



Peter Goldmark
Washington State
Commissioner of Public Lands

January 5, 2017

Mr. Mark Stiffler
Alcoa Corporate Center
201 Isabella Street
Pittsburgh, PA 15212-5858

Re: Denial of Consent to Sublease Aquatic Lands Lease No. 20-B09222

Dear Mr. Stiffler:

After careful consideration, the Department of Natural Resources has denied Northwest Alloys' request for consent to sublease to Millennium Bulk Terminals, LLC (Millennium) under Aquatic Lands Lease No. 20-B09222. As explained below, DNR's decision is based on Northwest Alloys' failure to provide requested information regarding the financial condition and business of Millennium as well as other factors that bear on the suitability of Millennium as a subtenant.

On February 3, 2016, and again on June 24, 2016, DNR requested financial statements for Millennium consistent with Northwest Alloys' lease as part of its consideration of Northwest Alloys' request to sublease. DNR's initial request closely followed the bankruptcy filing of Arch Coal Company, which, at that time, owned a significant stake in Millennium, and the decision of Alcoa to idle the Wenatchee Works, which was the primary beneficiary of Northwest Alloys' business on the property leased from DNR. Given the bankruptcy of Arch Coal and indefinite closure of the Wenatchee Works, DNR appropriately determined that more information regarding Millennium's financial condition was necessary to complete its consideration of the request to sublease. Northwest Alloys did not provide any financial statements for Millennium following DNR's February 3, 2016, request.

DNR reiterated its request for Millennium's financial statements in June after the bankruptcy court approved the sale of Arch Coal's stake in Millennium to LHR Infrastructure, LLC. Arch Coal's bankruptcy filings made in conjunction with the sale provided additional information that contributed to concerns regarding Millennium's financial condition. As part of its initial filings in the bankruptcy, Arch Coal listed the value of its stake in Millennium at \$37,589,416.10. Yet the bankruptcy documents show that Arch sold its stake for only a release of its obligations to provide financial support to Millennium and an option to purchase 10 percent of the capacity of a new coal export facility at market rate, if the facility is built.

That Arch Coal was able to sell the stake in Millennium in bankruptcy that it valued so highly for little more than a release of its financial obligations to Millennium raised concerns regarding the costs of maintaining Millennium as an ongoing enterprise. Arch Coal's bankruptcy filings attest to the validity of that concern. The filings show that Millennium has significant ongoing obligations that require substantial capital contributions from its owners. According to Arch Coal, had the company been unable to pay its share of Millennium's capital needs, it would have quickly eroded the company's ownership interest in Millennium. Arch Coal's bankruptcy filings report that as of June 2016 the capital needs of Millennium were so great that Arch Coal's entire membership interest in Millennium, valued at nearly

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\$38 million, would have been lost in a matter of eight weeks if Arch could not pay the capital contributions Millennium needed.

The Arch Coal bankruptcy also affected the security for Millennium's lease obligations to Northwest Alloys. According to Arch Coal, Millennium made commitments to Northwest Alloys under its January 1, 2011, ground lease which were secured by a \$10 million letter of credit from Arch Coal. Arch's bankruptcy filings indicate that meeting the obligation to provide security required annual payments of \$250,000. Following the sale of Arch Coal's interest, the security obligation now falls on Millennium's remaining owner, LHR Infrastructure. Given the disclosure of the relationship between the ground lease and Millennium's financial obligations, DNR requested a copy of the lease in its June 24, 2016, letter. DNR's request was reasonable and permitted under its lease with Northwest Alloys. The lease entitles DNR to consider both the nature of Millennium's business and its financial condition as part of the request to sublease. The disclosure of significant obligations flowing from Millennium to Northwest Alloys under their ground lease contributes to a need for evaluation of Millennium's financial condition, particularly in light of the idling of the Wenatchee Works. Northwest Alloys has not provided a copy its lease with Millennium.

The need for evaluation of Millennium's financial condition is also supported by the historically poor market conditions in the coal industry. The sale of Arch Coal's membership interest to LHR Infrastructure leaves LHR as the sole owner of Millennium. LHR is a wholly owned subsidiary of Lighthouse Resources, which owns and operates coal mines in the Powder River Basin. The difficulties currently faced by the coal industry are well documented. A steep decline in demand for coal has led to several bankruptcies among the largest coal producers. In addition to Arch Coal, several other major U.S. coal companies, including Peabody Energy Corp., Alpha Natural Resources, and Patriot Coal Corp., have filed bankruptcy since 2015. According to the November 3, 2016, *Annual Coal Report* produced by the U.S. Energy Information Administration, U.S. coal production dropped 10.3 percent in 2015 to its lowest level since 1986. The EIA forecasts that U.S. coal production for 2016 has decreased by an additional 15 percent, to its lowest level since 1978 and will remain at historically low levels in 2017.

Given the difficult market conditions in the coal industry, Millennium's commitments to Northwest Alloys, and the fact LHR now has the sole financial responsibility for Millennium, DNR's request for Millennium's financial statements was warranted. Because Northwest Alloys has not provided the financial statements after repeated requests, DNR has determined that denial of Northwest Alloys' request for DNR's consent to sublease is appropriate.

As the steward of Washington's state-owned aquatic lands, the financial capacity of a subtenant to perform is important to DNR. A subtenant who lacks the capacity to comply with lease requirements may cause damage to the property which may not be fully remedied for years, if ever. In making its decision, DNR is cognizant of the recent history of subletting under Northwest Alloys' lease with DNR. Northwest Alloys' previous tenant, Chinook Ventures, defaulted on its lease obligations and left behind significant cleanup obligations. The recent history under the lease supports the need for careful examination of the capacity of subtenants at the site to comply with lease obligations.

DNR would also like to take this opportunity to remind Northwest Alloys that the lease requires DNR's prior written consent to place, construct, remove or demolish improvements on the leasehold. As you recognized in a March 25, 2011 letter to DNR, and on other occasions, unlike operations for unloading

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alumina authorized under the lease, DNR has not authorized Millennium's planned infrastructure "upgrades" related to coal handling. Northwest Alloys has not requested and DNR has not provided consent for construction of the improvements planned by Millennium.

DNR notes that Millennium does not have a lengthy track record. In considering whether to consent to the sublease request, the lease permits DNR to consider Millennium's business reputation and experience. Millennium was formed in 2010 as a joint venture between subsidiaries of Arch Coal and LHR for the purpose, according to Arch Coal, of developing and operating a bulk cargo port and terminal facility in Longview. As a fledgling organization in 2010, Millennium made a significant error in applying for a shoreline significant development permit for that facility. Millennium failed to disclose in the application its plans to significantly increase the amount of coal shipped from the facility after permitting was completed. Such errors can prove costly. Millennium withdrew its application only to restart the process in 2012, leading to delay in consideration of the proposal and unnecessary expense related to application review. Other costs may have followed if the error had not been revealed when it was. That Millennium does not have a lengthy track record on which to judge performance and in its short history has made a significant error with respect to its planned activities on the leased property supports the need for a thorough review of Millennium's potential suitability as a subtenant, including its financial condition.

Northwest Alloys has failed to provide information reasonably requested by DNR as permitted under the lease for review of Northwest Alloys' request for consent to sublease. As detailed above, DNR's requests for information are supported by the bankruptcy of Arch Coal; Millennium's commitments to Northwest Alloys; market conditions facing Millennium's sole remaining owner, LHR; the history of subleasing under the lease; and the absence of a significant track record supporting Millennium. Accordingly, Northwest Alloys' request for consent to sublease has been denied.

Sincerely,



Peter Goldmark
Commissioner of Public Lands