986. Claims were asserted at 12 additional sites, bringing the total to 17, which have since been reduced to 11 by completion of work, transfer or regulatory inactivity. The number of PRP sites in and of itself is not a relevant measure of liability, because the nature and extent of environmental concerns varies by site, as does the estimated share of responsibility for Gold Fields or the former affiliate. Undiscounted liabilities for environmental cleanup-related costs for all of the sites noted above were $49.5 million as of December 31, 2009 and $45.3 million as of December 31, 2008, $7.9 million and $7.6 million of which was reflected as a current liability, respectively. These amounts represent those costs that the Company believes are probable and reasonably estimable. In September 2005, Gold Fields and other PRPs received a letter from the U.S. Department of Justice alleging that the PRP's mining operations caused the EPA to incur approximately $125 million in residential yard remediation costs at Picher, Oklahoma and will cause the EPA to incur additional remediation costs relating to historical mining sites. In September 2008, Gold Fields and other PRPs received letters from the U.S. Department of Justice and the EPA re-initiating settlement negotiations. Gold Fields continues to participate in the settlement discussions. Gold Fields believes it has meritorious defenses to these claims. Gold Fields is involved in other litigation in the Picher area, and the Company indemnified TXU Group with respect to a defendant as is more fully discussed under the "Oklahoma Lead Litigation" caption above. Gold Fields has also been contacted by the state of Kansas (Kansas Department of Health and Environment) and is in negotiations for final resolution of natural resource damages claims at two sites. Significant uncertainty exists as to whether claims will be pursued against Gold Fields in all cases, and where they are pursued, the amount of the eventual costs and liabilities, which could be greater or less than the liabilities recorded in the consolidated balance sheets. Based on the Company's evaluation of the issues and their potential impact, the amount of any future loss cannot be reasonably estimated. However, based on current information, the Company believes these claims and litigation are likely to be resolved without a material adverse effect on its financial condition, results of operations or cash flows.

*Comer, et al v. Murphy Oil Co., et al.*

In April 2006, residents and owners of land and property along the Mississippi Gulf coast filed a purported class action lawsuit in the U.S. District Court in the Southern District of Mississippi against more than 45 oil, chemical, utility and coal companies, including the Company. The plaintiffs alleged that defendants' greenhouse gas emissions "were a proximate and direct cause of the increase in the destructive capacity of Hurricane Katrina," and sought damages based on several legal theories. The defendants filed motions to dismiss on the grounds of lack of personal and subject matter jurisdiction. In August 2007, the court granted defendants' motion to dismiss for lack of subject matter jurisdiction finding that plaintiffs' claims are barred by the political question doctrine and for lack of standing. In October 2009, the U.S. Court of Appeals for the Fifth Circuit reversed in part the decision of the trial court, holding that the plaintiffs had standing to assert their public and private nuisance, trespass and negligence claims. The Fifth Circuit held that plaintiffs did not satisfy the prudential standing requirement for their unjust enrichment, fraudulent misrepresentation and civil conspiracy claims and dismissed those claims. The case was remanded to the court for further proceedings. The Company believes that this lawsuit is without merit and intends to defend against and oppose it vigorously, but cannot predict its outcome. Based on the Company's evaluation of the issues and their potential impact, the amount of any future loss cannot be reasonably estimated. However, based on current information, the Company believes this matter is likely to be resolved without a materially adverse effect on its financial condition, results of operations or cash flows.

*Native Village of Kivalina and City of Kivalina v. ExxonMobil Corporation, et al.*

In February 2008, the Native Village of Kivalina and the City of Kivalina filed a lawsuit in the U.S. District Court for the Northern District of California against the Company, several owners of electricity generating facilities and several oil companies. The plaintiffs are the governing bodies of a village in Alaska that they contend is being destroyed by erosion allegedly caused by global warming that the plaintiffs attribute to emissions of greenhouse gases by the defendants. The plaintiffs assert claims for nuisance, and allege that the defendants have acted in concert and are jointly and severally liable for the plaintiffs' damages. The suit seeks damages for lost property values and for the cost of relocating the village. The defendants filed motions to dismiss on the grounds of lack of personal and subject matter jurisdiction. In September 2009, the court granted defendants' motion to dismiss for lack of subject matter jurisdiction finding that plaintiffs' federal claim for nuisance is barred by the political question doctrine and for lack of standing. The plaintiffs are appealing the court's dismissal.

***Other***

In addition, at times the Company becomes a party to other claims, lawsuits, arbitration proceedings and administrative procedures in the ordinary course of business in the U.S., Australia and other countries where the Company does business. Based on current information, the Company believes that the ultimate resolution of such other pending or threatened proceedings is not reasonably likely to have a material adverse effect on its financial position, results of operations or liquidity.

*New York Office of the Attorney General Subpoena*

The New York Office of the Attorney General sent a letter to the Company dated September 14, 2007 that referred to the Company's "plans to build new coal-fired electric generating units," and said that the "increase in CO2 emissions from the operation of these units, in combination with Peabody Energy's other coal-fired power plants, will subject Peabody Energy to increased financial, regulatory, and litigation risks." The Company currently has no electricity generating capacity in place. The letter included a subpoena issued under New York state law, which seeks information and documents relating to the Company's analysis of the risks associated with climate change and possible climate change legislation or regulations, and its disclosure of such risks to investors. The Company believes that it has made full and proper disclosure of these potential risks.

## (21) SUMMARY QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

A summary of the unaudited quarterly results of operations for the years ended December 31, 2009 and 2008 is presented below. In the third quarter of 2009, the Company's Chain Valley Mine in Australia was held for sale and subsequently sold in the fourth quarter of 2009. See Note 2 for additional information regarding the sale. All periods presented below reflect the Chain Valley Mine as a discontinued operation.

| | 2009 | | | |
|---|---|---|---|---|
| *(In millions except per share data)* | *First Quarter* | *Second Quarter* | *Third Quarter* | *Fourth Quarter* |
| Revenues | $1,453.0 | $1,338.2 | $1,667.0 | $1,554.2 |
| Operating profit | 219.7 | 215.4 | 220.3 | 189.4 |
| Income from continuing operations, net of income taxes | 141.2 | 90.0 | 113.2 | 113.5 |
| Net income | 175.2 | 82.0 | 110.8 | 95.0 |
| Net income attributable to common stockholders | 170.0 | 79.2 | 106.8 | 92.2 |
| Basic earnings per share – continuing operations [1] | 0.51 | 0.33 | 0.41 | 0.41 |
| Diluted earnings per share – continuing operations [1] | 0.50 | 0.32 | 0.41 | 0.41 |
| Weighted average shares used in calculating basic earnings per share | 265.3 | 265.4 | 265.7 | 265.8 |
| Weighted average shares used in calculating diluted earnings per share | 267.3 | 267.1 | 267.3 | 267.7 |

[1] *Earnings per share for the quarters may not add to the amounts for the year as each period is computed on a discrete basis.*

Operating profit in the second, third and fourth quarters reflect lower contract pricing in Australia that began in the second quarter. Operating profit in the fourth quarter included an impairment loss of $34.7 million (see "Investments in Joint Ventures" section of Note 1 for additional information). Income from continuing operations, net of income taxes in the first quarter included a benefit of $0.9 million from the remeasurement of non-U.S. income tax accounts while the second, third and fourth quarters included non-cash tax expense of $47.7 million, $22.3 million, and $5.3 million, respectively. Net income in the first quarter included a gain of approximately $35 million (net of income taxes) related to a coal excise tax refund (see Note 2 for additional information).

| (In millions except per share data) | 2008 First Quarter | Second Quarter | Third Quarter | Fourth Quarter |
|---|---|---|---|---|
| Revenues | $1,259.9 | $1,517.6 | $1,889.6 | $1,893.9 |
| Operating profit | 185.0 | 346.0 | 496.6 | 368.7 |
| Income from continuing operations, net of income taxes | 79.5 | 244.9 | 383.2 | 280.3 |
| Net income | 57.9 | 235.8 | 371.8 | 293.6 |
| Net income attributable to common stockholders | 57.0 | 233.3 | 369.5 | 293.1 |
| Basic earnings per share - continuing operations [1] | 0.30 | 0.89 | 1.40 | 1.04 |
| Diluted earnings per share - continuing operations [1] | 0.29 | 0.89 | 1.39 | 1.04 |
| Weighted average shares used in calculating basic earnings per share | 269.2 | 270.0 | 270.2 | 266.1 |
| Weighted average shares used in calculating diluted earnings per share | 271.5 | 271.9 | 271.8 | 267.2 |

[1] *Earnings per share for the quarters may not add to the amounts for the year as each period is computed on a discrete basis.*

Operating profit in the first quarter included a $54.0 million gain on the sale of coal reserves and surface lands (see Note 4 for information). The second, third and fourth quarter operating profits reflect higher contract pricing in Australia that began in the second quarter. The second quarter operating profit also included revenue recovery of $56.9 million on coal supply agreements. Income from continuing operations, net of income taxes for the first and second quarters included non-cash tax expense of $15.8 million and $17.6 million, respectively, from the remeasurement of non-U.S. income tax accounts while the third and fourth quarters included non-cash tax benefits of $62.7 million and $35.9, respectively. Income from continuing operations, net of income taxes in the second quarter also included a tax benefit of $45.3 million due to the reduction in net operating loss valuation allowances (see Note 11 for information). Net income in the first quarter included a loss of approximately $12 million (net of income taxes) related to a coal excise tax refund (see Note 2 for additional information).

## (22) SEGMENT INFORMATION

The Company reports its operations primarily through the following reportable operating segments: "Western U.S. Mining," "Midwestern U.S. Mining," "Australian Mining," "Trading and Brokerage" and "Corporate and Other." Western U.S. Mining operations reflect the aggregation of the Powder River Basin, Southwest and Colorado mining operations, and Midwestern U.S. Mining operations reflects the Company's Illinois and Indiana mining operations. In 2008, the Company renamed its Eastern U.S. Mining segment to Midwestern U.S. Mining segment to better reflect the geography of the continuing operations of that region. The principal business of the Western U.S. Mining, Midwestern U.S. Mining and Australian Mining segments is the mining, preparation and sale of thermal coal, sold primarily to electric utilities, and metallurgical coal, sold to steel and coke producers. For the year ended December 31, 2009, 81% of the Company's total sales (by volume) were to U.S. electricity generators, 17% were to customers outside the U.S. and 2% were to the U.S. industrial sector. Western U.S. Mining operations are characterized by predominantly surface mining extraction processes, lower sulfur content and Btu of coal and higher customer transportation costs (due to longer shipping distances). Conversely, Midwestern U.S. Mining operations are characterized by a mix of surface and underground mining extraction processes, higher sulfur content and Btu of coal and lower customer transportation costs (due to shorter shipping distances). Geologically, Western operations mine bituminous and subbituminous coal deposits, and Midwestern operations mine bituminous coal deposits. Australian Mining operations are characterized by both surface and underground extraction processes, mining various qualities of low-sulfur, high Btu coal (metallurgical coal) as well as thermal coal primarily sold to an international customer base with a small portion sold to Australian steel producers and power generators. The Trading and Brokerage segment's principal business is the brokering of coal sales of other coal producers both as principal and agent, and the trading of coal, freight and freight-related contracts. Corporate and Other includes selling and administrative expenses, net gains on property disposals, costs associated with past mining obligations, joint venture earnings (losses) and revenues and expenses related to the Company's other commercial activities such as generation development, Btu Conversion, clean coal technologies and resource management.

The Company's chief operating decision maker uses Adjusted EBITDA as the primary measure of segment profit and loss. The Company defines Adjusted EBITDA as income from continuing operations before deducting net interest expense, income taxes, asset retirement obligation expense and depreciation, depletion and amortization.

Operating segment results for the year ended December 31, 2009 were as follows:

| (Dollars in millions) | Western U.S. Mining | Midwestern U.S. Mining | Australian Mining | Trading and Brokerage | Corporate and Other | Consolidated |
|---|---|---|---|---|---|---|
| Revenues | **$2,612.6** | **$1,303.8** | **$1,678.0** | **$391.0** | **$27.0** | **$6,012.4** |
| Adjusted EBITDA | **721.5** | **281.9** | **437.8** | **193.4** | **(344.5)** | **1,290.1** |
| Total assets | **3,061.3** | **334.3** | **3,386.8** | **673.0** | **2,499.9** | **9,955.3** |
| Additions to property, plant, equipment and mine development | **78.3** | **104.2** | **70.1** | **1.8** | **6.2** | **260.6** |
| Federal coal lease expenditures | **123.6** | **–** | **–** | **–** | **–** | **123.6** |
| Income (loss) from equity affiliates | **–** | **–** | **–** | **–** | **(69.1)** | **(69.1)** |
| Additions to advance mining royalties | **1.5** | **1.6** | **–** | **–** | **3.0** | **6.1** |

Operating segment results for the year ended December 31, 2008 were as follows:

| (Dollars in millions) | Western U.S. Mining | Midwestern U.S. Mining | Australian Mining | Trading and Brokerage | Corporate and Other | Consolidated |
|---|---|---|---|---|---|---|
| Revenues | $2,533.1 | $1,154.6 | $2,242.8 | $601.8 | $28.7 | $6,561.0 |
| Adjusted EBITDA | 681.3 | 177.3 | 1,016.6 | 218.9 | (247.2) | 1,846.9 |
| Total assets | 3,140.4 | 552.0 | 2,985.9 | 920.3 | 2,097.0 | 9,695.6 |
| Additions to property, plant, equipment and mine development | 140.4 | 30.3 | 62.8 | – | 30.6 | 264.1 |
| Federal coal lease expenditures | 178.5 | – | – | – | – | 178.5 |
| Income (loss) from equity affiliates | – | – | – | – | – | – |
| Additions to advance mining royalties | 2.1 | 2.2 | – | – | 1.7 | 6.0 |

Operating segment results for the year ended December 31, 2007 were as follows:

| (Dollars in millions) | Western U.S. Mining | Midwestern U.S. Mining | Australian Mining | Trading and Brokerage | Corporate and Other | Consolidated |
|---|---|---|---|---|---|---|
| Revenues | $2,063.2 | $987.1 | $1,117.6 | $320.7 | $35.2 | $4,523.8 |
| Adjusted EBITDA | 595.4 | 200.0 | 167.2 | 116.6 | (109.5) | 969.7 |
| Total assets | 2,893.8 | 529.6 | 3,033.3 | 346.8 | 2,278.8 | 9,082.3 |
| Additions to property, plant, equipment and mine development | 175.4 | 34.0 | 167.2 | – | 62.2 | 438.8 |
| Federal coal lease expenditures | 178.2 | – | – | – | – | 178.2 |
| Income (loss) from equity affiliates | – | – | – | – | 14.5 | 14.5 |
| Additions to advance mining royalties | 1.5 | 2.7 | – | – | 3.9 | 8.1 |

A reconciliation of adjusted EBITDA to consolidated income from continuing operations follows:

| (Dollars in millions) | 2009 | 2008 | 2007 |
|---|---|---|---|
| Total adjusted EBITDA | **$1,290.1** | $1,846.9 | $ 969.7 |
| Depreciation, depletion and amortization | **(405.2)** | (402.4) | (346.3) |
| Asset retirement obligation expense | **(40.1)** | (48.2) | (23.7) |
| Interest expense | **(201.2)** | (227.0) | (235.8) |
| Interest income | **8.1** | 10.0 | 7.0 |
| Income tax (provision) benefit | **(193.8)** | (191.4) | 70.7 |
| Income from continuing operations, net of income taxes | **$457.9** | $987.9 | $ 441.6 |

## (23) SUPPLEMENTAL GUARANTOR/NON-GUARANTOR FINANCIAL INFORMATION

Supplemental guarantor/non-guarantor financial information can be located in Note 23 of the Company's consolidated financial statements filed as part of the 2009 Annual Report on Form 10-K with the U.S. Securities and Exchange Commission.

# Stock Price and Performance Information

## MARKET INFORMATION

Our common stock is listed on the New York Stock Exchange, under the symbol "BTU". As of February 12, 2010, there were 1,395 holders of record of our common stock.

The table below sets forth the range of quarterly high and low sales prices (including intraday prices) for our common stock on the New York Stock Exchange during the calendar quarters indicated.

| | *Share Price High* | *Share Price Low* | *Dividends Paid* |
|---|---|---|---|
| **2008** | | | |
| First Quarter | $63.97 | $42.05 | $0.06 |
| Second Quarter | 88.69 | 49.38 | 0.06 |
| Third Quarter | 88.39 | 39.06 | 0.06 |
| Fourth Quarter | 43.99 | 16.00 | 0.06 |
| **2009** | | | |
| First Quarter | **$30.95** | **$20.17** | **$0.06** |
| Second Quarter | **37.44** | **23.56** | **0.06** |
| Third Quarter | **41.54** | **27.19** | **0.06** |
| Fourth Quarter | **48.21** | **34.54** | **0.07** |

## DIVIDEND POLICY

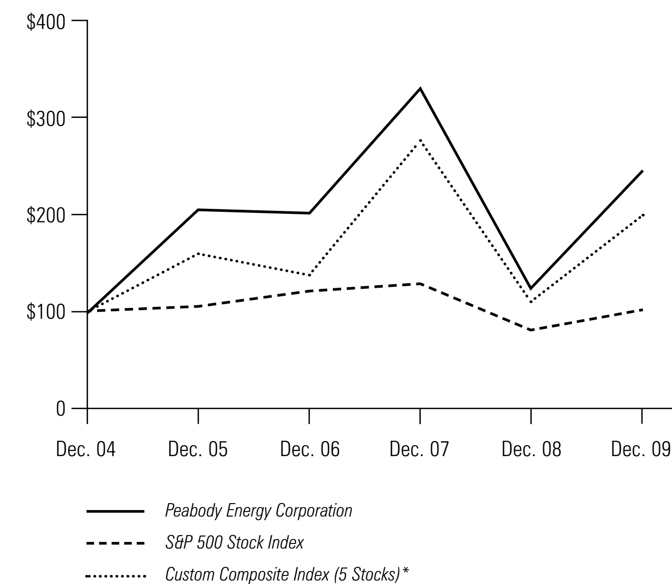
We paid quarterly dividends totaling $0.25 per share and $0.24 per share for the years ended December 31, 2009 and 2008, respectively. Most recently, our Board of Directors declared a dividend of $0.07 per share of common stock on January 27, 2010, payable on March 3, 2010, to stockholders of record on February 10, 2010. The declaration and payment of dividends and the amount of dividends will depend on our results of operations, financial condition, cash requirements, future prospects, any limitations imposed by our debt instruments and other factors deemed relevant by our Board of Directors. Limitations on our ability to pay dividends imposed by our debt instruments are discussed in Management's Discussion and Analysis of Financial Condition and Results of Operations.

## STOCK PERFORMANCE GRAPH

The following performance graph compares the cumulative total return on our common stock with the cumulative total return of the following indices: (i) the S&P 500 Stock Index and (ii) a peer group comprised of Arch Coal Inc., Massey Energy Company, CONSOL Energy, Inc., Alpha Natural Resources, Inc. and International Coal Group, Inc. (Custom Composite Index). The graph assumes that the value of the investment in our common stock and each index was $100 at December 31, 2004. The graph also assumes that all dividends, including the spin-off of Patriot Coal Corporation, were reinvested and that investments were held through December 31, 2009. These indices are included for comparative purposes only and do not necessarily reflect management's opinion that such indices are an appropriate measure of the relative performance of the stock involved, and are not intended to forecast or be indicative of possible future performance of the common stock.

### *Cumulative Total Return*

*(Based upon an initial investment of $100 on December 31, 2004 with dividends reinvested)*




| | Dec. 04 | Dec. 05 | Dec. 06 | Dec. 07 | Dec. 08 | **Dec. 09** |
|---|---|---|---|---|---|---|
| Peabody Energy Corporation | $100 | $205 | $202 | $331 | $123 | **$246** |
| S&P 500 Stock Index | $100 | $105 | $121 | $128 | $ 81 | **$102** |
| Custom Composite Index (5 Stocks)* | $100 | $160 | $138 | $278 | $110 | **$201** |

* *Alpha Natural Resources, Inc. acquired Foundation Coal Holdings Inc. in 2009, and therefore Foundation is no longer included as a stand-alone company in the Custom Composite Index.*

# Global Operations and Reserves

Peabody shipped 244 million tons of coal through sales, trading and brokerage activities in 2009. BTU has access to coal in major regions around the world, including the United States, Australia, Mongolia and Venezuela.

| **Geographic Region/Operation** | **2009 Sales** | **Mine Type** | **Type of Coal** | **Proven & Probable Reserves** |
|---|---|---|---|---|
| **UNITED STATES** | | | | |
| **Powder River Basin** | | | | |
| Caballo | 23.3 | S | T | |
| North Antelope Rochelle | 98.3 | S | T | |
| Rawhide | 15.8 | S | T | |
| **Southwest/Colorado** | | | | |
| Kayenta | 7.5 | S | T | |
| El Segundo | 5.4 | S | T | |
| Lee Ranch | 2.1 | S | T | |
| Twentymile | 7.7 | U | T | |
| Total U.S. West | 160.1 | | | 4,375 |
| **Midwest** | | | | |
| **Illinois** | | | | |
| Gateway | 3.4 | U | T | |
| Cottage Grove | 2.1 | S | T | |
| Wildcat Hills | 0.7 | U | T | |
| Willow Lake | 3.5 | U | T | |
| **Indiana** | | | | |
| Air Quality | 1.6 | U | T | |
| Bear Run | – | S | T | |
| Farmersburg | 3.6 | S | T | |
| Francisco | 2.0 | U | T | |
| Miller Creek | 2.0 | S | T | |
| Somerville Central | 3.4 | S | T | |
| Somerville North | 2.0 | S | T | |
| Somerville South | 1.7 | S | T | |
| Viking | 1.6 | S | T | |
| Other Midwest | 4.2 | | | |
| Total U.S. Midwest | 31.8 | | | 3,566 |
| **AUSTRALIA** | | | | |
| **Queensland** | | | | |
| Burton | 2.5 | S | T/M | |
| Eaglefield | 0.9 | S | M | |
| Millennium | 0.8 | S | M | |
| North Goonyella | 1.8 | U | M | |
| Wilkie Creek | 2.3 | S | T | |
| **New South Wales** | | | | |
| Metropolitan | 1.5 | U | M | |
| North Wambo | 2.3 | U | T/P | |
| Wambo | 1.9 | S | T | |
| Wilpinjong | 8.3 | S | T | |
| Total Australia | 22.3 | | | 1,074 |
| **Trading and Brokerage** | 29.4 | | | |
| **Total Coal Sales** | **243.6** | | | **9,015** |

**Mine Type**
U: Underground
S: Surface/Open Cut

**Type of Coal**
T: Thermal/Steam
M: Metallurgical
P: Pulverized Coal Injection

*Short tons in millions. Results from continuing operations.*

# Board of Directors and Executives

## Directors

**Gregory H. Boyce**
Chairman and
Chief Executive Officer
Peabody Energy

**William A. Coley**
Former Chief Executive Officer
British Energy Group plc

**William E. James**
Founding Partner
RockPort Capital Partners LLC

**Robert B. Karn III**
Former Managing Partner
Arthur Andersen Financial &
Consulting, St. Louis

**M. Frances Keeth**
Former Executive
Vice President
Royal Dutch Shell, plc

**Henry E. Lentz**
Managing Director
Lazard Frères & Co. LLC

**Robert A. Malone**
Former Chairman
and President
BP America Inc.

**William C. Rusnack**
Former President and
Chief Executive Officer
Premcor Inc.

**John F. Turner**
Former U.S. Assistant Secretary
of State for Oceans and
International Environmental
and Scientific Affairs

**Sandra A. Van Trease**
Group President
BJC Healthcare

**Alan H. Washkowitz**
Former Managing Director
Lehman Brothers Inc.

All Directors except Mr. Boyce are independent under New York Stock Exchange listing standards.

**Audit Committee**
William C. Rusnack, Chair
Robert B. Karn III
M. Frances Keeth
Robert A. Malone
Sandra A. Van Trease
Alan H. Washkowitz

**Compensation Committee**
William A. Coley, Chair
William E. James
Robert B. Karn III
M. Frances Keeth
Robert A. Malone
John F. Turner

**Executive Committee**
Gregory H. Boyce, Chair
William A. Coley
Henry E. Lentz
William C. Rusnack

**Nominating & Corporate Governance Committee**
Alan H. Washkowitz, Chair
William E. James
Henry E. Lentz
John F. Turner
Sandra A. Van Trease

## Senior Executives

**Gregory H. Boyce**
Chairman and
Chief Executive Officer

**Michael C. Crews**
Executive Vice President
and Chief Financial Officer

**Sharon D. Fiehler**
Executive Vice President
and Chief Administrative Officer

**Eric Ford**
Executive Vice President
and Chief Operating Officer

**Richard A. Navarre**
President and
Chief Commercial Officer

**Fredrick D. Palmer**
Senior Vice President of
Government Relations

**Alexander C. Schoch**
Executive Vice President Law,
Chief Legal Officer and Secretary

## Executives

**Terry L. Bethel**
Senior Vice President of
Resource Development

**Paul T. Demzik**
President of COALTRADE
International

**Bryan A. Galli**
President of COALSALES

**Christopher J. Hagedorn**
Senior Vice President and
Chief Procurement Officer

**Walter L. Hawkins**
Senior Vice President and
Treasurer

**Jeane L. Hull**
Group Executive of Powder
River Basin Operations

**Delbert Lee Lobb**
Senior Vice President of
Mongolian Operations

**Charles Meintjes**
Senior Vice President of
Engineering and Continuous
Improvement

**Stephen L. Miller**
President of COALTRADE

**Robert L. Reilly**
Senior Vice President of
Business Development

**L. Brent Stottlemyre**
Senior Vice President, Controller
and Chief Accounting Officer

**Vic Svec**
Senior Vice President of
Investor Relations and
Corporate Communications

**Tayeb Tahir**
President of Peabody China

**Julian Thornton**
Managing Director of
Peabody Australia

**Kemal Williamson**
Group Vice President
of Operations

**Lina A. Young**
Senior Vice President of
Marketing and Commercial
Services



# Shareholder Information

### Stock Exchange Listing
Peabody Energy stock is traded on the New York Stock Exchange (NYSE) under the ticker symbol BTU.

### Financial Information
Peabody Energy
701 Market Street, St. Louis, MO 63101-1826
Phone: (314) 342-7900 Fax: (314) 342-7799
E-mail: IR@PeabodyEnergy.com
Web: PeabodyEnergy.com

### Annual Meeting
Peabody Energy will hold its annual shareholders meeting at The Chase Park Plaza Hotel in St. Louis at 10 a.m. on Tuesday, May 4, 2010.

### Independent Auditors
Ernst & Young LLP
190 Carondelet Plaza, Suite 1300
Clayton, MO 63105
Phone: (314) 290-1000 Fax: (314) 290-1882

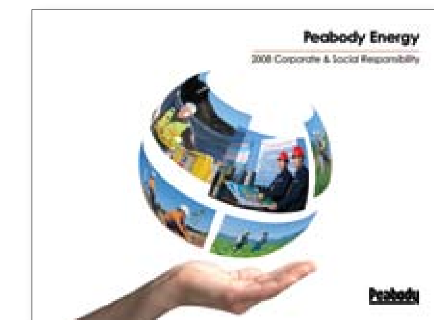
### Transfer Agent
If you have questions regarding your BTU account, please contact your broker, or our transfer agent, American Stock Transfer & Trust Company (AST), at (866) 621-2789 for residents of the United States or Canada, or (718) 921-8347 for residents outside the United States and Canada. AST may also be contacted at Amstock.com. AST can help with dividend reinvestments, lost certificates, transfer of stock to another person and additional services.

### Stock Splits
Shares of BTU split 2-for-1 on March 30, 2005, and again on Feb. 22, 2006.

### Dividends
Peabody pays quarterly dividends on common stock, subject to the approval of the Board of Directors.

### Disclosure Certification
Peabody has included as exhibits to its 2009 Annual Report on Form 10-K, filed with the Securities and Exchange Commission (SEC), certificates of Peabody's Chairman and Chief Executive Officer and Peabody's Executive Vice President and Chief Financial Officer, certifying the quality of the company's public disclosure.

### Report on Corporate and Social Responsibility
Peabody has a longstanding record of good corporate governance and sustainable practices. Our Corporate and Social Responsibility Report assesses progress against priorities and reviews Peabody's actions, positions and policies. Reports may be downloaded at PeabodyEnergy.com.




### Coal Can Do That
For the latest news, blogs, statistics and studies about clean energy solutions from coal, visit CoalCanDoThat.com.

### Peabody and Its Affiliates
The use of the words "Peabody," "the company," and "our" relate to Peabody, our subsidiaries and our majority-owned affiliates.

### Forward-Looking Statements
Some of the information included in this report contains forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, as amended, and is intended to come within the safe harbor protection provided by those sections. These statements relate to future events or our future financial performance. When considering these forward-looking statements, you should keep in mind the cautionary statements in our documents filed with the SEC.

Page 12 Great Plains photo courtesy of Basin Electric Power Cooperative
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