

MFA INCORPORATED AND SUBSIDIARIES

Consolidated Financial Statements

August 31, 2011 and 2010

(With Independent Auditors' Report Thereon)

Independent Auditors' Report

The Board of Directors
MFA Incorporated:

We have audited the accompanying consolidated balance sheets of MFA Incorporated and subsidiaries (the Company) as of August 31, 2011 and 2010, and the related consolidated statements of operations, members' equity earned, and cash flows for the years then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of the Company as of August 31, 2011 and 2010 and the results of their operations and their cash flows for the years then ended, in conformity with U.S. generally accepted accounting principles.

Williams - Keepers LLC

November 1, 2011

MFA INCORPORATED AND SUBSIDIARIES

Consolidated Balance Sheets

August 31, 2011 and 2010

| Assets | 2011 | 2010 |
|---|----------------|----------------|
| Current assets: | | |
| Cash and cash equivalents | \$ - | \$ 1,651,936 |
| Accounts and notes receivable, net of allowance for doubtful accounts of \$1,757,000 and \$1,631,000, respectively | 93,926,796 | 84,477,501 |
| Inventories | 187,830,813 | 142,886,452 |
| Refundable income taxes | - | 1,459,017 |
| Deferred income taxes (note 8) | 3,208,781 | 3,308,830 |
| Prepaid expenses and other current assets | 5,060,129 | 4,855,802 |
| Total current assets | 290,026,519 | 238,639,538 |
| Investments (note 2) | 30,649,158 | 26,278,589 |
| Notes receivable, net of allowance for doubtful accounts of \$0 and \$0, respectively | 3,828,846 | 3,940,602 |
| Other assets (note 3) | 5,619,687 | 6,947,261 |
| Goodwill | 1,446,800 | 1,446,800 |
| Plant and equipment, net (note 5) | 76,759,442 | 80,897,814 |
| Total assets | \$ 408,330,452 | \$ 358,150,604 |
| Liabilities and Members' Equity Earned | | |
| Current liabilities: | | |
| Notes payable to banks (note 6) | \$ 87,753,245 | \$ 72,700,000 |
| Accounts payable | 103,135,672 | 92,980,688 |
| Accrued expenses | 14,593,769 | 13,765,339 |
| Current maturities of long-term obligations (note 6) | 12,372,611 | 17,137,548 |
| Total current liabilities | 217,855,297 | 196,583,575 |
| Long-term obligations (note 6) | 70,336,904 | 59,436,124 |
| Other obligations (note 7) | 7,629,423 | 6,946,666 |
| Commitments and contingent liabilities (note 10) | - | - |
| Noncontrolling interest | 858,346 | 880,956 |
| Members' equity | 61,692,688 | 62,483,910 |
| Retained earnings | 49,957,794 | 31,819,373 |
| Total liabilities and members' equity earned | \$ 408,330,452 | \$ 358,150,604 |

See accompanying notes to consolidated financial statements.

MFA INCORPORATED AND SUBSIDIARIES

Consolidated Statements of Operations

Years Ended August 31, 2011 and 2010

| | <u>2011</u> | <u>2010</u> |
|---|----------------------|----------------------|
| Revenues: | | |
| Farm supply sales | \$ 736,421,808 | \$ 569,530,412 |
| Grain marketing sales | 572,990,159 | 430,838,019 |
| Other operating revenues | 45,572,498 | 37,213,015 |
| Total revenues | <u>1,354,984,465</u> | <u>1,037,581,446</u> |
| Cost of sales | <u>1,174,202,617</u> | <u>892,133,269</u> |
| Operating margin | 180,781,848 | 145,448,177 |
| Operating expenses | <u>155,844,159</u> | <u>136,538,538</u> |
| Income from operations | <u>24,937,689</u> | <u>8,909,639</u> |
| Other income (expense): | | |
| Interest expense | (12,340,951) | (12,253,360) |
| Other income, net | 10,975,303 | 13,815,982 |
| Total other income (expense), net | <u>(1,365,648)</u> | <u>1,562,622</u> |
| Income before income taxes | <u>23,572,041</u> | <u>10,472,261</u> |
| Income taxes: | | |
| Current provision | 4,500,000 | 749,000 |
| Deferred provision (benefit) | 900,000 | (47,000) |
| Total income taxes | <u>5,400,000</u> | <u>702,000</u> |
| Net income before noncontrolling interest | 18,172,041 | 9,770,261 |
| Noncontrolling interest in net income of subsidiary | 33,619 | 74,239 |
| Net income | <u>\$ 18,138,422</u> | <u>\$ 9,696,022</u> |

See accompanying notes to consolidated financial statements.

MFA INCORPORATED AND SUBSIDIARIES

Consolidated Statements of Members' Equity Earned

Years Ended August 31, 2011 and 2010

| | <u>Noncontrolling interest</u> | <u>Members' equity</u> | <u>Retained earnings</u> | <u>Total</u> |
|--|------------------------------------|----------------------------|------------------------------|----------------------|
| Balance, August 31, 2009 | \$ 1,065,260 | \$ 62,487,390 | \$ 22,119,917 | \$ 85,672,567 |
| Net income, excluding noncontrolling interest | | | 9,696,022 | 9,696,022 |
| Noncontrolling interest in net income of subsidiary | 74,239 | | | 74,239 |
| Retirement and reallocation of equities | | (3,480) | 3,434 | (46) |
| Net change in noncontrolling interest in subsidiary equities | <u>(258,543)</u> | | | <u>(258,543)</u> |
| Balance, August 31, 2010 | 880,956 | 62,483,910 | 31,819,373 | 95,184,239 |
| Net income, excluding noncontrolling interest | | | 18,138,422 | 18,138,422 |
| Noncontrolling interest in net income of subsidiary | 33,619 | | | 33,619 |
| Retirement and reallocation of equities | | (791,226) | | (791,226) |
| Net change in noncontrolling interest in subsidiary equities | <u>(56,230)</u> | | | <u>(56,230)</u> |
| Balance, August 31, 2011 | <u>\$ 858,345</u> | <u>\$ 61,692,684</u> | <u>\$ 49,957,795</u> | <u>\$112,508,824</u> |

See accompanying notes to consolidated financial statements.

MFA INCORPORATED AND SUBSIDIARIES

Consolidated Statements of Cash Flows

Years Ended August 31, 2011 and 2010

| | <u>2011</u> | <u>2010</u> |
|--|---------------------|---------------------|
| Cash flows from operating activities: | | |
| Net income | \$ 18,138,422 | \$ 9,696,022 |
| Adjustments to reconcile net income to net cash flows provided by (used in) operating activities: | | |
| Deferred income taxes | 900,000 | (47,000) |
| Depreciation and amortization | 15,229,377 | 15,571,388 |
| Noncash portion of allocated patronage dividends | (658,624) | (723,098) |
| Noncash earnings of joint ventures | (5,543,013) | (3,325,595) |
| Provision for bad debts | 806,849 | 234,481 |
| Gain on sale of plant and equipment | (373,647) | (5,298,774) |
| Cumulative bond interest | 1,014,472 | 939,826 |
| Noncontrolling interest in net income of subsidiary | 33,619 | 74,239 |
| Changes, exclusive of effect of business combinations, in: | | |
| Receivables | (10,256,144) | 17,527,170 |
| Inventories | (44,944,361) | (23,006,507) |
| Refundable income taxes | 1,459,017 | 12,247,983 |
| Prepaid expenses and other current assets | (204,328) | (289,624) |
| Accounts payable | 10,154,986 | 1,653,771 |
| Accrued expenses | 828,430 | 4,875,205 |
| Nonqualified retirement plan payments | (762,950) | (379,870) |
| Net cash (used in) provided by operating activities | <u>(14,177,895)</u> | <u>29,749,617</u> |
| Cash flows from investing activities: | | |
| Purchases of plant and equipment | (10,165,598) | (7,621,419) |
| Investments redeemed by other cooperatives | 1,827,002 | 2,271,036 |
| Proceeds from sale of plant and equipment | 893,387 | 7,753,370 |
| Cash investment in equity investee | - | (5,500,000) |
| Note receivable from equity investee | - | (2,500,000) |
| Other | 644,007 | 1,035,920 |
| Net cash (used in) investing activities | <u>(6,801,202)</u> | <u>(4,561,093)</u> |
| Cash flows from financing activities: | | |
| Net borrowings (repayments) under notes payable to bank | 15,053,245 | (37,300,000) |
| Proceeds from long-term obligations | 13,271,743 | 3,415,648 |
| Principal payments on long-term obligations | (8,079,108) | (6,667,930) |
| Noncontrolling interest in subsidiary equities | (56,230) | (258,543) |
| Cash patronage and retirement of equities | (791,226) | - |
| Payments for debt issuance | - | (897,094) |
| Other | (71,263) | 438,824 |
| Net cash provided by (used in) financing activities | <u>19,327,161</u> | <u>(41,269,095)</u> |
| Net (decrease) in cash and cash equivalents | <u>(1,651,936)</u> | <u>(16,080,571)</u> |
| Cash and cash equivalents, beginning of year | <u>1,651,936</u> | <u>17,732,507</u> |
| Cash and cash equivalents, end of year | <u>\$ -</u> | <u>\$ 1,651,936</u> |
| Supplemental disclosures of cash flow information: | | |
| Cash paid during the year for: | | |
| Interest | \$ 13,837,642 | \$ 14,260,315 |
| Income taxes (refunds) | 2,438,560 | (11,738,359) |

See accompanying notes to consolidated financial statements.

MFA INCORPORATED AND SUBSIDIARIES
Notes to Consolidated Financial Statements

(1) Summary of Significant Accounting Policies

(a) *Nature of Operations*

MFA Incorporated and subsidiaries (the Company) is a regional agricultural cooperative headquartered in Columbia, Missouri. The Company is a supplier of agricultural products and services including feed, seed, fertilizer, crop protection chemicals, and farm supplies. The Company also provides a marketing function for grain, livestock, and seed. The Company's customers are primarily farmers, locally owned cooperatives, and other agricultural supply businesses in the central United States.

(b) *Financial Statement Presentation*

The consolidated financial statements include the accounts of MFA Incorporated, its wholly owned subsidiary, MFA Enterprises, Inc. (divisions include Morris Farm Center, Phillips Feed, West Central AGRIServices, and Ag Choice), and a 94%-owned finance subsidiary, Agmo Corporation. All significant intercompany transactions and balances have been eliminated in consolidation.

The books of the Company are maintained on the accrual method of accounting for financial reporting purposes.

(c) *Cash Equivalents*

For purposes of the consolidated statement of cash flows, the Company considers all highly liquid debt instruments with an original maturity of three months or less as cash equivalents. Periodically, the Company maintains cash on deposit at financial institutions in excess of amounts insured by the U. S. Federal Deposit Insurance Corporation (FDIC). The cash balance shown on the balance sheet is offset by a line of credit balance maintained at a financial institution with a primary purpose of funding overdrafts of the Company's deposit accounts at the institution in the amount of \$3,898,000 and \$500 as of August 31, 2011 and 2010, respectively.

(d) *Receivables*

Substantially all of the Company's accounts and notes receivable are obligations of customers in the agricultural industry. The Company generally does not require collateral or other security on accounts receivable, but typically does require security on notes receivable. Credit risk is primarily controlled through credit approvals, limits, and monitoring procedures. The allowance for doubtful accounts is the Company's best estimate of the amount of probable credit losses in the Company's existing receivables. The Company determines the allowance based on historical write-off experience and specific identification.

(e) *Inventories*

All inventories are stated at the lower of cost or market using weighted-average cost, except as described herein.

(f) *Goodwill and Other Intangible Assets*

Goodwill represents the excess of costs over fair value of assets of businesses acquired. Goodwill and intangible assets acquired in a purchase business combination and determined to have an indefinite useful life are not amortized, but instead tested for impairment at least annually in accordance with the provisions of FASB ASC 350, *Intangibles - Goodwill and Other*. FASB ASC 350 also requires that intangible assets with estimable useful lives be amortized over their respective estimated useful lives to their estimated residual values, and be reviewed for impairment.

(g) *Investments*

Investments in cooperatives are stated at cost plus allocated equities, less equities redeemed, as the Company holds less than 20% of the equity of the cooperatives. All other investments, none of which are majority owned or controlled, are accounted for using the equity method.

(h) *Plant and Equipment*

Plant and equipment is carried at cost. Depreciation and amortization are calculated on the straight-line method over estimated useful lives of 20 to 50 years for buildings, 5 to 10 years for machinery and equipment and furniture and fixtures, and 3 to 5 years for transportation equipment.

(i) *Patronage Refunds Received*

Patronage refunds received from other cooperatives and affiliates are reflected as a reduction of cost of sales. Patronage refunds received from CoBank, ACB are deducted from interest expense.

(j) *Income Taxes*

As a cooperative, the Company is subject to income taxes on all income attributable to member business that is not paid or allocated to patrons and income arising from nonmember and non-patronage transactions. Income taxes are computed in accordance with the provisions of FASB ASC 740, *Income Taxes*. This approach requires the recognition of deferred tax assets and liabilities for the future tax consequences of temporary differences between the financial statement basis and the tax basis of assets and liabilities. Valuation allowances are established, when necessary, to reduce deferred income tax assets to the amount more likely than not to be realized. Open tax years subject to examination by the Internal Revenue Service as of August 31, 2011 were 2007 through 2010. Interest and penalties associated with income tax filings, if any, are recorded as other expense on the consolidated statement of operations.

(k) *Impairment of Long-lived Assets*

Long-lived assets are reviewed for impairment whenever events or changes in circumstances indicate the carrying amount of an asset or group of assets may not be recoverable. The impairment review includes a comparison of future cash flows expected to be generated by the asset or group of assets with their associated carrying value. If the carrying value of the asset or group of assets exceeds expected cash flows (undiscounted and without interest charges), an impairment loss is recognized to the extent fair value exceeds carrying amounts.

(l) *Use of Estimates*

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts

of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements, and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

(m) *Revenue Recognition*

The Company recognizes revenue when products are delivered and the customer takes ownership and assumes risk of loss, collection of the relevant receivable is probable, persuasive evidence of an arrangement exists, and the sales price is fixed or determinable.

(n) *Members' Equity*

The Company operates on a cooperative basis. Net income (determined on an income-tax basis) arising from transactions with members may be allocated to such members as patronage refunds. Each member's portion of the annual patronage refund is determined by the member's relative quantity or value of business transacted by the member. Patronage refunds are paid to members in the form of cash and allocated equities. Allocated equities are redeemable, at the discretion of the Company's board of directors or upon death of the member, at face value.

(o) *Sales Tax*

The Company collects sales tax from customers and remits the entire amount to the State. The Company's accounting policy is to exclude the tax collected and remitted to the State from revenues and cost of sales.

(p) *Subsequent Events*

The Company has evaluated events and transactions occurring after the balance sheet date through, November 1, 2011, which represents the date the audit of the consolidated financial statements were approved by management and, therefore, were available to be issued.

(2) Investments

Investments consist of the following as of August 31, 2011 and 2010:

| | <u>2011</u> | <u>2010</u> |
|------------------------------------|----------------------|----------------------|
| Cooperative investments: | | |
| CoBank, ACB | \$ 6,404,857 | \$ 5,985,799 |
| Ag Processing | 3,843,760 | 3,688,591 |
| Universal Cooperative | 2,108,824 | 2,108,824 |
| Other | 2,931,421 | 3,033,760 |
| Non-cooperative investments: | | |
| AgriServices of Brunswick, LLC | 5,053,269 | 2,285,317 |
| Cache River Valley Seed, LLC | 7,225,075 | 6,649,357 |
| Central Missouri AgriServices, LLC | 3,081,952 | 2,526,941 |
| | <u>\$ 30,649,158</u> | <u>\$ 26,278,589</u> |

Summarized financial information from the financial statements of the non-cooperative investments, as of August 31, 2011 and 2010, is as follows:

| | <u>2011</u> | <u>2010</u> |
|-------------|---------------|---------------|
| Assets | \$ 97,370,810 | \$ 78,931,194 |
| Liabilities | 65,142,830 | 54,883,498 |
| Revenues | 378,476,816 | 272,381,255 |
| Net income | 10,511,365 | 6,573,409 |

Receivables from investees of \$8,206,132 and \$12,595,968 at August 31, 2011 and 2010, respectively, are included in accounts and notes receivable.

(3) Other Assets

Other assets consist of the following as of August 31, 2011 and 2010:

| | <u>2011</u> | <u>2010</u> |
|---|---------------------|---------------------|
| Investments – nonqualified retirement plans | \$ 4,259,347 | \$ 4,574,151 |
| Debt issuance costs | 990,597 | 2,085,558 |
| Other | 369,743 | 287,552 |
| | <u>\$ 5,619,687</u> | <u>\$ 6,947,261</u> |

(4) Accounting for Derivatives and Hedging Activities

The Company accounts for derivative instruments under FASB ASC 815, *Derivatives and Hedging*. The Company formally documents its derivative activities, as well as its risk-management objectives and strategy for undertaking various hedge transactions. The Company formally assesses, both at the derivatives' inception and on an ongoing basis, whether the derivatives that are used in hedging transactions are to be accounted for as hedge transactions, and whether they qualify for the normal purchases and normal sales exemption under FASB ASC 815. The Company uses futures contracts to hedge against the effect of price fluctuations on forecasted purchases and sales of grain and livestock

transactions. Such contracts are not designated as hedging instruments under FASB ASC 815 and are, thus, reported at fair value and all market adjustments are recorded as either cost of sales or other operating revenue within the consolidated statement of operations.

At August 31, 2011 and 2010, the Company had recorded at fair value on its consolidated balance sheets the following assets and liabilities that are utilized for the sole purpose of managing the Company's price risk exposure on commodity purchases and sales:

| | | <u>Assets</u> | |
|--|------------------------|-----------------------|----------------------|
| | | Fair value | |
| | Balance sheet location | 2011 | 2010 |
| Futures contracts - grain | Inventories | \$ 135,198,063 | \$ 83,217,825 |
| Futures contracts - livestock | Inventories | - | 7,049,220 |
| Other | Inventories | 1,152,038 | - |
| Total derivative assets (not designated as hedging instruments under FASB ASC 815) | | <u>\$ 136,350,101</u> | <u>\$ 90,267,045</u> |

| | | <u>Liabilities</u> | |
|---|------------------------|--------------------|-------------------|
| | | Fair value | |
| | Balance sheet location | 2011 | 2010 |
| Futures contracts - grain | Inventories | \$ - | \$ - |
| Futures contracts - other | Inventories | - | 193,975 |
| Total derivative liabilities (not designated as hedging instruments under FASB ASC 815) | | <u>\$ -</u> | <u>\$ 193,975</u> |

For the years ended August 31, 2011 and 2010, the Company recorded in its statement of operations the following gains and losses on derivative instruments not designated as hedging instruments under FASB ASC 815:

| | | <u>Statement of Operations</u> | |
|---|---|--------------------------------|-----------------------|
| | | Amount recognized | |
| | Location of gain or (loss) on derivatives | 2011 | 2010 |
| Futures contracts - grain | Cost of sales | \$ 5,912,023 | \$ 1,890,528 |
| Futures contracts - livestock | Other operating revenue | 113,296 | (3,313,969) |
| Other | Cost of sales | (80,150) | (9,683) |
| Other | Other operating revenue | 76,045 | 7,227 |
| Total net income (loss) on derivatives not designated as hedging instruments under FASB ASC 815 | | <u>\$ 6,021,214</u> | <u>\$ (1,425,897)</u> |

The Company also enters into forward contracts on certain fertilizer products with contract terms normally lasting less than six months to protect against the effect of price fluctuations. These derivatives are exempt from accounting treatment under FASB ASC 815 as they qualify as normal purchase and normal sale derivatives. The Company has formal documentation regarding its strategy in its use of such instruments. Because these derivatives are exempt from accounting treatment under FASB ASC 815, they are classified as off-balance sheet hedges.

(5) Plant and Equipment

Plant and equipment consist of the following as of August 31, 2011 and 2010:

| | <u>2011</u> | <u>2010</u> |
|--|----------------------|----------------------|
| Land and buildings | \$ 93,888,338 | \$ 92,908,748 |
| Machinery and equipment | 148,950,614 | 146,483,896 |
| Transportation equipment | 33,596,091 | 33,979,474 |
| Furniture and fixtures | 14,049,005 | 14,001,003 |
| Construction in process | 812,293 | 1,659,664 |
| | <u>291,296,340</u> | <u>289,032,785</u> |
| Less accumulated depreciation and amortization | <u>214,536,899</u> | <u>208,134,971</u> |
| | <u>\$ 76,759,442</u> | <u>\$ 80,897,814</u> |

(6) Notes Payable to Banks and Long-Term Obligations

As of August 31, 2011 and 2010, the Company had open lines of short-term credit totaling \$250,000,000. At August 31, 2011, \$87,753,245 was outstanding at an average rate of 5.30%. At August 31, 2010, \$72,700,000 was outstanding at an average rate of 5.09%. Advances made under these commitments are primarily for financing seasonal inventories and accounts and notes receivable. The credit commitments are secured by inventories, accounts and notes receivable, and real estate.

The Company also had an open line of short-term credit totaling \$4,000,000 with a financial institution. The primary purpose of this line of credit is to fund overdrafts of deposit accounts held at the institution. At August 31, 2011 and 2010, \$3,898,000 and \$500 was outstanding, respectfully, with an average interest rate of 3.75%.

The Company's credit commitments require the Company to meet certain net worth, working capital and cash flow (EBITDA) requirements. The Company is also subject to additional covenants that limit debt and certain capital expenditures. As of August 31, 2011, the Company was in compliance all covenants.

Long-term obligations consist of the following as of August 31, 2011 and 2010:

| | <u>2011</u> | <u>2010</u> |
|--|----------------------|----------------------|
| Unsecured bonds, fixed rates from 2.5% to 8.25%, due through 2029 | \$ 55,696,391 | \$ 45,532,461 |
| Term loan, variable rate (3.88% as of August 31, 2011), due in annual installments of \$3,000,000 through 2019, secured by certain real property | 24,000,000 | 27,000,000 |
| Other, primarily capital leases | <u>3,013,124</u> | <u>4,041,211</u> |
| | 82,709,515 | 76,573,672 |
| Less current maturities | <u>12,372,611</u> | <u>17,137,548</u> |
| | <u>\$ 70,336,904</u> | <u>\$ 59,436,124</u> |

The maturity of long-term obligations by fiscal year is as follows:

| | |
|------------|----------------------|
| 2012 | \$ 12,372,611 |
| 2013 | 12,601,586 |
| 2014 | 11,223,729 |
| 2015 | 6,425,671 |
| 2016 | 11,579,142 |
| Thereafter | 28,506,776 |
| | <u>\$ 82,709,515</u> |

(7) Other Obligations

Other obligations consist of the following as of August 31, 2011 and 2010:

| | | |
|-------------------------------|---------------------|---------------------|
| | <u>2011</u> | <u>2010</u> |
| Nonqualified retirement plans | \$ 5,136,869 | \$ 4,627,107 |
| Deferred income taxes | 1,625,000 | 825,049 |
| Other | 867,554 | 1,494,510 |
| | <u>\$ 7,629,423</u> | <u>\$ 6,946,666</u> |

(8) Income Taxes

The difference between the provision for income taxes and the expected results by applying the Federal statutory rate to the pretax income results primarily from the available tax deduction status of cooperative member income.

The components of net deferred income tax assets and liabilities as of August 31, 2011 and 2010 are as follows:

| | <u>2011</u> | | <u>2010</u> | |
|--|------------------|------------------|------------------|------------------|
| | <u>Current</u> | <u>Long-Term</u> | <u>Current</u> | <u>Long-Term</u> |
| Deferred income tax assets: | | | | |
| Accruals not yet deductible for tax purposes | \$ 965,484 | \$ 701,182 | \$ 599,547 | \$ 7,060 |
| Uniform capitalization of inventory | 1,092,332 | - | 824,769 | - |
| Reserve for doubtful accounts | 380,065 | - | 357,315 | - |
| Net operating loss | 81,033 | 101,141 | 1,205,891 | 371,596 |
| Alternative minimum tax credit | - | - | 435,000 | 511,501 |
| Other | 1,235,500 | 53,237 | 690,713 | 1,010,517 |
| | <u>3,754,414</u> | <u>855,560</u> | <u>4,113,235</u> | <u>1,900,674</u> |

| | 2011 | | 2010 | |
|--|---------------------|-----------------------|---------------------|---------------------|
| | Current | Long-Term | Current | Long-Term |
| Deferred income tax liabilities: | | | | |
| Prepaid expenses deducted for tax purposes, not book | 545,633 | - | 441,760 | - |
| State refunds from net operating losses | - | - | 362,645 | - |
| Nonqualified notices of allocation | - | 9,781 | - | 9,781 |
| Depreciation | - | 2,372,914 | - | 2,633,161 |
| Other | - | 97,865 | - | 82,781 |
| | <u>545,633</u> | <u>2,480,560</u> | <u>804,405</u> | <u>2,725,723</u> |
| Net deferred income tax assets (liabilities) | <u>\$ 3,208,781</u> | <u>\$ (1,625,000)</u> | <u>\$ 3,308,830</u> | <u>\$ (825,049)</u> |

A valuation allowance for deferred tax assets is not considered necessary at August 31, 2011 and 2010.

(9) Employee Benefit Plans

The Company and several locally owned cooperatives participate in the MFA Incorporated Retirement Plan (the Plan), a multi-employer defined benefit pension plan, covering most of their employees with over one year of employment. Pension expense is recognized when billed by the Plan. The Company's pension expense for the years ended August 31, 2011 and 2010 was \$4,990,000 and \$4,165,000, respectively, which is equivalent to an average contribution rate of 7% of eligible participants' wages. The expense for 2011 includes an additional accrual of \$600,000 to cover the projected liability associated with a retroactive adjustment to the benefit multiplier. Net assets available for Plan benefits totaled \$101,527,751 and \$89,213,483 as of December 31, 2011 and 2010, respectively. The Company also offers an Excess Benefit Plan to all employees who are eligible for the Plan. The Company's expense for the years ended August 31, 2011 and 2010 was \$240,000 and \$230,000, respectively. The liability to participants was \$2,479,759 and \$2,557,366 as of August 31, 2011 and 2010, respectively. The fair value of plan assets was \$1,357,742 and \$1,608,838 as of August 31, 2011 and 2010, respectively.

The Company offers a nonqualified Voluntary Deferred Compensation Plan to certain management employees. The Company does not contribute to this Plan. The liability to participants was \$2,657,110 and \$2,069,741 as of August 31, 2011 and 2010, respectively. The fair value of plan assets was \$2,901,604 and \$2,965,313 as of August 31, 2011 and 2010, respectively.

The Company also has an employee 401(k) plan to which the Company may make discretionary matching contributions up to a maximum of \$400 per year to eligible participants. Contribution expense for the fiscal years ended August 31, 2011 and 2010 was approximately \$389,000 and \$393,000, respectively.

(10) Commitments and Contingent Liabilities

The Company has entered into various noncancelable operating lease agreements primarily for vehicles and other equipment. Rental expense related to operating leases was \$5,900,000 and \$5,859,000 for the years ended August 31, 2011 and 2010, respectively.

The Company is a defendant in several lawsuits arising from the normal course of business. Management is of the opinion that the ultimate resolution of these matters will not have a material adverse effect on the Company's consolidated financial statements.

The Company has guaranteed operating loans to AgriServices of Brunswick, LLC, a 50%-owned limited liability company. The maximum borrowings under the guaranteed operating loans of AgriServices of Brunswick, LLC are \$25,000,000. The loans guaranteed by the Company are limited to 55% of the commitment level, or no more than \$13,750,000. The amounts guaranteed totaled approximately \$0 and \$600,000 as of August 31, 2011 and 2010, respectively. The Company monitors its guarantees and reserves for losses on guarantees, if necessary.

At August 31, 2011, the Company services \$45.4 million loans sold to a third party under a master agreement where the Company has retained servicing. Under the terms of the master agreement, the Company has recourse on certain of these loans, ranging from 0% to 100%, with a total recourse potential of \$14.7 million. The Company has not recorded a reserve for this recourse liability based on estimated collectibility of the loans and prior payment history. The Company has not recorded an asset for servicing rights and has determined the amount to be immaterial to the consolidated financial statements.

(11) Fair Value of Financial Instruments

The Company applies the accounting standards under FASB ASC 820, *Fair Value Measurements and Disclosures*, which establishes a framework for measuring fair value and clarifies the definition of fair value within that framework. FASB ASC 820 defines fair value as an exit price, which is the price that would be received for an asset or paid to transfer a liability in the Company's principal or most advantageous market for the asset or liability, in an orderly transaction between market participants on the measurement date. The fair value hierarchy established in FASB ASC 820 generally requires an entity to maximize the use of observable inputs and minimize the use of unobservable inputs when measuring fair value. Observable inputs reflect the assumptions market participants would use in pricing the asset or liability and are developed based on market data obtained from sources independent of the reporting entity. Unobservable inputs reflect the entity's own assumptions based on market data and the entity's judgments about the assumptions that market participants would use in pricing the asset or liability, and are to be developed based on the best information available in the circumstances. The Company determines the fair market value of certain of its inventories of agricultural commodities and derivative contracts based on the fair value definition and hierarchy levels established in FASB ASC 820. FASB ASC 820 establishes three levels within its hierarchy that may be used to measure fair value:

Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities. Level 1 assets and liabilities include exchange-traded derivative contracts, U.S. treasury securities and certain publicly traded securities.

Level 2: Observable inputs, including Level 1 prices that have been adjusted; quoted prices for similar assets or liabilities; quoted prices in markets that are less active than traded exchanges; and other inputs that are observable or can be substantially corroborated by observable market data.

Level 3: Unobservable inputs that are supported by little or no market activity and that are a significant component of the fair value of the assets or liabilities. In evaluating the significance of fair value inputs, the Company generally classifies assets or liabilities as Level 3 when their fair value is determined using unobservable inputs that individually, or when aggregated with other unobservable inputs, represent more than 10 percent of the fair value of the assets or liabilities. Judgment is required in evaluating both quantitative and qualitative factors in the determination of significance for purposes of fair value level classification. Level 3 amounts can include assets and liabilities whose value is determined using internally developed pricing models, discounted cash flow methodologies or similar techniques, as well as assets and liabilities for which the determination of fair value requires significant management judgment or estimation.

The following table sets forth, by level, the Company's assets and liabilities that were accounted for at fair value on a recurring basis as of August 31, 2011. In some cases, a valuation technique used to measure fair value includes inputs from multiple levels of the fair value hierarchy. The lowest level of input that is a significant component of the fair value measurement determines the placement of the entire fair value measurement in the hierarchy.

| Description | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|--|--|---|--|-----------------|
| Assets: | | | | |
| Unrealized losses on exchange-traded derivative contracts, net of unrealized gains | \$ (15,919,438) | \$ - | \$ - | \$ (15,919,438) |
| Unrealized gains on forward purchase and sale contracts, net of unrealized losses | \$ - | \$ 21,727,824 | \$ - | \$ 21,727,824 |

The following table sets forth, by level, the Company's assets and liabilities that were accounted for at fair value on a recurring basis as of August 31, 2010:

| Description | Quoted Prices in Active Markets for Identical Assets (Level 1) | Significant Other Observable Inputs (Level 2) | Significant Unobservable Inputs (Level 3) | Total |
|--|--|---|--|----------------|
| Assets: | | | | |
| Unrealized losses on exchange-traded derivative contracts, net of unrealized gains | \$ (2,960,809) | \$ - | \$ - | \$ (2,960,809) |
| Unrealized gains on forward purchase and sale contracts, net of unrealized losses | \$ - | \$ 302,247 | \$ - | \$ 302,247 |

The Company's derivative contracts that are measured at fair value include exchange-traded commodity futures contracts and forward commodity purchase and sale contracts. Fair value for exchange-traded commodity futures contracts is based upon the broker quotations for identical commodities that are actively traded on an exchange. Fair value for forward commodity purchase and sale contracts is estimated based on exchange-quoted prices adjusted for differences in local markets. These differences are generally valued using inputs from broker or dealer quotations. When observable inputs are available for substantially the full term of the asset or liability, the derivative contracts are classified in Level 2. When

unobservable inputs have a significant impact on the measurement of fair value, the contract's fair value is classified in Level 3. Based on historical experience with suppliers and customers and knowledge of current market conditions, the Company does not view counterparty risk to be a significant input to fair value for the majority of its forward commodity purchase and sale contracts. However, in situations when the Company believes the counterparty risk to be a significant input, the Company records estimated fair value adjustments and classifies the contracts in Level 3 in the fair value hierarchy. Changes in the fair market value of commodity-related derivatives are recognized in the statement of operations as a component of cost of sales.

SUPPLEMENTARY INFORMATION

**INDEPENDENT AUDITORS' REPORT
ON ADDITIONAL INFORMATION**

To the Board of Directors of
MFA Incorporated:

Our report on our audits of the basic consolidated financial statements of MFA Incorporated and subsidiaries for 2011 and 2010 appears on page 1. Those audits were conducted for the purpose of forming an opinion on the basic consolidated financial statements taken as a whole. The accompanying information on pages 18 through 19 is presented for purposes of additional analysis and is not a required part of the basic consolidated financial statements. Such information has been subjected to the auditing procedures applied in the audits of the basic consolidated financial statements and, in our opinion, is fairly stated in all material respects in relation to the basic consolidated financial statements taken as a whole.

Williams - Keepers LLC

November 1, 2011

MFA INCORPORATED AND SUBSIDIARIES

Consolidating Balance Sheet

August 31, 2011

| Assets | MFA Inc. | MEI | AGMO | Eliminations | Consolidated |
|---|-----------------------|----------------------|----------------------|-----------------------|----------------------|
| Current assets: | | | | | |
| Cash and cash equivalents | \$ 1,315,880 | \$ (1,313,330) | \$ (2,550) | \$ - | \$ - |
| Accounts and notes receivable, net of allowance for doubtful accounts of \$1,757,000 | 99,547,868 | 11,352,877 | 10,145,904 | (27,119,853) | 93,926,796 |
| Inventories | 166,033,142 | 21,797,671 | - | - | 187,830,813 |
| Deferred income taxes | 3,556,781 | (348,000) | - | - | 3,208,781 |
| Prepaid expenses and other current assets | 4,594,040 | 454,697 | 11,392 | - | 5,060,129 |
| Total current assets | 275,047,711 | 31,943,915 | 10,154,746 | (27,119,853) | 290,026,519 |
| Investments | 48,183,000 | 371,685 | 254,496 | (18,160,023) | 30,649,158 |
| Notes receivable | 3,655,104 | 173,742 | - | - | 3,828,846 |
| Other assets | 5,619,687 | - | - | - | 5,619,687 |
| Goodwill | 1,446,800 | - | - | - | 1,446,800 |
| Plant and equipment, net | 67,201,330 | 9,557,859 | 253 | - | 76,759,442 |
| Total assets | <u>\$ 401,153,632</u> | <u>\$ 42,047,201</u> | <u>\$ 10,409,495</u> | <u>\$(45,279,876)</u> | <u>\$408,330,452</u> |
| Liabilities and Members' Equity Earned | | | | | |
| Current liabilities: | | | | | |
| Notes payable to banks | \$ 87,753,245 | \$ - | \$ - | \$ - | \$ 87,753,245 |
| Accounts payable | 98,225,871 | 27,279,654 | 4,750,000 | (27,119,853) | 103,135,672 |
| Accrued expenses | 13,047,271 | 1,528,504 | 17,994 | - | 14,593,769 |
| Current maturities of long-term obligations | 12,372,611 | - | - | - | 12,372,611 |
| Total current liabilities | 211,398,998 | 28,808,158 | 4,767,994 | (27,119,853) | 217,855,297 |
| Long-term obligations | 70,336,904 | - | - | - | 70,336,904 |
| Other obligations | 7,629,423 | - | - | - | 7,629,423 |
| Commitments and contingent liabilities | - | - | - | - | - |
| Noncontrolling interest | - | - | - | 858,346 | 858,346 |
| Members' equity | 61,692,688 | - | 5,127,512 | (5,127,512) | 61,692,688 |
| Retained earnings | 50,095,619 | 13,239,043 | 513,989 | (13,890,857) | 49,957,794 |
| Total liabilities and members' equity earned | <u>\$ 401,153,632</u> | <u>\$ 42,047,201</u> | <u>\$ 10,409,495</u> | <u>\$(45,279,876)</u> | <u>\$408,330,452</u> |

MFA INCORPORATED AND SUBSIDIARIES

Consolidating Statement of Operations

Year Ended August 31, 2011

| | <u>MFA Inc.</u> | <u>MEI</u> | <u>AGMO</u> | <u>Eliminations</u> | <u>Consolidated</u> |
|---|----------------------|---------------------|-------------------|-----------------------|----------------------|
| Revenues: | | | | | |
| Farm supply sales | \$ 713,460,836 | \$ 104,268,548 | \$ - | \$ (81,307,576) | \$ 736,421,808 |
| Grain marketing sales | 491,491,771 | 81,498,388 | - | - | 572,990,159 |
| Other operating revenues | 41,949,145 | 6,573,084 | - | (2,949,731) | 45,572,498 |
| Total revenues | <u>1,246,901,752</u> | <u>192,340,020</u> | <u>-</u> | <u>(84,257,307)</u> | <u>1,354,984,465</u> |
| Cost of sales | <u>1,088,148,209</u> | <u>167,361,984</u> | <u>-</u> | <u>(81,307,576)</u> | <u>1,174,202,617</u> |
| Operating margin | 158,753,543 | 24,978,036 | - | (2,949,731) | 180,781,848 |
| Operating expenses | <u>135,642,314</u> | <u>20,147,765</u> | <u>54,080</u> | <u>-</u> | <u>155,844,159</u> |
| Income (loss) from operations | 23,111,229 | 4,830,271 | (54,080) | (2,949,731) | 24,937,689 |
| Other income (expense): | | | | | |
| Interest expense | (12,340,951) | (1,025,865) | (438,230) | 1,464,095 | (12,340,951) |
| Other income, net | 11,238,144 | 194,955 | 1,006,299 | (1,464,095) | 10,975,303 |
| Total other income (expense), net | <u>(1,102,807)</u> | <u>(830,910)</u> | <u>568,069</u> | <u>-</u> | <u>(1,365,648)</u> |
| Income before income taxes | <u>22,008,422</u> | <u>3,999,361</u> | <u>513,989</u> | <u>(2,949,731)</u> | <u>23,572,041</u> |
| Income taxes: | | | | | |
| Current provision | 3,115,000 | 1,385,000 | - | - | 4,500,000 |
| Deferred provision | 755,000 | 145,000 | - | - | 900,000 |
| Total income taxes | <u>3,870,000</u> | <u>1,530,000</u> | <u>-</u> | <u>-</u> | <u>5,400,000</u> |
| Net income before noncontrolling interest | 18,138,422 | 2,469,361 | 513,989 | (2,949,731) | 18,172,041 |
| Noncontrolling interest in net income of subsidiary | - | - | - | (33,619) | 33,619 |
| Net income | <u>\$ 18,138,422</u> | <u>\$ 2,469,361</u> | <u>\$ 513,989</u> | <u>\$ (2,916,112)</u> | <u>\$ 18,138,422</u> |