



## 2004 Results

North American Coal (“NACoal”) operates six surface lignite coal mining operations which delivered 34.4 million tons of lignite coal in 2004 compared with 35.5 million tons in 2003, maintaining NACoal’s position as the nation’s largest lignite coal producer and among the top ten coal producers nationwide. Lignite coal deliveries

recognized in 2003. However, these favorable results were partially offset by increased employee-related costs and increased costs at the Mississippi Lignite Mining Company.

During 2004, NACoal was awarded an investment-grade rating (BBB low) by Dominion Bond Rating Services, an accredited rating agency with expertise in the mining industry,



# THE NORTH AMERICAN COAL CORPORATION

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decreased primarily due to reduced customer fuel requirements caused by an increase in scheduled and unscheduled customer power plant outages. The company’s lignite coal reserve position, including reserves related to unconsolidated project mining operations, remains strong with a total of 2.4 billion tons, of which 1.3 billion tons are committed to current customers.

NACoal’s limerock dragline mining operations had an excellent year, with limerock deliveries 72 percent higher in 2004 compared with 2003. Deliveries were 18.9 million cubic yards of limerock during 2004 compared with 11.0 million cubic yards during 2003. Increased limerock deliveries in 2004 were primarily attributable to the start-up of new limerock dragline mining operations in the fourth quarter of 2003 and the second quarter of 2004.

NACoal had a strong year in 2004, with net income increasing 30 percent over 2003. Net income in 2004 was \$18.6 million compared with \$14.3 million in 2003. This increase resulted primarily from the addition of new limerock dragline mining operations, better performance at the San Miguel Lignite Mining Operations (“San Miguel”), increased royalty income, lower interest expense and the absence of a \$1.3 million charge for the cumulative effect of an accounting change

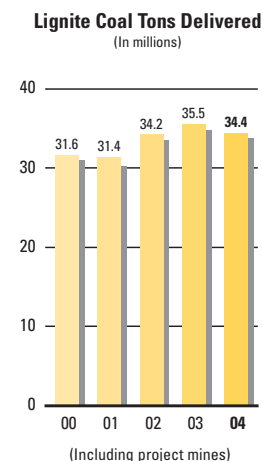
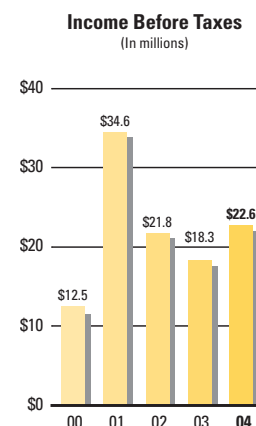
in conjunction with the company’s private placement of \$35 million of unsecured senior notes in October 2004. An additional placement of \$10 million in January 2005 increased the total amount funded to \$45 million. The company believes it is the only operating coal company in the United States with an investment-grade rating.

## Vision, Strategy and Core Competencies

NACoal’s vision is to be the leading low-cost miner of lignite coal used in power generation and coal gasification plants and to provide selected value-added mining services for other natural resources companies.

NACoal’s strategy is to leverage low-cost mining expertise at existing mines while pursuing new mining opportunities.

Core competencies supporting this strategy include operating mines in a safe, low-cost and environmentally responsible manner through disciplined, efficient and responsible processes; fostering successful, long-term partnerships with power generating customers; and analyzing regional opportunities, understanding new coal-based power generating technologies and identifying potential partners for future development.



*Left: North American Coal’s limerock dragline mining operation at the Krome Quarry in South Florida.*

## **Key Programs to Enhance Profitability**

**Employee safety.** Employee safety is the number-one priority at NACoal. Each of the mines emphasizes safety as part of its daily routine. Red River Mining Company (“Red River”) has not had a lost-time accident since it began operations in 1989. In addition, five of the company’s seven operations worked the entire 2004 calendar year without incurring a single lost-time accident. NACoal continues to believe that its commitment to safety and strong employee relations improves productivity and employee retention and thereby enhances profitability.

**Mississippi Lignite Mining Company.** Because this mine and its customer’s power plant were fully operational for all of 2004, NACoal was able to aggressively focus on achieving planned profitability through the application of its extensive mining expertise. In 2004, the mine gained efficiencies by using power plant ash, a waste product from the process of burning coal, on its roads to significantly enhance the productivity of trucks used to haul lignite coal. However, mining efficiency was affected in 2004 by certain adverse geological conditions in the current mining area and by mining through a hill, which required the removal of an unusually large amount of soil to reach the lignite coal below. Mining efficiency is expected to continue to be affected by these factors in 2005. Improvements in mining efficiency and profitability are expected during 2006.

**San Miguel Lignite Mining Operations.** NACoal continues to mine more lignite coal at this mine than originally anticipated, which has positively affected volume but resulted in higher mining costs, increased equipment needs and higher equipment maintenance costs. These growing cost pressures were not covered by contractual cost escalators, which historically resulted in significant losses at this operation. In early 2004, NACoal renegotiated the contract with the operation’s customer in order to reduce near-term losses. This amended contract also is expected to continue to solidify a strong working relationship with the customer. Because of this amended contract, results at San Miguel improved significantly in 2004 compared with

2003. The company currently anticipates that San Miguel will return to profitability by 2007, the final year of the contract.

**Innovative mining methods.** NACoal continues to be a leader in developing innovative mining methods, which have improved mining efficiencies and coal recovery, reduced costs, enhanced safety and lessened the environmental impact of mining. These methods, also described in previous Annual Reports, include:

- Utilizing Easi-Miners, equipment resembling road resurfacers, to extract thinner seams of coal, thereby improving coal recovery and reducing costs.
- Designing a unique slurry wall dewatering system at Red River in Louisiana. This system enables workers to mine lignite coal safely and efficiently in flood plain areas.
- Developing specialized non-stick linings for the inside of truck beds and buckets on earth-moving equipment to improve efficiencies and lower costs.
- Using special proprietary software to track equipment utilization and optimize service intervals for lower overall maintenance costs.

**Environmental commitment.** NACoal is committed to protecting the environment by restoring mined land to its original or an improved condition. The company has been a prominent recipient of environmental awards over the years.

## **Key Programs to Generate Growth**

**Lignite coal reserve development strategies.** The foundation for new lignite coal mining projects continues to be the ongoing, in-depth analysis of power generation supply and demand in each of the regions where NACoal has reserves. In areas where future power generation demand outpaces supply, there is potential for the development of new power plants, which could utilize lignite coal owned or controlled by NACoal. Based on results of this ongoing analysis, NACoal adjusts ownership plans for existing lignite coal reserves as well as strategies to secure ownership or leases for additional reserves which offer potential for future development. In addition, NACoal owns



*NACoal continues to be a leader in developing innovative mining methods, which have improved mining efficiencies and reduced costs*



*Above: At The Sabine Mining Company's South Hallsville #1 Mine in Texas, an Easi-Miner loads lignite coal into a 160-Ton Capacity Bottom Dump Truck, which will deliver the lignite coal to the customer's power generation facility adjacent to the mine.*

what it believes is the most extensive bank of geological data on lignite coal reserves in the country, consisting of data on company-owned reserves as well as lignite coal reserves owned or controlled by others. This wealth of data provides a strategic advantage to NACoal as it works to identify, prioritize and pursue opportunities to develop its own reserves as well as other new contract mining opportunities utilizing lignite coal reserves owned by others.

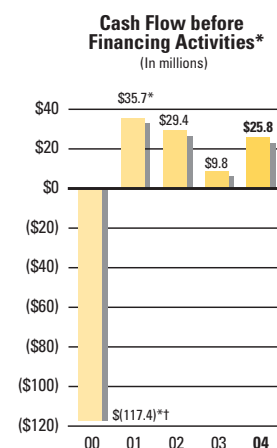
**Limerock dragline mining projects.** The company continues to be very optimistic that niche growth opportunities to provide high-value-added services for other natural resource mining applications, such as limerock dragline mining services, will continue to emerge. Discussions are ongoing with NACoal's existing limerock customers, as well as other potential new customers, about their future increased limerock requirements.

NACoal provided dragline mining services at Rinker Materials of Florida Inc.'s ("Rinker") Krome Quarry for its first full year in 2004, with the company delivering more limerock than expected. That mining service agreement has a seven-year term that ends in 2010 and includes three potential one-year extensions. In addition, mining commenced at Rinker's Alico Quarry in the third quarter of 2004. This contract runs through 2011. In 2004, NACoal signed new agreements with White Rock Quarries ("WRQ") for the

expansion of limerock dragline mining services at the current White Rock Quarry location and new locations at that same quarry beginning in 2005. These agreements extend through 2020 and 2009, respectively. Finally, in early 2005, NACoal signed agreements with Rinker to start mining at Rinker's FEC Quarry in late 2005 and with WRQ to start mining at WRQ's new quarry, White Rock Quarry South, in late 2006 or early 2007. These agreements run through 2013 and 2016, respectively. All of these operations are located in Florida.

**Corporate Initiatives**

Central to NACoal's successes are its efforts to minimize exposure to the market price of coal. This goal is accomplished through carefully structured coal supply agreements, which essentially establish the specific mining services that NACoal will perform for its customers and the mechanisms by which it will be compensated for performing those activities. Because NACoal is selling its services in addition to its coal, these agreements include various cost escalation mechanisms and may include performance incentives. Through these mining agreements, NACoal and its customers share a common goal of minimizing costs. By eliminating speculation on the future price of coal, these contracts allow the company to consistently earn sound margins for its services and earn, on a regular basis, returns on capital employed substantially in excess of the company's cost of capital.



\* Cash Flow before Financing Activities for 2000 and 2001 has not been restated to reflect the 2003 adoption of FIN No. 46 retroactive to January 1, 2002.

† Includes the Phillips Coal asset acquisition

The expected outcome of NACoal's overall strategy is the profitable operation of all existing mines coupled with the development of new mines that utilize the company's lignite coal reserves or its mining experience.

### Outlook for 2005 and Beyond

NACoal's financial objectives are to earn a minimum return on capital employed of 13 percent, attain positive Economic Value Income from all existing consolidated mining operations as well as any new projects, maintain or increase the profitability of all existing unconsolidated project mining operations and deliver substantial consolidated cash flow before financing activities.

In addition to key programs outlined previously, NACoal is working to improve profitability at Red River. Certain adverse geological conditions have recently contributed to slightly higher mining costs than anticipated,

technologies involves gasifying coal, which can significantly reduce key emissions, such as SO<sub>2</sub> (sulfur dioxide), NO<sub>x</sub> (nitrous oxides), particulate matter and mercury, and create an opportunity to produce marketable byproducts, such as synthetic diesel or jet fuel. This highly efficient process of coal gasification also produces lower levels of CO<sub>2</sub> (carbon dioxide) and allows for CO<sub>2</sub> separation and sequestration. This process can also extract hydrogen, which can be used in fuel cells to produce emission-free power generation.

The company continues to invest significant effort in understanding and promoting these new clean coal power technologies. In fact, NACoal has developed its own flexible power plant vision, called FlexGen, which would allow power companies to generate power from natural gas, coal-based synthetic gas or fuel cells to produce a variety of byproducts, including hydrogen, and to significantly reduce, or even eliminate, many



*As NACoal implements its programs, the company anticipates further improvement in return on capital employed, particularly in 2006–2007*

and the customer continues to take only the contractual minimum number of tons. The company is working to develop a solution to its temporary mining challenges in the near term and expects that the mine will experience improved geological mining conditions in the long term. The company's objective is to work with the customer to increase deliveries over the long term, which would add significantly to profitability.

With implementation of all of NACoal's programs, the company anticipates further improvement in return on capital employed, particularly in 2006 and 2007, as well as increased cash flow before financing activities.

NACoal believes that in the long term, future development of coal reserves in the United States will depend greatly upon the adoption of newer power plant technologies that substantially lower emissions. One of the most promising new

harmful emissions, including CO<sub>2</sub>. In the context of sustained, relatively high natural gas prices in the United States, it is the company's hope that adoption of new coal-based technologies will create new lignite coal mining opportunities.

Finally, I would like to thank all NACoal employees for their hard work and dedication in making 2004 another safe and successful year for the company. I look forward to working with all of our employees to accomplish our goals in 2005.



*Clifford R. Miercort*

**Clifford R. Miercort**  
President and Chief Executive Officer  
The North American Coal Corporation

*Right: At The Coteau Properties Company's Freedom Mine in North Dakota, an Electric Shovel loads overburden, or soil that must be removed to mine the lignite coal below, into a Caterpillar End Dump Truck.*