

DOM 1275M
 (Coal Lease)
 (Revised 3/92)
 DNR #10-1126 3/92

STATE OF ALASKA
 DEPARTMENT OF NATURAL RESOURCES
 DIVISION OF MINING AND WATER MANAGEMENT

Coal Lease

LEASE ADL NO: 32144

This lease is entered into between the State of Alaska (referred to in this lease as "the state") and North Pacific Mining Corporation

(referred to in this lease as "the lessee", whether one or more), whose address is:

2525 C Street, Suite 500
 Anchorage, AK 99503
 ATTN: Thomas C Crafford

In consideration of the cash payment made by the lessee to the state, which payment includes the first year's rental and any required cash bonus, and subject to the provisions of this lease, including the stipulation(s) numbered 1-6 attached to this lease and by this reference incorporated in this lease, the state and the lessee agree as follows:

1. GRANT. (a) The state grants to the lessee

(1) the exclusive right to mine and dispose of all the coal in or upon the following tract of land:

PALMER RECORDING DISTRICT

Township 19 North, Range 2 East, Seward Meridian

Section 22: S $\frac{1}{2}$ SW $\frac{1}{4}$, W $\frac{1}{2}$ SE $\frac{1}{4}$

Section 27: N $\frac{1}{2}$, N $\frac{1}{2}$ S $\frac{1}{2}$

Section 28: N $\frac{1}{2}$ SE $\frac{1}{4}$, SE $\frac{1}{4}$ NE $\frac{1}{4}$, S $\frac{1}{2}$ SW $\frac{1}{4}$ NE $\frac{1}{4}$, NW $\frac{1}{4}$ SW $\frac{1}{4}$ NE $\frac{1}{4}$

containing approximately 790 acres, more or less, referred to as the "leased area";

(2) the exclusive right to explore for coal within the leased area;

(3) subject to the lessee obtaining required federal, state and municipal agency permits under paragraph 9 below, for the right to erect, construct, maintain, and use buildings, stockpiles, dumps, drains, roads, pipelines, powerlines, railroads or other improvements, and remove as much soil and occupy as much of the leased area as may be necessary in the mining and removal of coal from the leased area, subject to approval by the state; and

(4) the right to easements to and from the leased area across land owned by the state for purposes reasonably related to the activities of lessee under this lease and along routes to be approved by the state, to be granted in accordance with state statutes and regulations.

(b) Subject to the lessee's compliance with the requirements set out in paragraphs 9 and 10, the lessee may mine and remove the coal by any method consistent with good mining practice, including underground, surface mining, and in situ processes. However, the rights granted by this lease are subject to prior vested mineral rights. In addition, the rights granted by this lease are to be exercised in a manner that will not unreasonably interfere with the rights of any permittee, lessee, or grantee of the state, consistent with the principle of reasonable concurrent uses as set out in article VIII, section 8 of the Alaska Constitution.

(c) The surface use rights granted by this lease may, in the lessee's discretion, be exercised in connection with mining coal from other or adjacent state land when mining on that land is carried on in conjunction with mining coal on the leased area.

(d) For the purposes of this lease, the leased area contains the legal subdivisions as shown on the attached plat marked Exhibit A.

RETURN TO: STATE OF ALASKA, DNR
 DIVISION OF MINING & WATER MGMT
 3801 C ST., SUITE 800
 ANCHORAGE, AK 99503-5935

STATE BUSINESS, NO CHARGE

Exhibit 27

(e) If the leased area is described by protracted legal subdivisions and, after the effective date of this lease, the leased area is surveyed under the public land rectangular survey system, the boundaries of the leased area are those established by that survey, when approved, subject, however, to the provisions of applicable regulations relating to those surveys.

(f) If the state's ownership in the coal in the leased area is less than the entire and undivided interest, the grant under this lease is effective only as to the state's interest in the coal, and the royalties and rentals provided for in this lease must be paid to the state in the proportion that the state's interest bears to the entire undivided fee.

2. RESERVED RIGHTS. (a) The state, for itself and others, reserves all rights not expressly granted to the lessee by this lease. These reserved rights include:

(1) the right to explore for coal in order to conduct geological and geophysical surveys, and to explore for, develop, lease, and remove from the leased area all oils, gases, ores, minerals, fissionable materials, geothermal resources and fossils of ever name, kind or description, other than coal;

(2) the right to establish or grant easements and rights-of-way upon, through, or in the leased area for any lawful purpose, including pipelines, drill holes, shafts, and tunnels necessary or convenient for the working of the leased area for natural resources other than coal or necessary or convenient for access to or the working of other land for any purpose;

(3) the right to manage and dispose of the surface of the leased area or interests in that land by grant, lease, permit, or otherwise to third parties; and

(4) the rights set out in AS 38.05.125 that are not granted by this lease.

(b) The rights reserved pursuant to paragraph 2(a) and AS 38.05.125 shall not be exercised in any manner that unreasonably interferes with lessee's enjoyment of this lease or that endangers lessee's operations under the lease. The state shall provide lessee with prior notice of the state's intent to exercise any rights reserved under paragraph 2(a) or AS 38.05.125 and the opportunity to comment on the proposed exercise of these rights. The parties shall work cooperatively to identify potential conflicts and the state shall require as a condition to the state or any other party's exercise of any reserve rights, such stipulations as appear necessary to avoid unreasonable interference with lessee's enjoyment of this lease or endangerment of lessee's operations.

3. TERM. This lease is issued for an indefinite period of time from the effective date of this lease, subject to all provisions in this lease.

4. COAL MINE GAS AND PEAT. (a) Methane gas and other gases in a mineable coal seam that the state determines are capable of being sold, disposed of, or consumed by the lessee are the property of the state. The lessee shall report the presence of any gas to the state. The lessee may flare or vent gas to the extent necessary for mining safety only if the venting or flaring complies with all federal, state, and local laws, regulations, and ordinances.

(b) Peat overlying a mineable coal seam is the property of the state. The lessee may remove peat if the state determines that removal is necessary in order to extract coal from the leased area. Removed peat must be conserved in a prudent manner until disposed of by the state.

5. RENTAL. (a) The lessee shall pay annual rental to the state in the amount of \$3 per acre or fraction of an acre. However, the state may adjust the annual rental rate as provided by applicable law and regulation not more frequently than every 10 years from the effective date of this lease.

(b) The rental for each year is a credit against the royalty or net profit share as it accrues for that year.

(c) The lessee shall pay the annual rental in advance, on or before the anniversary date of this lease. If the state's or depository's office is not open for business on the annual anniversary date, the time for payment is extended to include the next day on which that office is open for business.

6. RECORDS. The lessee shall keep and have in its possession books and records (including records of expenses) showing the development, production, beneficiation, transportation, and disposition (including records of sales prices, volumes, and purchasers) of all coal produced from the leased area and any other records necessary to justify any items deducted in arriving at an adjusted gross value under paragraphs 33 and 34 of this lease. The lessee shall

permit the state or its agents to examine these books and records at all reasonable times and to make copies of those records. Upon the lessee's request, the state will keep all information under this paragraph confidential in accordance with AS 38.05.035(a)(9). In keeping these books and records, the lessee shall use methods that will ensure the most accurate figures reasonably available to determine the weight, quantity, and character of all leased deposits mined and either marketed or used. The lessee shall use generally accepted accounting principles.

7. LIMITATION ON OVERRIDING ROYALTY. The lessee may not create an overriding royalty, net profits interest, or other payment out of production or revenues from the leased area that would exceed the rate of royalty set out in paragraph 33 of this lease unless the state authorizes a higher overriding royalty under 11 AAC 85.260 or other applicable regulations.

8. PAYMENTS. All payments to the state under this lease must be made payable to the state in the manner directed by the state, and, unless otherwise specified, must be tendered to the state at:

DEPARTMENT OF NATURAL RESOURCES
SUPPORT SERVICES DIVISION, FINANCIAL SERVICES
3601 C STREET, SUITE 1230
ANCHORAGE, AK 99503-5921

or to any depository designated by the state with at least 60 days' notice to the lessee.

9. PLAN OF OPERATIONS AND GENERAL PERMITTING REQUIREMENTS. (a) All coal exploration and surface coal mining operations conducted on the leased area must comply with the provisions of the Alaska Surface Coal Mining Control and Reclamation Act (ASCMCRA) (AS 27.21) and accompanying regulations (11 AAC 90.001--11 AAC 90.911). For any exploration or mining operation exempt from the provisions of ASCMCRA, the lessee shall submit to the state for approval a plan of operations that accords with the principles of ASCMCRA, and may not begin exploration or mining operations on the leased area until the plan has been approved by the state. Before activities requiring permits occur under this lease, permits required for those specific activities must be issued.

(b) If review under NEPA regulations are required (Public Law 91-190) of federal agencies, permits for baseline environmental studies and NEPA implementation will be required.

(c) Federal and state permits which may or may not be required during exploration, development and construction, and production phases, include, but are not limited to: federal Section 10 permits under the Rivers and Harbors Act; federal Section 404 permits under the Clean Water Act; state Habitat permits; state Land Use permits; federal and state Fuel Storage permits, Air Quality permits, Wastewater permits, and Solid Waste Disposal permits.

(d) Before undertaking operations on the leased area, the lessee shall provide under AS 38.05.130 for full payment of all damages sustained by the owner of the surface estate by reason of entering the land.

10. PLAN OF EXPLORATION AND DEVELOPMENT. Within one year after the issuance of this lease, the lessee shall submit to the state for approval one copy of a proposed plan of exploration and development that describes the lessee's plans for exploring and developing the leased area, as set out in 11 AAC 85.215. No exploration or development of the leased area may occur until a plan of exploration and development has been approved by the state.

11. REPORTS. (a) The lessee shall furnish the state, upon request, a copy of all factual data pertaining to the leased area or products from it, including all pertinent tests, records, surveys, and analyses. The data need not include interpretation of these items or proprietary research data or techniques.

(b) With each production royalty payment, the lessee shall submit to the state a statement of the coal sold, disposed of, or consumed, including unwashed coal, washed or otherwise treated coal, and coal developed into liquid or gaseous products or other commercial products by in situ processes or treatment, that is mined or extracted from the leased area. The statement must include the price and proceeds obtained or, where the coal or products are used without sale, evidence of their fair market value, and such other information relating to valuation as the state may require.

(c) If the lessee, or the operator or any contractor for the lessee, discovers a mineral other than coal within the leased area, the lessee

shall promptly notify the state.

(d) If the leased area is part of a unit as described in 11 AAC 85.270, the lessee shall promptly notify the state, in writing, of any change in total estimated reserves if the change affects the state-approved allocation formula referred to in paragraph 15 of this lease.

(e) Any information filed by the lessee with the state in connection with this lease will be available for use by the state. Upon the lessee's request, the state will keep information submitted to the state under this paragraph confidential in accordance with AS 38.05.035(a)(9).

12. TITLE OF THE STATE. The state makes no representations or warranties, express or implied, as to title to, or access to, or quiet enjoyment of, the leased area. The state is not liable to the lessee for any deficiency in title to the leased area, nor is the lessee or any successor in interest to the lessee entitled, due to deficiency in title, to any refund for rentals, bonuses, or royalties paid under this lease.

13. DILIGENT DEVELOPMENT AND CONDUCT OF OPERATIONS. (a) The lessee shall diligently develop the leased area unless consent to suspend operations temporarily is granted by the state. After the lessee is producing coal in commercial quantities from the leased area, or after the leased area has been committed to a coal mining unit from which coal is being produced in commercial quantities, the lessee shall continually operate the mine or mines on the leased area or in the coal mining unit that includes the leased area.

(b) The condition of diligent development is met if, upon review of the lease operations, the state finds that

(1) coal is being produced from the leased area in commercial quantities;

(2) the leased area is committed to a unit under 11 AAC 85.270 and coal is being produced from the unit in commercial quantities;

(3) the lessee is proceeding in good faith to develop the leased area by complying with the approved plan of exploration and development under 11 AAC 85.215(c); or

(4) the lessee has shown to the satisfaction of the state that development in accordance with a plan of exploration and development under 11 AAC 85.215(c) is delayed or interrupted by force majeure.

(c) After the lessee is producing coal in commercial quantities, if operations are interrupted for more than 30 days, the lessee shall promptly notify the state.

(d) The lessee shall perform all operations under this lease in a lawful, prudent, and good workmanlike manner under the plan of exploration and development, with regard for safety, prevention of waste, and preservation and conservation of the leased area for future productive operations. The lessee shall try to avoid damage to and waste of other natural resources not covered by this lease. The lessee shall carry out at the lessee's expense all lawful orders and requirements of the state relative to the lessee's occupation and use of the leased area. If the lessee fails to carry out these orders, the state has, together with any other available legal recourse, the right to enter the leased area to repair damage or prevent waste at the lessee's expense.

14. BINDING EFFECT. This lease and all of its provisions and any attached stipulations extend to and are binding on the heirs, executors, administrators, successors, or assigns of the state and the lessee.

15. COAL MINING UNIT. If it will not violate anti-trust laws, when the reserves in an area have been qualitatively and quantitatively delineated, the leased area may be united with other leased areas under a unit agreement for the development and operation of that area including the leased area upon receiving approval from the state, as provided in 11 AAC 85.270. Any unit agreement encompassing net profit share leases or leases with different royalty rates must include a formula allocating coal production and unit operating costs. The allocation formula and any revision of it must be approved by the state in writing before taking effect. The allocation formula must be revised if a change in the total estimated reserves, referred to in paragraph 11(d) of this lease, results in the allocation formula's no longer protecting the state's financial interest.

16. **INSPECTION.** The lessee shall keep available at all reasonable times, and with prior reasonable notice for inspection by any authorized representative of the state, the leased area, all improvements, machinery, and fixtures on the leased area, and all reports and records relative to operations on or with regard to the leased area or under this lease, except for such documents which are protected under any law, regulation or rule of court. The lessee shall permit the state to copy and make extracts from any such reports and records. All documents entitled to confidentiality pursuant to paragraph 11(b) above shall be kept confidential by the state in accordance with state law.

17. **SUSPENSION.** (a) The lessee may apply for a suspension of operations or production as provided for in applicable statutes and regulations. The state may approve an application for suspension upon a showing of necessity or justification in accordance with statutory and regulatory requirements, or from time to time may, in writing, direct suspension of production or other operations under this lease as provided by law. If the state directs or approves in writing a suspension of all operations on or production from the leased area (except for a suspension necessitated by the lessee's negligence), or if a suspension of all operations on or production from the leased area has been ordered under federal, state, or local law, the lessee's obligation to comply with any express or implied provisions of this lease requiring operations or production will be suspended, but not voided, and the lessee will not be liable for damages for failure to comply with that provision. Upon removal of a suspension, the lessee will have a reasonable time, which will not be less than six months, to resume operations or production.

(b) Nothing in subparagraph (a) suspends the obligation to pay royalties or other production or profit-based payments to the state from operations on the leased area that are not affected by any suspension, or suspends the obligation to pay rentals unless otherwise provided in the terms of the suspension.

18. **ASSIGNMENT.** The lessee may assign, sublease, or transfer this lease, or any interest in or rights under this lease, only upon approval of the state under applicable laws and regulations.

19. **SURRENDER.** The lessee may at any time surrender all or part of the leased area under 11 AAC 82.635.

20. **DEFAULT AND TERMINATION; CANCELLATION.** (a) The failure of the lessee to timely perform its obligations under this lease, or the failure of the lessee otherwise to abide by all express or implied provisions of this lease, is a default in the lessee's obligations under this lease. Whenever the lessee fails to comply with any of the provisions of this lease, and fails, within 30 days after written notice of the default and an opportunity to be heard, to cure the default or to begin and diligently continue to remedy the default, Department of Natural Resources may order suspension of activity on the leased area until compliance is achieved, or may terminate this lease after additional written notice and an opportunity to be heard.

(b) If, at any time while this lease is in effect, or upon termination of this lease for any reason, the lessee has defaulted on this lease, the state may take possession of the property, improvements, and equipment of the lessee on the leased area as security for the payment of rent and royalties due, or to indemnify against any loss or damage sustained by reason of the default of the lessee.

(c) The state may cancel this lease at any time if it determines, after the lessee has been given written notice and a reasonable opportunity to be heard, that (1) continued operations under this lease probably will cause serious harm or damage to biological resources, property, mineral resources, or the environment (including the human environment), (2) the threat of harm or damage will not disappear or decrease to an acceptable extent within a reasonable period of time, and (3) the advantages of cancellation outweigh the advantages of continuing this lease in effect. A cancellation under this subparagraph will not occur unless operations under this lease have been suspended as provided in subparagraph (a) above or in paragraph 17 of this lease or under temporary prohibition by the state continuously for a period of five years or for a lesser period upon request of the lessee. Any cancellation under this subparagraph will entitle the lessee to receive compensation which is determined by the state to be equal to the value of the cancelled rights as of the date of cancellation, with consideration being given to both anticipated revenues from this lease and anticipated costs, including costs of compliance with all applicable regulations and stipulations, liability for clean-up costs or damages, or both, and all other

costs reasonably anticipated under this lease.

21. RIGHTS AND OBLIGATIONS UPON TERMINATION. (a) Upon the termination of this lease as to all or any portion of the leased area, the lessee shall, within a period of one year after the termination, remove from the leased area or portion of the leased area all machinery, equipment, tools, and materials except those items held by the state under paragraph 20(b) of this lease. Upon the expiration of that period and at the option of the state, any machinery, equipment, tools, or materials that the lessee has not removed from the leased area or portion of the leased area become the property of the state and may be removed by the state at the lessee's expense.

(b) If lease operations were exempt from the provisions of the Alaska Surface Coal Mining Control and Reclamation Act, upon termination all improvements must, at the option of the state, either be abandoned and the sites rehabilitated by the lessee to the satisfaction of the state, or be left intact. If they are left intact, the lessee is absolved of all further responsibility as to their maintenance, repair, and eventual abandonment and the rehabilitation of the leased area.

(c) Subject to the conditions set out in this paragraph, the lessee shall deliver up the leased area or portion of the leased area in good condition.

22. DAMAGES AND INDEMNIFICATION. (a) No rights under the AS 38.05.125 reservation may be exercised by the lessee until the lessee has provided to pay the owner of the land on which the reserved rights are sought to be exercised full payment for all damages sustained by the owner by reason of entering the land. If the owner for any reason does not settle the damages, the lessee may enter the land in the exercise of the AS 38.05.125 reserved rights after posting a surety bond determined by the state, after notice and an opportunity to be heard, to be sufficient as to form, amount, and security to secure to the owner payment for damages, and may institute legal proceedings in a court of competent jurisdiction in the judicial district where the land is located to determine the damages that the owner of the land may suffer. The lessee agrees to pay for any damages that may become payable under AS 38.05.130 or by reason of its failure to comply with the reasonable concurrent use requirements of paragraph 1(b) of this lease and article VIII, section 8 of the Alaska Constitution and to indemnify the state and hold it harmless from and against any claims, demands, liabilities, and expenses arising from or in connection with such damages. The state will regard the furnishing of a bond in compliance with this paragraph as sufficient provision for the payment of all damages that may become payable under AS 38.05.130 by virtue of this lease.

(b) The lessee shall indemnify the state for, and hold it harmless from, any claim, including claims for loss or damage to property or injury to any person, caused by or resulting from any act or omission committed under this lease by or on behalf of the lessee. The lessee is not responsible to the state under this subparagraph for any loss, damage, or injury caused by or resulting from the sole negligence of the state.

(c) The lessee expressly waives any defense to an action for breach of a provision of this lease, or to an action for damages, where such defense is based on the fact that the act or omission complained of was committed by an independent contractor. The lessee expressly agrees to assume responsibility for all actions of its independent contractors.

(d) As used in this paragraph and in paragraph 9(b), "owner" means one or more persons, jointly or severally, in whom is vested (1) all or part of the legal title to property or (2) all or part of the beneficial ownership and a right to present use and enjoyment of the property.

23. BONDS. (a) The lessee shall furnish a bond or evidence of an existing bond before lease issuance in an amount equal to at least \$5 per acre or fraction of an acre contained in the leased area, but not less than \$5,000, and shall maintain that bond as long as required by the state, in accordance with 11 AAC 85.245.

(b) The state may, after notice to the lessee and a reasonable opportunity to be heard, require a bond in a reasonable amount greater than the amount specified in (a) above where a greater amount is justified by the nature of the surface and its uses and the degree of risk involved in the types of operations being or to be carried out under this lease.

24. AUTHORIZED REPRESENTATIVES. The director of the Division of Mining, Department of Natural Resources, State of Alaska, and the person executing this lease on behalf of the lessee will be the authorized representatives of their

respective principals for the purposes of administering this lease. The state or the lessee may change the authorized representative or the address to which notices to that representative are to be sent by a notice given in accordance with paragraph 25. When activities under a plan of operations are underway, the lessee shall also designate, in a notice under paragraph 25, by name, job title, and address, an agent who will be present in the state during all lease activities.

25. NOTICES. (a) Any notices required or permitted under this lease must be by electronic media producing a permanent record or in writing and must be given personally or by registered or certified mail, return receipt requested, addressed as follows:

TO THE STATE:
DIRECTOR, DIVISION OF MINING &
WATER MANAGEMENT
DEPARTMENT OF NATURAL RESOURCES
3601 C STREET, SUITE 800
ANCHORAGE, ALASKA 99503-5935

TO THE LESSEE:
NORTH PACIFIC MINING CORPORATION
2525 C STREET, SUITE 500
ANCHORAGE, AK 99503
ATTN: THOMAS C CRAFFORD

(b) Any notice given under (a) of this paragraph will be effective when received by the representative specified in (a).

26. STATUTES AND REGULATIONS. This lease is subject to all applicable state and federal statutes and regulations in effect on the effective date of this lease, and to all statutes and regulations placed in effect after the effective date of this lease. A reference to a statute or regulation in this lease includes any change in that statute or regulation, whether by amendment, repeal and replacement, or other means. This lease does not limit the power of the State of Alaska or the United States of America to enact and enforce legislation or to adopt and enforce regulations affecting, directly or indirectly, the activities of the lessee or its agents in connection with this lease or the value of the interest held under this lease.

27. INTERPRETATION. This lease is to be interpreted in accordance with the rules applicable to the interpretation of contracts made in the state. The paragraph headings are not part of this lease and are inserted only for convenience. The state and the lessee expressly agree that the laws of the State of Alaska will apply in any judicial proceeding affecting this lease.

28. INTEREST IN REAL PROPERTY. It is the intention of the parties that the rights granted to the lessee by this lease constitute an interest in real property in the leased area.

29. WAIVER OF CONDITIONS. The state reserves the right to waive any breach of a provision of this lease, but any such waiver extends only to the particular breach so waived and does not limit the rights of the state with respect to any future breach; nor will the waiver of a particular breach prevent cancellation of this lease for any other cause or for the same cause occurring at another time. Notwithstanding the foregoing, the state will not be deemed to have waived a provision of this lease unless it does so in writing.

30. SEVERABILITY. If it is finally determined in any judicial proceeding that any provision of this lease is invalid, the state and the lessee may jointly agree by a written amendment to this lease that, in consideration of the provisions in that written amendment, the invalid portion will be treated as severed from this lease and that the remainder of this lease, as amended, will remain in effect.

31. CONDITIONAL LEASE. If all or a part of the leased area is land that has been selected by the State of Alaska under laws of the United States granting land to the state, but the land has not been patented to the state by the United States, then this lease is a conditional lease as provided by law until the patent becomes effective. If for any reason the selection is not finally approved, or the patent does not become effective, any rental, royalty, or other production or profit-based payments made to the state under this lease will be not be refunded.

32. DEFINITIONS. All words and phrases used in this lease are to be interpreted consistently with AS 01.10.040. However, the following words have the following meanings unless the context unavoidably requires otherwise:

(1) "commercial quantities" means a quantity of coal sufficient to yield a return in excess of operating costs, even if exploration and development costs may never be repaid and the undertaking considered as a whole may ultimately result in a loss;

(2) "continued operation" means production of coal in commercial quantities, except when operations under the lease are suspended with approval of the state or interrupted by force majeure;

(3) "force majeure" means strikes, the elements, or casualties not attributed to the lessee;

(4) "proceeding in good faith to develop" means complying with the plan of exploration and development referred to in paragraph 10 of this lease;

(5) "reasonable beneficiation costs" means the reasonable costs of any processing performed before sale that adds value to the coal as compared to its run-of-mine value; these deductible processing costs include the costs of grinding, washing, drying, grading, sorting, briquetting, any other means of beneficiation, and any reasonable transportation costs necessitated solely by this beneficiation; primary crushing, loading, and storing costs are not included, whether or not they are incurred on or away from the leased area;

(6) "reasonable transportation costs" means the actual costs of transportation after the coal leaves the mine mouth, including the use of tankers, roads, conveyor belts, trucks, rail transportation, and slurry pipelines; if the transportation facilities are owned by the lessee, then actual costs are limited to direct operating expenses and depreciation on capital equipment and do not include overhead or an internal rate of return on the capital investment; the state may determine the reasonable transportation costs when any of the following conditions exist:

(A) the transportation contract is not an arm's-length transaction or is not representative of the market value of the transportation; or

(B) the method of transportation is not reasonable in view of existing alternative methods of transportation;

(7) "mine mouth" means the tippie, railroad, or other loadout facility, where the coal is initially weighed or measured and loaded for transport to a buyer or user;

(8) "point of extraction" means that point where the coal first enters the lessee's coal transport system;

(9) "point of sale" means the point of first transfer for value, if title also transfers, or point of entry into a free marketplace;

(10) "underlifted coal" means coal not taken by the state when the state by choice takes less than its in-kind royalty share of production.

33. ROYALTY ON PRODUCTION. (a) The lessee shall pay to the state as a royalty 5 percent in amount or value of the adjusted gross value of coal from the leased area that is sold, disposed of, or consumed.

(b) If the lessee produces any liquid or gaseous hydrocarbon or other substance by any in situ process or synthetic fuel process for treatment of coal produced from the leased area, whether by chemical or mechanical means or a combination of chemical and mechanical means, the royalty is 5 percent in amount or value of the adjusted gross value of that product that is sold, disposed of, or consumed; however, if the product is sold away from the leased area, then the reasonable transportation costs from the mine mouth to the point of sale will be deducted from the gross value of that product before computing the royalty.

(c) The state may adjust the royalty rate and the method of calculation set out in subparagraphs (a) and (b) above not more frequently than every 10 years, with the first adjustment not sooner than 10 years after the lease's effective date, in accordance with 11 AAC 85.220.

34. ROYALTY IN VALUE. (a) Unless the state elects to receive all or a portion of its royalty in kind as provided in paragraph 35 of this lease, the lessee shall pay to the state the value of all royalty on coal as determined under this paragraph. Royalty paid in value must be free and clear of all lease expenses, unless expressly provided for in (b) of this paragraph, and of any portion of those expenses incurred away from the leased area. All royalty that may become payable in money to the state must be paid no later than the last day of the calendar month following the month in which the coal is produced. The amount of all royalty-in-value payments that are not paid when due under this lease or that are subsequently determined to be due as the result of a redetermination will bear interest from the date the obligation accrued, until it is paid in full, at a variable annual rate equal to 1.25 percent plus the prime rate as announced from time to time by the Bank of America, San Francisco, California.

(b) In this lease, if the coal is sold in a bona fide arm's-length transaction between independent parties, "adjusted gross value" is the full consideration received by the lessee minus the following costs if those costs were borne by the lessee:

(1) reasonable beneficiation costs as defined in paragraph 32 of this lease, and

(2) reasonable transportation costs from the mine mouth to the point of sale, as defined in paragraph 32 of this lease.

(c) The state will allow deductions under (b) of this section when the state determines that the lessee has provided an accurate account and description of the reasonable costs. All deductions claimed are subject to audit by the state.

(d) The state will determine the adjusted gross value of the coal, taking into account the consideration being paid for coal in the same general area or other relevant areas, including areas outside Alaska, reasonable transportation costs, reasonable beneficiation costs, and other relevant factors including the composition and special characteristics of the deposit, and the Btu content of the coal, if the state determines that coal from the leased area is

(1) sold or disposed of in other than a bona fide arm's-length transaction between independent parties;

(2) sold or disposed of under a contract that sets a single price for coal without adjustments tied to market conditions;

(3) sold or disposed of under a contract that does not reflect the value of the coal at the time the coal is produced; or

(4) consumed by the lessee.

(e) The state may, upon petition by the lessee, convert the percent-of-value royalty rate to a comparable cents-per-ton rate in a written determination that states that it is in the best interest of the State of Alaska to make the conversion and that the state has adequate information to make an adjustment that is equitable to the state and the lessee. This cents-per-ton rate will be readjusted as necessary to reflect changes in adjusted gross value.

(f) When requested by the state, the lessee shall promptly file with the state all information relating to royalty value computation.

35. ROYALTY IN KIND. (a) At the state's option, which may be exercised from time to time upon not less than nine months' notice to the lessee, the lessee shall deliver all or a portion of the state's royalty coal from the leased area in kind, in good and merchantable condition and free and clear of all lease expenses and of any portion of those expenses incurred away from the leased area. The lessee shall deliver the royalty coal free of charge into a regulated common carrier or other transportation facility on the leased or unit area, or onto storage piles on the leased or unit area, designated by the state. The lessee is not required to provide free storage for longer than 30 days or pay slurry pipeline charges for any coal run into storage piles or into slurry pipelines. The state may elect to receive the royalty coal at the point of sale or any other established unloading or transfer point between the lease and the point of sale, but the lessee is not required to pay delivery and handling costs incurred after the coal leaves the leased area, or, if the lease is part of a unit as described in 11 AAC 85.270, after the coal leaves the unit. The lessee is not liable for the loss or destruction of stored royalty coal from causes beyond the lessee's reasonable control.

(b) Deliveries of royalty coal to the state must accord with a schedule setting out the dates, places of delivery, and amounts of coal to be taken, to be submitted by the state before the beginning of each quarter during which coal is taken in kind. The state may take more or less than its royalty share at any one delivery during each quarter; however, at the end of each quarter, the total amount taken by the state must be equivalent to its royalty share for that quarter. If a royalty purchaser from the state refuses or for any reason fails to take delivery of coal, or, in an emergency and with as much notice to the lessee as is practical or reasonable under the circumstances, the state may elect without penalty to underlift for up to 10 months all or a portion of the state's royalty coal produced from the leased or unit area and taken in kind. The state's right to underlift is limited to the portion of royalty coal that the royalty purchaser refused or failed to take delivery of or the portion necessary to meet the emergency condition. Underlifted coal may be recovered by the state in subsequent deliveries in amounts not to exceed 50 percent of the royalty interest share taken at each delivery during the underlift recovery, in

accordance with the schedule to be submitted by the state before each quarter during which coal is taken in kind.

(c) After having given notice of its intention to take, or after having taken, its royalty in kind, the state, at its option and upon nine months' notice to the lessee, may elect to receive a different portion or none of its royalty in kind.

36. REDUCTION OF RENTAL AND ROYALTY. The state may reduce the lessee's obligations to pay royalty on all of the leased area or on any tract or portion of the leased area segregated for royalty purposes, or may waive, suspend, refund, or reduce the rental on all or any portion of the leased area, in accordance with applicable statutes and regulations.

37. EFFECTIVE DATE. This lease takes effect Sep 1, 1995.

BY SIGNING THIS LEASE, the state as lessor and the lessee agree to be bound by its provisions.

STATE OF ALASKA

By: [Signature]
Title: Director DMWM

LESSEE

By: [Signature]
Title: Vice President

STATE OF ALASKA

Third Judicial District) ss.

This is to certify that on August 30, 1995, before me appeared Thomas C. Crafford, who executed this lease and acknowledged voluntarily signing it.

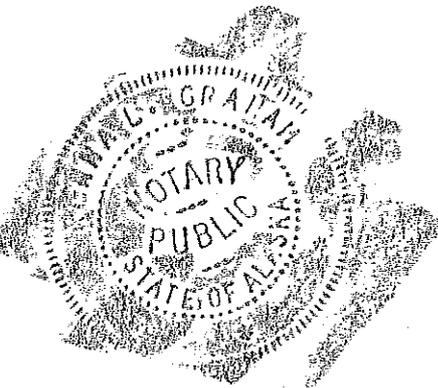


[Signature]
Notary public in and for Alaska
My commission expires: Oct 10, 1997

STATE OF ALASKA

Third Judicial District) ss.

This is to certify that on August 31, 1995, before me appeared Jules Tlestan of the Division of Mining and Water Management of the State of Alaska, Department of Natural Resources, who executed this lease and acknowledged voluntarily signing it on behalf of the State of Alaska as lessor.



[Signature]
Notary public in and for Alaska
My commission expires: Oct 10, 1997

Stipulations

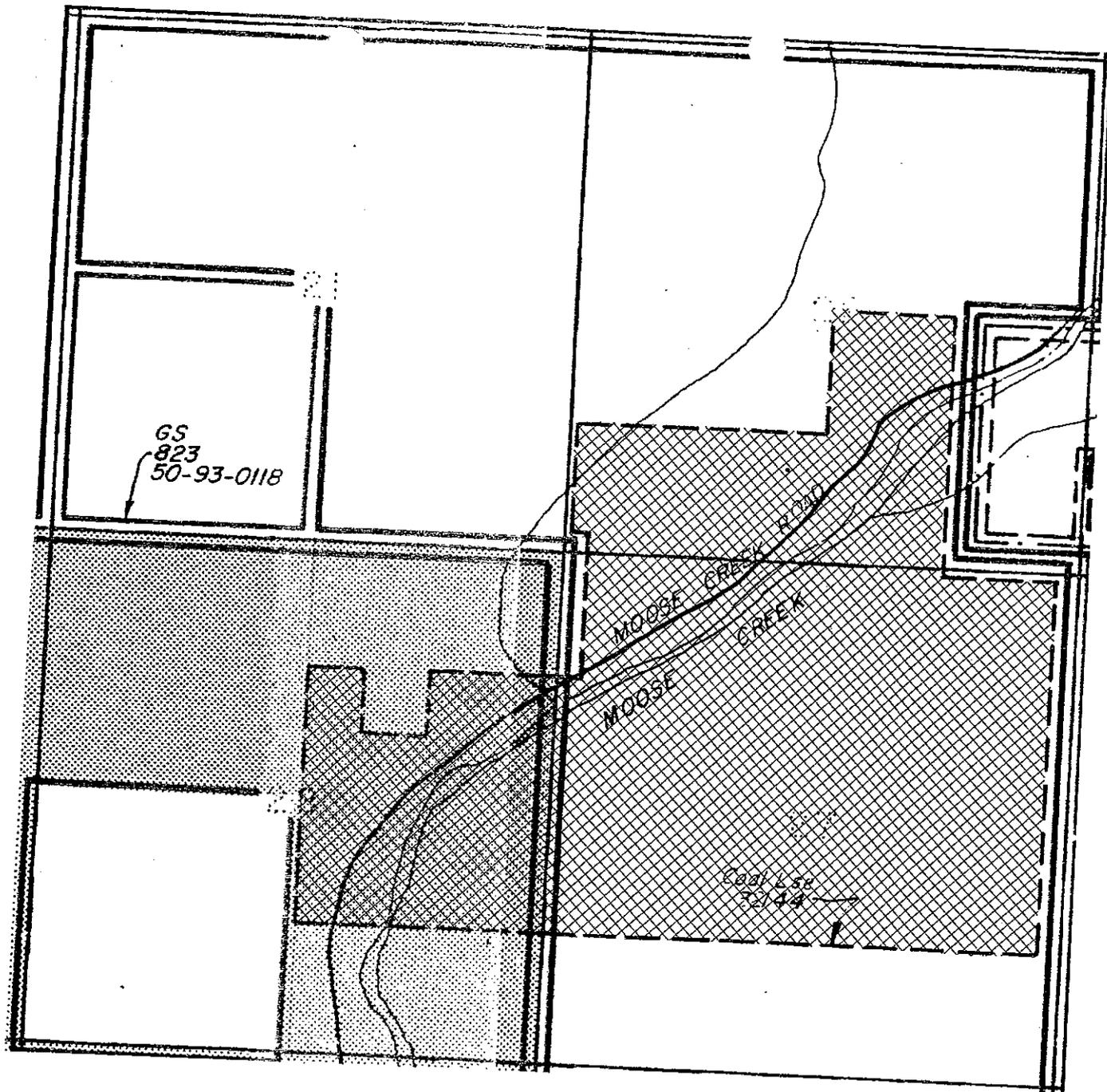
This lease is subject to special conditions and stipulations that have been determined by the Director of the Division of Mining and Water Management to be in the best interests of the State (AS 38.05.035(e)). Those conditions and stipulations are:

1. Permanent roads may not be constructed during exploration unless the Commissioner of the Department of Natural Resources determines that such construction is in the state's best interest because it (1) serves a state objective for use of other resources or (2) is reasonably necessary for the development of commercial coal deposits.
2. A performance bond according to the provisions of 11 AAC 90.167 will be required for exploration activities that substantially disturb the natural land surface.
3. Public access to, and use of, the leased area will not be restricted as a consequence of coal activities except in the vicinity of mines, buildings and other mine-related structures, and for safety reasons. Areas where access will be restricted must be identified in applications for an exploration permit or surface mine permit. No facilities or operations may be located where they would block existing access routes (as determined by the Department of Natural Resources in consultation with the Department of Fish and Game) for hunting, fishing, or public recreation, unless an alternative access route approved by the Department of Natural Resources, after consultation with the Department of Fish and Game, is provided. No facilities or operations may be located where they would block public access to navigable and public waters as defined in AS 38.05.365(22) and AS 38.05.365(23). If facilities are proposed to be located in the vicinity of navigable or public waters, an easement will be reserved under AS 38.05.127 and 11 AAC 53.330 to ensure the right of public access.
4. If only the subsurface estate is owned by the state, or if the surface is owned by the state but subject to third party interests, including native allotments, the lessee must not enter upon such land until the lessee makes a good faith effort to agree with the surface interest holder on settlement of damages that may be caused by lease activities. If an agreement cannot be reached, the Director of the Division of Mining and Water Management has the authority to approve the activity, provided adequate provisions have been made with the state to pay for any damages the surface interest holder may suffer.
5. Should the lessee or its contractors discover a historic or archeological find, it must immediately report the discovery to the director of the Division of Mining and Water Management and make every effort to prevent damage to the find until the director, after consultation with the Office of History and

Archeology, has given directions as to its preservation or disposition.

6. Where the state is owner of the surface estate, the post-mining land use will be that use or uses which the disturbed area was capable of supporting before mining, or if so provided by the Matanuska Valley Moose Range Management Plan at the time the Surface Mining Permit application was filed, such higher or better use or uses achievable under 11 AAC 90.481.

rlg\coal\sti



COAL LEASE ADL 32144

Township 19 North, Range 2 East, Seward Meridian

Section 22: S $\frac{1}{2}$ SW $\frac{1}{4}$, W $\frac{1}{2}$ SE $\frac{1}{4}$

Section 27: N $\frac{1}{2}$, N $\frac{1}{2}$ S $\frac{1}{2}$

Section 28: N $\frac{1}{2}$ SE $\frac{1}{4}$, SE $\frac{1}{4}$ NE $\frac{1}{4}$, S $\frac{1}{2}$ SW $\frac{1}{4}$ NE $\frac{1}{4}$, NW $\frac{1}{4}$ SW $\frac{1}{4}$ NE $\frac{1}{4}$

containing approximately 790 acres, more or less.