

**COBALT COAL LTD.**  
**2000, 840 – 7TH AVE SW**  
**CALGARY, AB T2P 3G2**

March 2, 2012

Norris Enterprises Co., Inc.  
4101 Alleghany Road  
Coeburn, VA 24230

**Attention: Tommy Bright**

KDS Energy, LLC ("**KDS**") and  
KMH Energy Corporation ("**KMH**")  
235 Marigold Lane  
Coeburn, VA 24230

**Attention: Kenneth Stanley ("Stanley")**

and to

Kentucky Coal Partners International, LLC  
("**KCPI-Virginia**")  
1326 South 2<sup>nd</sup> Street  
Louisville, Kentucky 40208

**Attention: Brett Scott and Chip Miller**

Dear Sirs:

**Re: Acquisition of Assets**

Subject to and in accordance with the terms and conditions hereinafter contained, this letter agreement is intended to set forth the basic terms and conditions of the proposed acquisition of the assets described in paragraph 2 hereof (the "**Transactions**"). In connection with the completion of the Transactions, Cobalt Coal Ltd., or Cobalt Coal LLC, or a wholly-owned subsidiary of Cobalt Coal Ltd., as applicable (collectively, "**Cobalt**") proposes to secure additional financing. We propose that the Transactions will proceed as follows:

1. **Background of Cobalt:** Cobalt is a public company in good standing with its common shares (the "**Cobalt Common Shares**") listed for trading on TSX Venture Exchange Inc. ("**TSX Venture**"). Cobalt currently has 61,386,895 Cobalt Common Shares outstanding.
2. **Asset Acquisition:** We understand KCPI-Virginia is in the process of negotiating an exclusive right to purchase certain assets from KDS Energy, LLC ("**KDS**"), KMH Energy Corporation, an "S" corporation for United States income tax purposes ("**KMH**") and Norris Enterprises Co, Inc. ("**Norris**") (collectively, KDS, KMH and Norris are referred to as the "**Vendors**"). We also understand that KCPI-Virginia is in the process of negotiating an exclusive option agreement (the "**KCPI EPRA**"), pursuant to which KCPI-Virginia will be granted an exclusive option to lease property (the "**KCPI Steinman Lease**") from Steinman Development Company ("**Lessor**"). The parties hereto agree that in exchange for a finder's fee and other consideration from Cobalt to

KCPI-Virginia described in paragraphs 6 and 13 hereof, KCPI-Virginia will not proceed with either the KCPI EPRA or the KCPI Steinman Lease, and in lieu thereof, Cobalt will enter into a formal purchase agreement with the Vendors (the "**Cobalt Purchase Agreement**") to be in a form mutually agreed between the parties, an option agreement with Lessor (the "**Cobalt Option Agreement**" in the form attached hereto as Schedule "A") and a share purchase agreement with Stanley regarding KMH, which is an "S" Corporation for income tax purposes (the "**KMH Share Purchase Agreement**") to be in a form mutually agreed between Cobalt and Stanley, pursuant to which Cobalt will have the option to complete the following transactions (which transactions the parties agree will close simultaneously):

- (a) Cobalt will be granted a lease from Lessor (the "**Steinman Lease**") with respect to certain deep mining rights on five non-contiguous tracts of coal minerals located in Dickenson County, Virginia. The five (5) tracts are referred to by Lessor as: (a) the 900-acre Mill Creek Tract; (b) the 900-acre Tarpon Tract (c) the 1963-acre Davis Tract; (d) the 337-acre Stanley Tract; and (e) the 803-acre Fleming Tract (the "**Steinman Lease Lands**");
- (b) KMH will, upon closing of the transaction contemplated in the Cobalt Option Agreement and the issuance of the Steinman Lease, surrender to Lessor that certain 1985 lease among Lessor and KMH pertaining to coal mining rights and surface usage rights on portions of the 900-acre Mill Creek Tract described above in exchange for an overriding royalty of two percent (2%) of gross coal sales price on all production derived from the Steinman Lease Lands (the "**Overriding Royalty**") pursuant to an overriding royalty agreement to be entered into with Norris (the "**Overriding Royalty Agreement**"). The parties agree the Overriding Royalty shall be calculated in the same manner and paid at the same time as production royalties are payable to Steinman as set forth in the Steinman Lease;
- (c) Vendors will assist Cobalt in obtaining a lease from Lessor with respect to a rail loadout site located at Addington Station in Wise County, Virginia under terms that are mutually agreeable to both Lessor and Cobalt (the "**Addington Station Lease**");
- (d) KMH is the holder of a valid mining permit covering portions of Lessor's 900-acre Mill Creek Tract issued by the Commonwealth of Virginia Department of Mines, Minerals and Energy renewed on February 25, 2011 and expiring February 25, 2016 (the "**KMH Permit**"). KMH will allow Cobalt to act as either a "contractor" or "operator" under the KMH Permit until April 30, 2012 or the "Closing Date" whichever occurs earlier to complete site preparation work, as well as to remove and sell up to 14,000 tons of coal (collectively, the "**Cobalt Permitted Operations**") with the restrictions as indicated in paragraph 3 hereof. In addition, pursuant to the KMH Share Purchase Agreement, Cobalt will acquire all of the shares of KMH, and KMH shall have no liabilities, debts, obligations or assets whatsoever, other than the KMH Permit; and
- (e) in exchange for the Steinman Lease, Cobalt shall, pursuant to the Cobalt Option Agreement, pay to Lessor a total advance minimum royalty payment in the amount of US\$500,000, payable as follows: (i) a US\$300,000 "deposit" upon execution of the Cobalt Option Agreement; and (ii) a US\$200,000 payment to Lessor on the Closing Date (as defined herein).

3. The Cobalt Permitted Operations shall be restricted as follows:
- (a) Cobalt shall be required to deliver to the Virginia Department of Mines, Minerals and Energy (the "**VDMME**") before the sooner to occur of: (i) Cobalt's commencement of any excavation work and/or coal removal activities on the permitted area; or (ii) 5:00 PM on April 30, 2012, the full replacement of the reclamation performance bond as currently posted on the KMH Permit covering the Mill Creek Tract. Cobalt further agrees to immediately assume responsibility for the reimbursement of any prorated premiums incurred by Jerry Wharton/A&G Coal (as the premium payee of said surety bond) during the period beginning on the date hereof and ending upon VDMME's approval of a full release of said bond due to the posting of a new bond by Cobalt;
  - (b) during the entirety of its tenure as either a "contractor" or "operator" of the KMH Permit, Cobalt shall assume the duty and full financial responsibility for taking all actions necessary to maintain the KMH Permit in full compliance with all applicable laws, rules and regulations, which duty shall include, but not be limited to, the assumption of all water monitoring activities and all outside consulting fees necessary to diligently prosecute the pending permit revision package;
  - (c) during the entirety of its tenure as either a "contractor" or "operator" of the KMH Permit, Cobalt shall retain the consulting services of Mr. Kenneth D. Stanley as on-site oversight inspector, with the business terms and conditions of Mr. Stanley's compensation for such consulting services to be reasonably comparable to local industry compensation levels for such services. The Vendors represent and warrant to Cobalt that, at present, no fees are owing to Mr. Stanley;
  - (d) Cobalt shall obtain all necessary surface occupancy rights from Steinman;
  - (e) Cobalt hereby agrees to indemnify, defend and hold forever harmless Vendors and their respective officers and members, from any and all damages, liabilities, claims, fines, and penalties resulting directly or indirectly, or occurring as a consequence of, the activities of, or failures to act by, Cobalt or its agents while acting as either a "contractor" or "operator" on the KMH Permit; and
  - (f) in the event that Cobalt fails to close the transactions contemplated herein on or before the Closing Date (as may be extended herein), Cobalt shall within 15 days take all necessary actions to vacate the permitted area of the KMH Permit and remove itself as "contractor" or "operator", as applicable, from the KMH Permit. Prior to vacating the permitted area, Cobalt shall be responsible for placing the permitted area in a condition that is in full compliance with the conditions of the KMH Permit.
4. As consideration for the above described actions, assets or transactions identified in subparagraphs 2(a) to (d) inclusive (collectively, the "**Assets**"), Cobalt shall be required to pay Vendors a total purchase price of US\$14,500,000 (US\$15,000,000 less the US\$500,000 deposit paid to KDS pursuant to paragraph 7 hereof). Cobalt, at its sole discretion, may choose to pay the balance of US\$14,500,000 on the Closing Date or to pay the US\$14,500,000 in instalments under either of the following payment schedules:
- (a) US\$4,500,000 in cash due on the Closing Date, with the remaining US\$10,000,000 plus interest at 5% per annum to be payable to KDS pursuant to a promissory note of Cobalt to be issued on the Closing Date requiring monthly instalments commencing nine months

from the Closing Date from net revenues generated from coal sales to Cobalt from the Steinman Lease Lands to be the greater of:

- (i) 70% of Cobalt's total net revenue per month; or
- (ii) \$20 per ton if Cobalt's coal sales price is \$125 per ton or greater; or
- (iii) \$15 per ton if Cobalt's coal sales price is between \$115 and \$124 per ton; or
- (iv) \$10 per ton if Cobalt's coal sales price is between \$105 and \$114 per ton; or
- (v) \$5 per ton if Cobalt's coal sales price is between \$100 and \$104 per ton; or
- (vi) \$2 per ton if Cobalt's coal sales price is \$99 or less per ton.

Payments pursuant to this provision shall become due and payable to KDS upon receipt of proceeds by Cobalt from the sale of coal produced from the Steinman Lease Lands and, commencing twelve months after the Closing Date, KDS shall be entitled to a guaranteed minimum payment (regardless of actual production or lack thereof) of US\$150,000 per month. In the event that the cumulative monthly payments from Cobalt for any rolling 12-month period reaches a balance of US\$2,000,000, the guaranteed monthly minimum payment from coal production from the Steinman Lease Lands under this provision shall be suspended for the remainder of that rolling 12-month period; or

- (b) US\$3,500,000 in cash due on the Closing Date, with the remaining \$11,000,000 plus interest at 5% per annum to be payable to KDS under a promissory note of Cobalt to be issued on the Closing Date (the "**Promissory Note**"). Cobalt agrees to retain a qualified third-party engineering firm: (i) to conduct a comprehensive reserve study; and (ii) at the conclusion of this study, to issue a final report to Cobalt, Steinman, and KDS (the "**43-101 Report**"). The 43-101 Report shall, among other things, identify and summarize the total recoverable tonnage of mineable and merchantable coal on the Steinman Lease Lands. The 43-101 Report shall be released to Cobalt, Steinman and KDS within two years of the Closing Date and, in the event that the 43-101 Report identifies reserves in excess of 50,000,000 mineable and marketable tons, interest payable on the Promissory Note shall be increased to 15% per annum on the outstanding principal at that time. Otherwise, the Promissory Note shall bear interest at a rate of 5% per annum on the outstanding principal and shall be payable as to:
  - (i) US\$4,000,000 on April 30, 2013, plus accrued interest; and
  - (ii) US\$7,000,000 on April 30, 2014, plus accrued interest.

On the Closing Date, Cobalt shall inform KDS which of the two above installment schedules that it intends to select, and Cobalt shall be bound to those terms unless the parties mutually agree in writing to modify these terms. In the event that Cobalt shall default for more than sixty (60) days on any payment to KDS under either of the instalment payment schedules outlined above, KDS, or its designee, shall be entitled to an assignment of the Steinman Lease and the KMH Permit, subject to the consent of Steinman to such assignment (the "**KDS Security**"). KDS acknowledges and agrees the KDS Security shall be subordinated on a one-time basis to a senior lender to Cobalt

associated with the completion of the Transactions to a maximum amount of US\$4,500,000.

5. **Transaction Structure and Allocation of Purchase Price:** The parties agree the Cobalt Purchase Agreement shall be structured in a manner that the share purchase contemplated therein shall be treated as a deemed asset sale for tax purposes and the parties agree to file a joint election confirming this under Section 338(h)-10 of the United States Internal Revenue Code.
6. **Finder's Fee:** The parties agree, upon closing of the Transactions and subject to TSX Venture approval, KCPI-Virginia shall be paid a cash finder's fee by Cobalt in an amount equal to 3.95% of the purchase price paid by Cobalt for the Assets. The Vendors warrant that Cobalt shall not be responsible for any finder's fees or commissions as a result of commitments made by Vendors. Likewise, Cobalt warrants that Vendors shall not be responsible for any finder's fees or commissions as a result of commitments made by Cobalt. All parties to these Transactions agree that Lessor shall not be responsible for the payment of any finder's fees or similar fees to any party with respect to the Transactions.
7. **Deposit:** Upon execution of this letter agreement and execution of the Cobalt Purchase Agreement, Cobalt shall pay to KDS a deposit in the amount of US\$500,000 as a deposit in respect of the Transactions (the "**KDS Deposit**"). Upon signing of this letter agreement and execution of the Cobalt Option Agreement, Cobalt shall pay to the Lessor a deposit in the amount of US\$300,000 as an advance against minimum royalties in respect of the Steinman Lease (the "**Royalty Deposit**").

The KDS Deposit shall be non-refundable other than:

- (a) in the event KDS, KMH or Norris fail to close the Transactions contemplated herein for any reason other than the failure of Cobalt to perform its obligations hereunder or under the KMH Share Purchase Agreement or the Cobalt Purchase Agreement;
  - (b) in the event the KMH VDMME Permit is not valid or in good standing and owned by KMH, or in the event the representations and warranties of KMH in the KMH Share Purchase Agreement or the Vendors in the Cobalt Purchase Agreement are not true and correct; or
  - (c) in the event the Vendors fail to comply with their covenants contained in the Cobalt Purchase Agreement or KMH fails to comply with its covenants in the KMH Share Purchase Agreement.
8. **Interim Operations:** The parties agree that until closing of the Transactions, other than the Cobalt Permitted Operations, no mining operations will be permitted on the Assets. However, representatives of Cobalt shall be allowed access to the Assets as required to secure mining licences and/or permits to accelerate the commencement of mining operations, as well as to complete the Cobalt Permitted Operations. In addition, until closing of the Transactions, access to the Assets shall be granted to representatives of Cobalt accompanied by representatives of an independent firm in order to complete an independent evaluation of the permits and the 43-101 Report in support of closing the Transactions and obtaining TSX Venture approval.
  9. **Further Funding Efforts by Cobalt:** Cobalt intends to use its best efforts to secure additional funding by way of equity, debt or other industry participant financing for minimum gross proceeds of a minimum of US\$20 million (the "**Cobalt Financing**"). Cobalt will engage an

investment dealer or a syndicate of investment dealers to act as agent (the "**Agents**") on a "commercially reasonable efforts" basis for the Cobalt Financing. In connection therewith, Cobalt intends to pay a cash commission that is industry standard for financings of this nature.

10. **Cobalt Representations and Warranties:** Cobalt represents and warrants to KCPI-Virginia, the Vendors and the Lessor as follows:
- (a) Cobalt is duly incorporated and is validly subsisting under the laws of Alberta;
  - (b) Cobalt is in material compliance with all of its obligations as a reporting issuer in the jurisdictions where it is a reporting issuer, including those imposed pursuant to securities legislation, and the regulations and policies thereunder;
  - (c) Cobalt is in material compliance with all of the policies of TSX Venture;
  - (d) Cobalt's authorized capital consists of an unlimited number of common shares and an unlimited number of preferred shares, issuable in series;
  - (e) Cobalt currently has 61,386,895 Cobalt Common Shares issued and outstanding and all of such shares are validly issued and outstanding as fully paid and non-assessable shares of Cobalt;
  - (f) the financial statements of Cobalt for the period ended September 30, 2011 were true and correct as at the date thereof and were prepared in accordance with Canadian generally accepted accounting principles consistently applied;
  - (g) Cobalt has filed all forms, reports, documents and information required to be filed by it, whether pursuant to applicable securities legislation or otherwise, with the applicable securities commissions (the "**Disclosure Documents**"). As of the time the Disclosure Documents were filed with the applicable securities regulators and on SEDAR (System for Electronic Document Analysis and Retrieval)(or, if amended or superseded by a filing prior to the date of this letter agreement, then on the date of such filing): (i) each of the Disclosure Documents complied in all material respects with the requirements of the applicable securities laws; and (ii) none of the Disclosure Documents contained any untrue statement of a material fact or omitted to state a material fact required to be stated therein or necessary in order to make the statements therein, in the light of the circumstances under which they were made, not misleading;
  - (h) there is no "material fact" or "material change" (as those terms are defined in applicable securities legislation) in the affairs of Cobalt that has not been generally disclosed to the public; and
  - (i) there is no action, suit, litigation, arbitration, investigation, inquiry or other proceeding in progress, or, to the best of Cobalt's knowledge, pending or threatened against or relating to Cobalt or its material assets and there is no circumstance, matter or thing known to Cobalt which might give rise to any such proceeding or to any governmental investigation relative to Cobalt and there is not outstanding against Cobalt any judgment, decree, injunction, rule or order of any court, government department, commission, agency or arbitrator.

11. **Regulatory Requirements:** The Vendors acknowledge that Cobalt is a public company that is subject to the policies of the TSX Venture Corporate Finance Manual (the "**Policies**"). Upon execution of this letter agreement, the Policies require Cobalt to submit for review to TSX Venture a filing statement which must contain full, true and plain disclosure of all material facts relating to Cobalt, the Cobalt Purchase Agreement, the Cobalt Option Agreement, the KMH Share Purchase Agreement, the Addington Station Lease, the Assets and the Transactions (the "**Filing Statement**"). Cobalt will be required to include in its Filing Statement prospectus-level disclosure on KMH, the Steinman Lease Lands and the Assets. In addition, the Policies also require Cobalt to submit an independent geology and reserve report (the 43-101 Report referred to previously) with respect to the Assets prepared in compliance with Canadian National Instrument 43-101 *Standards for Disclosure for Mineral Projects*.
12. **Formal Agreement:** Subject to the results of the investigations to be conducted pursuant to paragraph 16, Cobalt and the Vendors covenant and agree to execute the Cobalt Purchase Agreement and the KMH Share Purchase Agreement by March 31, 2012 (the "**Execution Date**"), or such later date as the parties may mutually agree.
13. **Consulting and Employment Agreements:** Upon execution of this letter agreement, Cobalt will enter into consulting agreements with each of Brett Scott and Chip Miller retaining their services for \$12,000 per month each for a term of three months, such consulting agreements to be in a form mutually satisfactory to the parties. Upon completion of the Transactions, Cobalt agrees to enter into employment agreements (the "**Employment Agreements**") with each of Chip Miller and Brett Scott providing for annual compensation of \$140,000 per annum. Pursuant to the Employment Agreements, Cobalt agrees each of Messrs. Miller and Scott will be granted stock options on terms that are mutually agreeable by Messrs. Miller and Scott and the Board of Directors of Cobalt, subject to TSX Venture approval.
14. **Closing:** The parties contemplate the closing of the Transactions shall take place after the receipt of the regulatory and stock exchange approval of Cobalt for the Transactions, and in any event, not later than April 30, 2012 (the "**Closing Date**"). The parties agree that Cobalt shall not have the right to a financial penalty to elect to close the Transactions in advance of the proposed Closing Date. The parties also agree that all definitive closing documentation will be negotiated in good faith and in final form prior to April 30, 2012 (the "**Closing Document Condition**").

Provided Cobalt has engaged in diligent and good faith efforts to complete the Cobalt Financing and has complied with the Closing Document Condition, the parties agree Cobalt shall be entitled to a thirty (30) day extension to the Closing Date to complete the Cobalt Financing the ("**Extended Closing Date**") under either of the following limited circumstances:

- (a) Cobalt has entered into an agreement with a registered investment dealer, engaged in the business of acquiring investment capital, that such agent has issued a "term sheet" in favor of Cobalt for a financing in an amount equal to or greater than US\$5,000,000, and that the closing of such financing will occur within the extension period requested by Cobalt; or
- (b) Cobalt has entered into an agreement with a recognized institutional lender, and that such institutional lender has issued a "term sheet" in favor of Cobalt for a loan to Cobalt in an amount equal to or greater than US\$5,000,000 and that the closing of such loan will take place within the extension period requested by Cobalt.

In the event the Closing Date has been extended under the terms herein and the Closing Document Condition has been complied with, Cobalt can also extend the Extended Closing Date an additional thirty (30) days provided: (a) Cobalt can demonstrate progress has been made on the Cobalt Financing and that closing of the financing or the loan, as applicable, will occur within the extended thirty (30) day period; and (b) Cobalt shall have paid KDS an additional US\$150,000 deposit in respect of the Transactions, which additional deposit shall be treated the same as the KDS Deposit and shall be a reduction in the balance of the purchase price payable for the Assets pursuant to paragraph 4 hereof.

15. **Costs:** Each party agrees to pay its own costs in respect of the Transactions, including legal and accounting costs.
16. **Due Diligence:** For the purposes of allowing Cobalt to complete a due diligence review of the Assets to determine if there are any facts relating to the Assets which, if known to it, would cause it to elect to not close the Transactions on or before April 30, 2012, the Vendors shall permit Cobalt and their counsel and agents to conduct, upon execution hereof, up to and including the Closing Date, such investigations as Cobalt may deem reasonably necessary or advisable in order to ensure that each of the representations, warranties, covenants and agreements by the Vendors contained in the Cobalt Purchase Agreement and the KMH Share Purchase Agreement will be true and accurate.
17. **Conditions:** The obligations of the parties to consummate the Transactions shall be subject to the fulfilment of the following conditions in favor of Cobalt:
  - (a) the receipt of all necessary regulatory and TSX Venture approvals;
  - (b) the review to the sole satisfaction of Cobalt of the Assets;
  - (c) the approval of the Transactions by the Board of Directors of Cobalt;
  - (d) the entering into of the Cobalt Option Agreement in the form attached hereto as Schedule "A";
  - (e) the entering into of the Cobalt Purchase Agreement, the Steinman Lease, the Addington Station Lease and the KMH Share Purchase Agreement in such form as is mutually agreeable to the parties thereto;
  - (f) the completion of the minimum Cobalt Financing; and
  - (g) the closing of all of the Transactions contemplated herein are completed concurrently.
18. **Non-Solicitation:** The Vendors agree that during the period from the date hereof until the Closing Date, they:
  - (a) shall immediately cease and cause to be terminated any existing discussions or negotiations or other proceedings initiated prior to the date hereof by it, or its officers, directors, employees, financial advisors, representatives and agents ("**Representatives**") or others with respect to all Proposals (as defined below);
  - (b) shall not solicit or cause or facilitate anyone else to solicit any Proposal;

- (c) shall not provide information concerning its securities, assets or business to anyone for or in furtherance of anything mentioned in subparagraphs 18(a) or (b); and
- (d) shall not, and shall not authorize or permit any of its Representatives to, directly or indirectly, solicit, initiate or encourage (including by way of furnishing information) any inquiries or the making of any proposal that constitutes or may reasonably be expected to lead to a Proposal from any person, or engage in any discussions, negotiations or inquiries relating thereto.

For the purposes of this letter agreement, "Proposal" means a proposal or offer by a third person (i.e., other than by Cobalt as contemplated herein), whether or not subject to a due diligence condition and whether or not in writing, to acquire in any manner, directly or indirectly, beneficial ownership of all or any portion of any interest in the Assets whether by way of arrangement, merger, asset purchase, joint venture or other business combination, including without limitation any single or multi-step transaction or series of related transactions that is structured to permit such third person to acquire beneficial ownership of all or any portion of the Assets.

19. **Confidential Information:** All information provided by each of Cobalt and the Vendors, in any form whether written, electronic or verbal, as to financial condition, business, properties, title, assets and affairs (including any material contracts) as may reasonably be requested by any other party hereto, including information contemplated by paragraph 16, will be kept confidential by each party (the "**confidential information**"), other than information that:
- (a) has become generally available to the public;
  - (b) was available to a receiving party or its representatives on a non-confidential basis before the date hereof; or
  - (c) has become available to a receiving party or its representatives on a non-confidential basis from a person who is not, to the knowledge of the receiving party or its representatives, otherwise bound by confidentiality obligations to the provider of such information or otherwise prohibited from transmitting the information to the receiving party or its representatives.

No confidential information may be released by a receiving party to any third party without the consent of the provider thereof, except if such information is required to be released by law, court order or stock exchange rule; and confidential information may be used by a receiving party solely for the purpose of consummating the Transactions contemplated by this letter agreement.

20. **Press Releases:** Neither of the parties will hereafter make any public statement or press release in respect of the Transactions (including in respect of the execution of this letter agreement) without the prior written consent of the other parties; provided that no party shall be prevented from making any public statement or press release which is required to be made by law or any rule of a stock exchange or similar organization to which it is bound. For greater certainty, upon the execution of this letter agreement, Cobalt will issue a press release as required by TSX Venture and such press release shall be in a form satisfactory to the Lessor and the Vendors prior to its issuance.
21. **Closing Covenant:** Until the Closing Date, each of Cobalt and the Vendors covenants and agrees with the other party hereto to use all commercially reasonable efforts to take all actions with the

intent that the closing conditions herein that are within its control to satisfy shall be satisfied, and all covenants and agreements herein made by it shall have been performed. Regardless of the aforesaid, the Vendors shall be under no obligation to cause or induce Lessor to undertake any actions to close with Cobalt. Cobalt hereby undertakes the full responsibility of inducing Lessor to enter into the Cobalt Option Agreement and the Steinman Lease.

22. **Termination:** This letter agreement may be terminated in writing at any time by notice from one of the parties to the other parties hereto in accordance with the terms contained herein:
- (a) by April 30, 2012, if the party issuing such notice, after completing its due diligence review in good faith, is not prepared to complete the Transactions as a result of its due diligence review; or
  - (b) by the Closing Date (which may be extended as indicated herein), or such later date as the parties may agree in writing, if the Transactions have not closed by that date.

In the event of termination by any of the parties as provided for in this paragraph, this letter agreement shall become void and of no effect, without any liability or obligation on the part of the parties hereto, other than paragraphs 15, 19 (as to the confidentiality of previously disclosed information) and 23 hereof and the KDS Deposit made to Vendors shall be forfeited by Cobalt unless otherwise provided for herein.

23. **Governing Law:** This letter agreement shall be governed by the laws of the Commonwealth of Virginia and the federal laws of the USA applicable therein.
24. **Enforceability:** This letter agreement constitutes an enforceable legal agreement, the consideration for which shall be the mutual covenants of the parties contained herein.
25. **Assignment:** This letter agreement shall be assignable by Cobalt to a subsidiary, partnership, limited liability company, trust or other entity that is related to or affiliated with Cobalt or is owned or controlled by a current officer or director of Cobalt, without the consent of the other parties hereto. This letter agreement shall not be assignable by Cobalt to any entity not affiliated or related to Cobalt or owned or controlled by a current officer or director of Cobalt without the consent of the other parties hereto, such consent shall not be unreasonably withheld.
26. **Resolution of Conflicting Terms:** In the event that any of the terms contained in this letter agreement conflict with terms contained in the Cobalt Purchase Agreement, such discrepancies shall be resolved in favor of the Cobalt Purchase Agreement.

If the foregoing correctly sets forth your understanding, please indicate your acceptance thereof by signing and returning the enclosed duplicate of this letter on or before 5:00 p.m. (Calgary time) on March 2, 2012.

This letter may be signed in counterparts which together shall be deemed to constitute one (1) letter agreement, and delivery of the counterparts may be effected by means of telecopier from us to you and from you to us.

Yours truly,

**COBALT COAL LTD.**

Per: "Mike Crowder"  
Mike Crowder, CEO

ACKNOWLEDGED AND AGREED TO this 2<sup>nd</sup> day of March, 2012.

**KENTUCKY COAL PARTNERS  
INTERNATIONAL, LLC**

Per: "Brett Scott"  
Brett Scott

Per: "Chip Miller"  
Chip Miller

**NORRIS ENTERPRISES CO., INC.**

Per: "Tommy Bright"  
Tommy Bright

**KDS ENERGY, LLC**

Per: "Kenneth Stanley"  
Kenneth Stanley

**KMH ENERGY CORPORATION**

Per: "Kenneth Stanley"  
Kenneth Stanley

**SCHEDULE "A"**  
**COBALT OPTION AGREEMENT**

## OPTION AGREEMENT

This is an option agreement ("Option") made and entered into this 2<sup>nd</sup> day of March, 2012 by and between STEINMAN DEVELOPMENT COMPANY, a Pennsylvania limited partnership ("Steinman") and Cobalt Coal, LLC, a Virginia limited liability company with an office at P.O. Box 191, 101 Bulldog Lane, Premier, WV 24878 ("Cobalt-VA").

The background of this Option is as follows:

- (a) Steinman controls certain surface and mineral properties located in Dickenson County, Virginia further described as: (i) the 900-acre Mill Creek Tract; (ii) the 900-acre Tarpon Tract; (iii) the 1963-acre Davis Tract; (iv) the 337-acre Stanley Tract; and (v) the 803-acre Fleming Tract (collectively, the "Properties");
- (b) Cobalt-VA wishes to lease the Properties from Steinman;
- (c) Steinman is willing grant Cobalt-VA the Option to lease the Properties on the terms and conditions set forth herein; and
- (d) Cobalt intends to use its best efforts to secure funding by way of equity, debt or other industry participant financing for minimum gross proceeds of a minimum of US\$20 million (the "Cobalt Financing") in order to develop and mine the Properties.

In consideration of the premises and the mutual promises contained herein, the parties have agreed as follows:

1. In consideration of the sum of Three Hundred Thousand and 00/100 Dollars (US\$300,000.00), cash in hand paid, the receipt of which is hereby acknowledged (the "Deposit"), Steinman grants Cobalt-VA the sole and exclusive option to lease the Properties on substantially the same terms and conditions set forth in the lease attached hereto as Exhibit A and made a part hereof (the "Lease").
2. The exercise of the Option shall be made by Cobalt-VA delivering written notice of the exercise of the Option to Steinman not later than 5:00 p.m. EST on the 30th day of April, 2012 (the "Expiry Date") to Steinman's attention, c/o William E. Bradshaw, 302 Shawnee Avenue, East, Big Stone Gap, VA 24219 by either certified mail/return receipt requested or by an overnight mail service. If Cobalt-VA does not exercise this Option by the Expiry Date (which may be extended as indicated below), this Option shall be considered null, void and of no effect, and Steinman shall retain the Deposit.
3. Provided Cobalt has engaged in diligent and good faith efforts to complete the Cobalt Financing, the parties agree Cobalt shall be entitled to an additional thirty (30) days to complete the Cobalt Financing and to exercise the Option (the "Extended Expiry Date") under either of the following limited circumstances:
  - (a) Cobalt has entered into an agreement with a registered investment dealer engaged in the business of acquiring investment capital, that such agent has issued a "term sheet" in favor of Cobalt for a financing in an amount equal to or greater than US\$5,000,000, and that the closing of such financing will occur within the extension period requested by Cobalt; or
  - (b) Cobalt has entered into an agreement with a recognized institutional lender, and that such institutional lender has issued a "term sheet" in favor of Cobalt for a loan to Cobalt in an

amount equal to or greater than US\$5,000,000 and that the closing of such loan will take place within the extension period requested by Cobalt.

In the event the Expiry Date has been extended under the terms herein, Cobalt can also extend the Extended Expiry Date an additional thirty (30) days in the event that Cobalt can demonstrate progress has been made on the Cobalt Financing and that closing of the financing or the loan, as applicable, will occur within the extended thirty (30) day period. If Cobalt wants to extend beyond May 30<sup>th</sup>, it must pay Steinman a fee of \$50,000.00 USD, non-refundable and non-recoupable, in order to exercise the extension. However, if the Option is exercised then Cobalt shall receive a credit for the said \$50,000.00 that shall be treated as advance minimum royalty.

4. Steinman represents and warrants to and in favour of Cobalt and acknowledges that Cobalt is relying upon such representations and warranties in making the Deposit:

- (a) Steinman is a partnership duly formed under the laws of Pennsylvania and has all necessary power and authority to enter into this agreement, grant the Option and enter into the Lease if the Option is exercised;
- (b) there is no suit, action, litigation, arbitration proceeding or governmental proceeding in progress, or, to the knowledge of Steinman, pending or threatened against or relating to, or affecting the Properties, which if determined adversely to Steinman might materially and adversely affect the Properties, or the right of Steinman to use, develop, produce from or sell the Properties, in whole or in part, and there is not presently outstanding against Steinman any material judgment, decree, injunction, rule or order of any court, governmental department, commission, agency or arbitrator relating to the Properties;
- (c) other than the Option granted herein, no person, company, partnership, trust or other entity has any written or oral agreement, option, understanding or commitment, or any right or privilege capable of becoming an agreement for the purchase, exchange, transfer or other disposition from Steinman of any part of the Properties;
- (d) Steinman has not incurred any obligation or liability, contingent or otherwise, for broker's or finder's fees in respect of the transaction contemplated herein;
- (e) the execution and delivery of this agreement and the completion of the transaction contemplated herein have been, or in respect of the transaction contemplated herein will have been prior to Closing, duly approved by the board of directors of the general partner of Steinman and this agreement constitutes a valid and binding obligation of Steinman enforceable against it in accordance with its terms, subject, however, to limitations imposed by law in connection with bankruptcy or similar proceedings and to the extent that equitable remedies such as specific performance or injunction are granted at the discretion of a court of competent jurisdiction;
- (f) Steinman owns a mixture of mineral rights, surface rights and fee simple interests in the Properties as may be ascertained from Steinman's records and the land records in the Dickenson County Circuit Court Clerk's Office free and clear of all liens, charges and claims of others other than as indicated in the Lease and no taxes or rentals are due in respect of the Properties other than as disclosed in the Lease;
- (g) other than leases to: (i) KMH Energy Corp. in respect of deep mining rights on the Mill Creek and Tarpon tracts; (ii) Hill Fuel, Inc. in respect of surface mining rights on the Mill

Creek and Tarpon tracts; and (iii) Southwest Coal Company, Inc. in respect of coal seams overlying the Lower Beanner Seam on the Davis tract, there is no adverse claim or challenge against or to the ownership of or title to the Properties, nor to the knowledge of Steinman after due inquiry, is any of the foregoing pending or threatened, and no person, company, partnership, trust or other entity has any royalty or other interest whatsoever in production from any of the Properties, except as otherwise set forth in the Lease, other than as might be apparent from a physical inspection of the Properties with respect to surface rights;

- (h) in respect of the Properties, Steinman has been prosecuted for an offence alleging, material non compliance with any environmental laws.
5. The Deposit shall be non-refundable, other than in the event:
- (a) the representations and warranties of Steinman contained herein are not true and correct; or
  - (b) Steinman fails to close the transaction contemplated herein for any reason, other than the failure of Cobalt to perform its obligations herein.
6. In the event Cobalt-VA exercises this Option, the following provisions shall apply:
- (a) At the time of exercise, Cobalt-VA shall deliver to Steinman the additional sum of Two Hundred Thousand and 00/100 Dollars (US\$200,000.00) (the "Option Exercise Payment"). Which sum, together with the Deposit paid upon execution of this Option, shall constitute the advance production royalties specified in paragraph 2B of the Lease.
  - (b) As a condition precedent to exercise of the Option, Cobalt-VA shall have been duly authorized to conduct business in the Commonwealth of Virginia.
  - (c) As a further condition precedent to exercise of the Option, Cobalt-VA shall demonstrate to Steinman's reasonable satisfaction that it has all necessary and appropriate permits, governmental and agency licenses and permissions to promptly commence mining activities on the Properties.
7. This Option shall be binding upon and inure to the benefit of the respective successors in interest of the parties. Cobalt-VA shall not set over or assign this Option, except with the prior written consent of Steinman, which consent shall not be unreasonably withheld.
8. This Option represents the entire understanding between the parties and there are no collateral or oral agreements or understandings. This Option shall not be modified or amended except in writing signed by the parties.
9. This Option shall be construed in accordance with and governed by the laws of the Commonwealth of Virginia.

IN WITNESS WHEREOF, this Option has been executed on behalf of the parties by their respective duly-authorized representatives effective on the date first set forth above.

**STEINMAN DEVELOPMENT COMPANY**

Per: "signed"  
Vice President (Steinman Coal Corporation)  
(General Partner of Steinman Development Company)

STATE OF *Virginia*,

COUNTY OF *Wise*, TO-WIT:

I, *Sandra Gail Coeburn*, a Notary Public within and for the County and State aforesaid, do hereby certify that *James L. Sykes*, of Steinman Coal Corporation (General Partner of Steinman Development Company), whose name is signed to the foregoing Option bearing date of the 2<sup>nd</sup> day of March, 2012 has this day acknowledged before me as the act and deed of Steinman Development Company, a limited partnership, in my State and County.

"signed"  
Notary Public

My Commission Expires:*4-30-13*

**COBALT COAL, LLC**

Per: "signed"  
Managing Member

STATE OF *Kentucky*,

COUNTY OF *Jefferson*, TO-WIT:

I, *Steve Kirsch*, a Notary Public within and for the County and State aforesaid, do hereby certify that *Brett P. Scott*, of Cobalt Coal, LLC whose name is signed to the foregoing Option, bearing date of the 2<sup>nd</sup> day of March, 2012 has this day acknowledged before me as the act and deed of Cobalt Coal, LLC, a Virginia limited liability company, in my State and County.

"signed"  
Notary Public

My Commission Expires:*10-7-2012*