

# MGP INGREDIENTS INC

## FORM 10-Q (Quarterly Report)

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Address	1300 MAIN ST ATCHISON, KS 66002
Telephone	9133671480
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Sector	Consumer/Non-Cyclical
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**UNITED STATES  
SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

**FORM 10-Q**

(Mark One)

- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the quarterly period ended **March 31, 2006**.

or

- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File Number: **0-17196**

**MGP INGREDIENTS, INC.**

(Exact name of registrant as specified in its charter)

**KANSAS**

(State or other jurisdiction of incorporation or organization)

**48-0531200**

(I.R.S. Employer Identification No.)

**1300 Main Street, Atchison Kansas**

(Address of principal executive offices)

**66002**

(Zip Code)

**(913) 367-1480**

(Registrant's telephone number, including area code)

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.  Yes  No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer and large accelerated filer" in Rule 12b02 of the Exchange Act.

(Check One)  Large accelerated filer  Accelerated filer  Non-accelerated filer

Indicated by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).  Yes  No

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Common stock, no par value  
16,149,090 shares outstanding  
as of March 31, 2006

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PART I. FINANCIAL INFORMATION

- Item 1. Financial Statements
  - Independent Accountants' Review Report
  - Condensed Consolidated Balance Sheets as of March 31, 2006 and June 30, 2005
  - Condensed Consolidated Statements of Income for the Three and Nine Months Ended March 31, 2006 and 2005
  - Condensed Consolidated Statements of Cash Flows for the Nine Months Ended March 31, 2006 and 2005
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## Report of Independent Registered Public Accounting Firm

Audit Committee, Board of Directors  
and Stockholders  
MGP Ingredients, Inc.  
Atchison, Kansas

We have reviewed the accompanying condensed consolidated balance sheet of MGP Ingredients, Inc. as of March 31, 2006 and the related condensed consolidated statements of income for the three-month and nine-month periods ended March 31, 2006 and 2005, and cash flows for the nine-month periods ended March 31, 2006 and 2005. These interim financial statements are the responsibility of the Company's management.

We conducted our reviews in accordance with the standards of the Public Company Accounting Oversight Board (United States). A review of interim financial information consists principally of applying analytical procedures to financial data and making inquiries of persons responsible for financial and accounting matters. It is substantially less in scope than an audit conducted in accordance with the standards of the Public Company Accounting Oversight Board, the objective of which is the expression of an opinion regarding the financial statements taken as a whole. Accordingly, we do not express such an opinion.

Based on our reviews, we are not aware of any material modifications that should be made to the condensed consolidated financial statements referred to above for them to be in conformity with accounting principles generally accepted in the United States of America.

We have previously audited, in accordance with the standards of the Public Company Accounting Oversight Board (United States), the consolidated balance sheet as of June 30, 2005 and the related consolidated statements of income, stockholders' equity and cash flows for the year then ended (not presented herein); and in our report dated August 26, 2005, we expressed an unqualified opinion on those consolidated financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of June 30, 2005 is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

/s/ **BKD, LLP**

Kansas City, Missouri  
May 2, 2006

MGP Ingredients, Inc.

Condensed Consolidated Balance Sheets (in Thousands)

Assets	March 31, 2006 (Unaudited)	June 30, 2005
<b>Current Assets</b>		
Cash and cash equivalents	\$ 3,586	\$ 10,384
Receivables, net of allowance of \$320 at March 31, 2006 and \$320 at June 30, 2005	32,024	28,097
Inventories	40,071	31,252
Prepaid expenses	1,446	628
Refundable income taxes		2,622
Deferred income taxes	945	663
<b>Total current assets</b>	<u>78,072</u>	<u>73,646</u>
Property and Equipment, at cost	331,514	317,626
Less accumulated depreciation	(211,080)	(201,997)
<b>Total property and equipment, net</b>	<u>120,434</u>	<u>115,629</u>
Other Assets	215	225
<b>Total assets</b>	<u>\$ 198,721</u>	<u>\$ 189,500</u>

See Accompanying Notes to Condensed Consolidated Financial Statements  
and Independent Accountants' Review Report

MGP Ingredients, Inc.

Condensed Consolidated Balance Sheets (in Thousands)

<b>Liabilities and Stockholders' Equity</b>	<b>March 31, 2006 (Unaudited)</b>	<b>June 30, 2005</b>
<b>Current Liabilities</b>		
Current maturities of long-term debt	\$ 3,757	\$ 4,705
Note payable bank	6,000	—
Accounts payable	11,701	11,744
Accrued expenses	6,819	5,621
Deferred revenue	9,767	10,948
Income taxes payable	1,186	—
<b>Total current liabilities</b>	<b>39,230</b>	<b>33,018</b>
<b>Long-term Debt</b>	<b>13,317</b>	<b>16,785</b>
<b>Post-Retirement Benefits</b>	<b>6,624</b>	<b>6,342</b>
<b>Deferred Income Taxes</b>	<b>12,811</b>	<b>12,828</b>
<b>Stockholders' Equity</b>		
Capital stock		
Preferred, 5% cumulative, \$10 par value; authorized 1,000 shares; issued and outstanding 437 shares	4	4
Common, no par; authorized 40,000,000 shares; issued 19,530,344 shares	6,715	6,715
Additional paid-in capital	6,117	5,341
Retained earnings	128,901	124,754
Accumulated other comprehensive loss - Cash flow hedges	360	(228)
	<b>142,097</b>	<b>136,586</b>
<b>Treasury stock, at cost</b>		
Common		
March 31, 2006 - 3,381,254 shares		
June 30, 2005 - 3,536,064 shares	(15,358)	(16,059)
<b>Total stockholders' equity</b>	<b>126,739</b>	<b>120,527</b>
<b>Total liabilities and stockholders' equity</b>	<b>\$ 198,721</b>	<b>\$ 189,500</b>

See Accompanying Notes to Condensed Consolidated Financial Statements  
and Independent Accountants' Review Report.

MGP Ingredients, Inc.

Condensed Consolidated Statements of Income (in Thousands)

(Unaudited)

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2006	2005	2006	2005
Net sales	\$ 79,422	\$ 71,186	\$ 232,139	\$ 201,228
Cost of sales	71,348	64,270	206,141	182,466
<b>Gross profit</b>	<b>8,074</b>	<b>6,916</b>	<b>25,998</b>	<b>18,762</b>
Selling, general and administrative	5,471	4,864	16,219	14,254
	2,603	2,052	9,779	4,508
Other operating income	150	153	599	579
<b>Operating income</b>	<b>2,753</b>	<b>2,205</b>	<b>10,378</b>	<b>5,087</b>
Other income (expense)	417	505	1,054	870
Interest (expense)	(350)	(350)	(1,182)	(1,040)
<b>Income before income taxes</b>	<b>2,820</b>	<b>2,360</b>	<b>10,250</b>	<b>4,917</b>
Provision for income taxes	737	733	3,618	1,645
<b>Net income</b>	<b>2,083</b>	<b>1,627</b>	<b>6,632</b>	<b>3,272</b>
Other comprehensive income, net of taxes	330	569	588	222
<b>Comprehensive income</b>	<b>\$ 2,413</b>	<b>\$ 2,196</b>	<b>\$ 7,220</b>	<b>\$ 3,494</b>
Basic earnings per common share	\$ 0.13	\$ 0.10	\$ 0.41	\$ 0.20
Diluted earnings per common share	\$ 0.12	\$ 0.10	\$ 0.40	\$ 0.20
Dividends per common share	\$ —	\$ —	\$ 0.15	\$ 0.15

See Accompanying Notes to Condensed Consolidated Financial Statements and Independent Accountants' Review Report.

MGP Ingredients, Inc.

Condensed Consolidated Statements of Cash Flows (in Thousands)

Nine Months Ended March 31,

(Unaudited)

	2006	2005
<b>Operating Activities</b>		
Net income	\$ 6,632	\$ 3,272
Items not requiring cash		
Depreciation and amortization	9,130	11,867
Gain on sale/conversion of property and equipment	(14)	(811)
Deferred income taxes	(299)	(2,700)
Changes in:		
Accounts receivable	(3,927)	2,321
Inventories	(8,231)	(4,936)
Insurance receivable	—	1,425
Accounts payable and accrued expenses	1,207	(2,346)
Deferred income	(1,181)	(1,242)
Income taxes receivable/payable	3,808	(7)
Prepaid expenses and other current assets	(818)	(686)
<b>Net cash provided by operating activities</b>	<b>6,307</b>	<b>6,157</b>
<b>Investing Activities</b>		
Additions to property and equipment	(13,732)	(13,695)
Proceeds from sale/conversion of property and equipment	51	1,005
<b>Net cash used in investing activities</b>	<b>(13,681)</b>	<b>(12,690)</b>
<b>Financing Activities</b>		
Proceeds from stock options exercised	1,477	721
Proceeds from issuance of long-term debt	7,000	9,990
Borrowings on line of credit	6,000	2,000
Payments on long-term debt	(11,416)	(3,666)
Dividends paid	(2,485)	(2,431)
<b>Net cash provided by financing activities</b>	<b>576</b>	<b>6,614</b>
Increase (Decrease) in Cash and Cash Equivalents	(6,798)	81
Cash and Cash Equivalents, Beginning of Period	10,384	6,488
Cash and Cash Equivalents, End of Period	<u>\$ 3,586</u>	<u>\$ 6,569</u>

See Accompanying Notes to Condensed Consolidated Financial Statements and Independent Accountants' Review Report.



## MGP Ingredients, Inc.

### Notes to Condensed Consolidated Financial Statements

#### Note 1. Basis of Presentation

The accompanying unaudited condensed consolidated financial statements reflect all adjustments that are, in the opinion of the Company's management, necessary to fairly present the financial position, results of operations and cash flows of the Company. Those adjustments consist only of normal recurring adjustments. The condensed consolidated balance sheet as of June 30, 2005 has been derived from the audited consolidated balance sheet of the Company as of that date. Certain information and note disclosures normally included in the Company's annual financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the consolidated financial statements and notes thereto in the Company's Form 10-K Annual Report for the fiscal year ended June 30, 2005 filed with the Securities and Exchange Commission. The results of operations for the period are not necessarily indicative of the results to be expected for the full year.

#### Note 2. Earnings Per Share

Earnings per common share data is based upon the weighted average number of common shares outstanding. Employee stock—based compensation represents the only potentially dilutive securities held by the Company.

	Three Months Ended March 31, 2006	Nine Months Ended March 31, 2006	Three Months Ended March 31, 2005	Nine Months Ended March 31, 2005
Weighted average shares:				
Basic	16,136,450	16,068,767	15,989,499	15,967,992
Additional weighted average shares attributable to:				
Employee shared-based compensation:	751,826	698,200	420,008	580,716
Diluted	<u>16,888,276</u>	<u>16,766,967</u>	<u>16,409,507</u>	<u>16,548,708</u>

The Company has a stock-based employee compensation plan, which it accounts for under the recognition and measurement principles of APB Opinion No. 25, *Accounting for Stock Issued to Employees*, and Statement of Financial Accounting Standard No. 123R, *Share-Based Payment*, ("SFAS 123R"). Compensation expense is recognized in net income over the vesting period for restricted stock awards and stock options. For the quarter and year to date periods ended March 31, 2005, no compensation expense is reflected in net income related to stock options issued.

Effective July 1, 2005, the Company adopted SFAS 123R using the modified prospective application transition method. This standard requires the Company to record compensation costs, on a prospective basis, for the unvested portion of stock awards with such amount being calculated under the fair value based method. Compensation expense related to share-based employee compensation for the nine months ended March 31, 2006 was approximately \$272,000.

The following table illustrates the effect on net income and earnings per share if the Company had applied the fair value provisions of SFAS 123R, to all of the stock based employee compensation under those plans.

	Three Months Ended March 31, 2006	Nine Months Ended March 31, 2006	Three Months Ended March 31, 2005	Nine Months Ended March 31, 2005
	(in thousands except per share amounts)			
Net income, as reported	\$ 2,083	\$ 6,632	\$ 1,627	\$ 3,272
Plus: Stock-based employee compensation included in net income	—	—	66	132
Less: Total stock-based employee compensation cost determined under the fair value based method, net of income taxes	—	—	(156)	(312)
Pro forma net income	<u>\$ 2,083</u>	<u>\$ 6,632</u>	<u>\$ 1,537</u>	<u>\$ 3,092</u>
	Three Months Ended March 31, 2006	Nine Months Ended March 31, 2006	Three Months Ended March 31, 2005	Nine Months Ended March 31, 2005
Earnings per share				
Basic - as reported	\$ 0.13	\$ 0.41	\$ 0.10	\$ 0.20
Basic - pro forma	\$ —	\$ —	\$ 0.10	\$ 0.19
Diluted - as reported	\$ 0.12	\$ 0.40	\$ 0.10	\$ 0.20
Diluted - pro forma	\$ —	\$ —	\$ 0.09	\$ 0.18

**Note 3. Long Term Debt**Note Payable: General Electric Capital Corporation :

The Company borrowed an additional \$7,000,000 from General Electric Capital Corporation (GECC) on September 29, 2005 and paid the unsecured senior notes payable to The Principal Mutual Life Insurance Company of \$6,816,000. The Company's obligations to GECC are evidenced by a promissory note bearing interest at 5.92% per annum and payable in 60 consecutive monthly payments, with the first payment being \$138,525, the next 58 payments being \$135,071 and the final payment being the remaining amount of outstanding principal and interest. The note may be prepaid at any time in its entirety subject to the payment of a prepayment premium equal to 3% of the original principal amount if the note is prepaid prior to the first anniversary, declining to 1% if paid prior to the third anniversary and 0% thereafter.

The Company also entered a security agreement to secure the note. The security agreement grants a security interest in all the Company's equipment located or to be located at the Company's KCIT facility in Kansas City, Kansas. Under the security agreement, the Company has agreed to indemnify the secured party against any claim arising in connection with the collateral.

Indebtedness under the note can be accelerated if any payment is not made within 10 days of its due date or if there is an event of default under the security agreement, certain acts of bankruptcy or insolvency, defaults by the Company under any other obligations and the merger or consolidation of the Company without the consent of GECC, which consent may not be unreasonably withheld.

At the time of the loan from GECC, the Company's other indebtedness included a note payable to GE Capital Public Finance ("GECPF"), an affiliate of GECC, which also is secured by equipment at the Company's Kansas City, Kansas facility. In connection with the loan to GECC, the Company also entered into a cross-collateral and cross default agreement with GECC and GECPF in which the Company agreed, among other matters, that all collateral in which either creditor has a security interest will secure the payment of liabilities to both creditors.

Revolving Line of Credit :

At March 31, 2006, the Company has borrowed \$6.0 million on its \$20.0 million unsecured revolving line of credit, which presently is scheduled to expire on July 1, 2006. The current rate on these borrowings is prime minus 1%.

**Note 4. Contingencies**

There are various legal proceedings involving the Company and its subsidiaries. Except as noted below, management considers that the aggregate liabilities, if any, arising from such actions would not have a material adverse effect on the consolidated financial position or operations of the Company.

The Company has been in negotiations with the United States Environmental Protection Agency (USEPA), the Illinois Attorney General's Office and the Illinois Environmental Protection Agency (IEPA) to settle two separate enforcement proceedings related to emissions at the Pekin, Illinois location. The Company also has been in discussions with the Kansas Department of Health and Environment (KDHE) relating to air emissions at its Atchison facility. The Company has entered into a consent agreement with KDHE resolving past allegations relating to its Atchison facility and paid a civil penalty of \$26,000. The Company has entered a consent decree to resolve the USEPA Illinois proceeding and agreed to pay a federal penalty of \$172,000 which is due by May 19, 2006. The consent decree been approved by the court. The IEPA has most recently requested a \$600,000 penalty payable over time or a \$500,000 penalty payable in a lump sum to resolve its complaint. The Company and IEPA are involved in efforts to settle the IEPA proceeding, but no resolution has occurred. As of March 31, 2006, the Company had accrued \$600,000, which is included in other accrued liabilities, with respect to these matters. The amount of the ultimate settlement could differ materially in the near future.

**Note 5. Operating Segments**

The Company is a fully integrated producer of ingredients and distillery products. Products included within the ingredients segment consist of starches, including commodity wheat starch and modified and specialty wheat and potato starches, proteins, including commodity wheat gluten, specialty wheat, soy and other proteins, and mill feeds. Distillery products consist of food grade alcohol, including beverage alcohol and industrial alcohol, fuel alcohol, commonly known as ethanol, and distillers grain and carbon dioxide, which are by-products of the Company's distillery operations.

The operating profit for each segment is based on net sales less identifiable operating expenses. Interest expense, investment income and other general miscellaneous expenses have been excluded from segment operations and classified as Corporate. Receivables, inventories and equipment have been identified with the segments to which they relate. All other assets are considered as Corporate.

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2006	2005	2006	2005
Ingredients	\$ 22,324	\$ 24,245	\$ 66,786	\$ 65,859
Distillery products	57,098	46,941	165,353	135,369
	<u>\$ 79,422</u>	<u>\$ 71,186</u>	<u>\$ 232,139</u>	<u>\$ 201,228</u>
Depreciation				
Ingredients	\$ 1,587	\$ 1,682	\$ 4,685	\$ 4,805
Distillery products	1,394	2,196	4,044	6,554
Corporate	135	143	391	508
	<u>\$ 3,116</u>	<u>\$ 4,021</u>	<u>\$ 9,120</u>	<u>\$ 11,867</u>
Income before income taxes				
Ingredients	\$ (2,175)	\$ (941)	\$ (4,568)	\$ (2,741)
Distillery products	5,831	3,576	16,636	8,751
Corporate	(836)	(275)	(1,818)	(1,093)
	<u>\$ 2,820</u>	<u>\$ 2,360</u>	<u>\$ 10,250</u>	<u>\$ 4,917</u>
			March 31, 2006	June 30 2005
Identifiable assets				
Ingredients			\$ 79,436	\$ 81,507
Distillery products			97,227	79,678
Corporate			22,058	28,315
			<u>\$ 198,721</u>	<u>\$ 189,500</u>

**Note 6. Pension and Post Retirement Benefit Obligations**

The Company and its subsidiaries provide certain post-retirement health care and life benefits to all employees. The liability for such benefits is unfunded. The Company uses a May 31 measurement date for the plan

The components of the Net Periodic Benefit Cost for the three months and nine months ended March 31 are as follows:

	Three Months Ended March 31,		Nine Months Ended March 31,	
	2006	2005	2006	2005
Service cost	\$ 74	\$ 60	\$ 222	\$ 180
Interest cost	74	75	222	225
Prior service cost	(9)	(12)	(27)	(36)
(Gain) loss	—	(1)	—	(3)
Total post-retirement benefit cost	<u>\$ 139</u>	<u>\$ 122</u>	<u>\$ 417</u>	<u>\$ 366</u>

The Company previously disclosed in its financial statements for the year ended June 30, 2005, amounts expected to be paid to plan participants. There have been no revisions to these estimates and there have been no changes in the estimate of total employer contributions expected to be made for the fiscal year ended June 30, 2006.

Total employer contributions for the quarter and year to date ended March 31, 2006 were \$138,000.

The Medicare Prescription Drug Improvement Modernization Act of 2003 (the Act) provides certain drug benefits under Medicare Part D, as well as a federal subsidy to sponsors of retiree health care benefit plans that provide benefits at least actuarially equivalent to Medicare Part D. The Company has been unable to conclude whether the benefits provided under the plan are actuarially equivalent to Medicare Part D. Accordingly, the net periodic post-retirement benefit costs above do not reflect any amount associated with the subsidiary.

#### **Note 7. New Accounting Pronouncements**

In May 2005, the Financial Accounting Standards Board (FASB) issued SFAS Statement No. 154 (“SFAS 154”), Accounting Changes and Error Corrections. SFAS 154 requires that, when a company changes its accounting policies, the change must be applied retrospectively to all prior periods presented instead of a cumulative effect adjustment in the period of the change. SFAS 154 may also apply when the FASB issues new rules requiring changes in accounting. If the new rule allows cumulative effect treatment, it will take precedence over SFAS 154. This statement is effective for fiscal years beginning after December 15, 2005. Because the Company’s financial statements for the periods ended March 31, 2006 and 2005 contain no error corrections or accounting changes affected by SFAS 154, this statement has had no impact. In future periods, as the FASB issues new rules requiring changes in accounting, this statement could have a material impact on financial results previously reported.

## **ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS.**

### **FORWARD-LOOKING STATEMENTS**

This section contains forward-looking statements as well as historical information. All statements, other than statements of historical facts, included in this Quarterly Report on Form 10-Q regarding the prospects of our industry and our prospects, plans, financial position and business strategy may constitute forward-looking statements. In addition, forward-looking statements are usually identified by or are associated with such words such as "intend," "plan", "believe," "estimate," "expect," "anticipate," "hopeful," "should," "may," "will", "could" and or the negatives of these terms or variations of them or similar terminology. They reflect management's current beliefs and estimates of future economic circumstances, industry conditions, Company performance and financial results and are not guarantees of future performance. All such forward-looking statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those contemplated by the relevant forward-looking statement. Important factors that could cause actual results to differ materially from our expectations include, among others: (i) the availability and cost of grain, (ii) fluctuations in gasoline prices, (iii) fluctuations in energy costs, (iv) competitive environment and related market conditions, (vi) our ability to realize operating efficiencies, (vii) the effectiveness of our hedging programs, (viii) access to capital and (ix) actions of governments. For further information on these and other risks and uncertainties that may affect our business, see *Item 1. Business — Risks and Uncertainties* of our Annual Report on Form 10-K for the fiscal year ended June 30, 2005.

### **RESULTS OF OPERATIONS**

#### **General**

Reference is made to *Management's Discussion and Analysis of Financial Condition and Results of Operations—General*, incorporated by reference to Item 7 of our Annual Report on Form 10-K for the fiscal year ended June 30, 2005, for certain general information about our principal products and costs.

#### **Critical Accounting Policies**

Reference is made to *Management's Discussion and Analysis of Financial Condition and Results of Operations—Critical Accounting Policies*, incorporated by reference to Item 7 of our Annual Report on Form 10-K for the fiscal year ended June 30, 2005, for accounting policies which are considered by management to be critical to an understanding of the Company's financial statements.

#### **Developments in the Distillery Products Segment**

On March 16, 2006 our Board of Directors approved plans for an \$11.1 million capital project that is expected to improve production efficiencies and fulfill air emission control requirements at our Pekin, Illinois, distillery. The project involves the purchase and installation of a new dryer system for the manufacture of distillers feed, the principal by-product of the alcohol production process. The new dryer

system is expected to result in cost savings related to energy usage and maintenance needs. It also will permit us to meet Environmental Protection Agency requirements in a recently filed consent decree. We chose the dryer over less costly alternatives because of the improved plant efficiencies it is expected to provide. Work on the dryer project is expected to commence in the summer of 2006 and be completed by the fall of 2007.

### Developments in the Ingredients Segment

In the first quarter of fiscal 2005, we entered into a business alliance with Cargill, Incorporated for the production and marketing of a new resistant starch called Fibersym™ HA that is derived from high amylose corn. Shortly thereafter, we put the sale and additional production of that product on hold because of pending litigation filed in November of that year (see Item 3. *Legal Proceedings* in our Annual Report on Form 10-K for the fiscal year ended June 30, 2005). The litigation is still pending, but we have resumed limited marketing efforts.

### Segment Results

The following is a summary of revenues and pre-tax income/(loss) allocated to each reportable operating segment for the three months and nine months ended March 31, 2006 and 2005. (For additional information regarding our operating segments, see *Note 5-Operating Segments* included under *Part 1, Item 1, Financial Statements* of this Form 10-Q and incorporated herein by reference.)

(In Thousands)	<u>Third Quarter Fiscal 2006</u>	<u>Third Quarter Fiscal 2005</u>	<u>Nine Months Fiscal 2006</u>	<u>Nine Months Fiscal 2005</u>
<b>Ingredients</b>				
Net Sales	\$ 22,324	\$ 24,245	\$ 66,786	\$ 65,859
Pre-Tax Income	(2,175)	(941)	(4,568)	(2,741)
<b>Distillery Products</b>				
Net Sales	\$ 57,098	\$ 46,941	\$ 165,353	\$ 135,369
Pre-Tax Income	5,831	3,576	16,636	8,751

### General

Total earnings in the third quarter of fiscal 2006 increased compared to the third quarter of fiscal 2005 as the result of increased profitability in our distillery products segment, which more than offset a loss in our ingredients segment. The increase in distillery profits occurred notwithstanding higher energy costs resulting from significant hikes in natural gas prices, principally during the first two months of the quarter, which also partially impacted our earnings performance in the ingredients segment. Profitability in the ingredients segment was further affected by reduced unit sales and prices for certain of our higher valued specialty ingredients along with higher raw material prices for wheat compared to the prior year's third quarter.



The improvement in total sales revenue compared to a year ago resulted from increased sales in the distillery products segment of our business. Distillery products sales rose by approximately \$10.2 million, or 21.6 percent, above distillery products sales in the third quarter of fiscal 2005. Sales of ingredients, on the other hand, decreased by approximately \$1.9 million, or approximately 8 percent, compared to last year's third quarter.

The increase in distillery products sales resulted from higher unit sales and improved selling prices for food grade alcohol for beverage and industrial applications combined with improved prices for fuel grade alcohol. Sales of distillers feed, the principal by-product of our alcohol production process, increased slightly compared to the prior year's third quarter due to higher unit sales, which offset lower selling prices. A significant percentage of our fuel grade alcohol sales are made pursuant to contracts of from six to nine months duration. In line with this practice, at April 1, 2006 we had contracted a sizeable portion of our total current alcohol capacity to customers in the fuel alcohol area through the end of calendar 2006. Consistent with forward market activity, these contracts are at prices higher than previous contracts which were in effect during all or part of the third quarter.

The decrease in ingredients sales resulted primarily from lower sales of specialty ingredients for both food and non-food applications combined with lower sales of commodity gluten. Sales of commodity wheat starch, meanwhile, increased compared to a year ago as the result of increased unit sales and prices.

The decrease in sales of specialty ingredients for food applications was principally due to lower unit sales of our Fibersym™ line of resistant starches for incorporation in fiber-enriched, reduced carbohydrate and lower calorie foods together with reduced unit sales and lower prices for our Arise® line of specialty wheat protein isolates. These decreases were partially offset by improved sales of our Wheatex® line of textured proteins for use in the production of vegetarian products and meat extension applications, as well as certain of our Pregel™ instant starches that are used in a variety of processed and bakery food applications. The decline in sales of specialty ingredients for non-food applications resulted mainly from decreased sales of our MGPI Chewtix™ line of protein- and starch-based resins, which are produced for use in the manufacture of pet chews and related treats. However, Chewtix™ sales improved on a sequential basis compared to the second quarter. Sales of ingredients for use in personal care products decreased modestly compared to the prior year.

## **Ingredients**

Total ingredient sales in the third quarter of fiscal 2006 decreased by approximately \$1.9 million, or approximately 8 percent, compared to the prior year's third quarter. This principally was due to a nearly \$500,000, or 5 percent, decline in sales of specialty ingredients for food applications and a \$1.2 million, or 15 percent, reduction in sales of specialty ingredients for non-food applications. Commodity ingredient sales decreased by approximately \$800,000, or 18.7 percent. This decrease resulted from a \$1.2 million, or 35.1 percent, drop in sales of commodity gluten, which more than offset a \$400,000, or 41.9 percent, increase in sales of commodity starches. Sales of mill feed and other mill products increased by nearly \$600,000, or 265 percent. The decrease in sales of specialty ingredients for food applications compared to the prior year's third quarter was mainly attributable to reduced sales of our Fibersym™ resistant starches and Arise® wheat protein isolates. Higher sales of our Wheatex® textured wheat proteins and certain of our Pregel™ specialty starches partially offset these reductions. The decrease in sales of specialty ingredients for non-food applications principally occurred in sales of our Chewtix® protein- and starch-based resins for use in pet industry products. The increase in sales of mill feeds, which is a by-product in the manufacture of flour, and other mill products resulted from the processing of more flour in the current year's third quarter for use in producing starches and proteins.

## **Distillery Products**

Total sales of our distillery products in the third quarter of fiscal 2006 rose by approximately \$10.2 million, or 21.6 percent, compared to the third quarter of fiscal 2005. This improvement was due to a \$6.4 million, or 43.2 percent, increase in sales of food grade alcohol and a \$3.7 million, or 14.8 percent, increase in sales of fuel grade alcohol. In the food grade area, sales of alcohol for industrial applications rose by \$4.7 million, or 45.0 percent, and sales of food grade alcohol for beverage applications rose by approximately \$1.6 million, or 37.2 percent, in each case due to a combination of higher prices and increased unit sales. The increased sales of fuel grade alcohol resulted from higher average selling prices. Distillers feed increased by \$100,000, or 1.4 percent, as the result of higher unit sales.

## **Sales**

Net sales in the third quarter of fiscal 2006 were approximately \$8.2 million, or 11.6 percent, higher than net sales in the third quarter of fiscal 2005. This improvement was due to a \$10.2 million, or 21.6 percent, increase in sales of distillery products, which more than offset a \$1.9 million, or approximately 8 percent decrease in sales of ingredients. The increase in distillery products resulted from increased unit sales and higher selling prices for food grade alcohol for both industrial and beverage applications, increased prices for fuel grade alcohol and increased unit sales of distillers feed, which offset a small decline in fuel alcohol unit sales and lower prices for distillers feed year-over-year. The decrease in ingredients sales was principally due to reduced sales of specialty ingredients for both food and non-food applications together with lower unit sales of commodity gluten. Sales of commodity wheat starches were higher than the prior year due to increased unit sales and improved prices.

For the first nine months of fiscal 2006, net sales increased by \$30.9 million, or 15.4 percent, above net sales for the first nine months of fiscal 2005. This improvement was principally due to increased distillery products sales in each of the first three quarters of fiscal 2006. Ingredients sales increased slightly in the first nine months of the current fiscal year compared to the same period the prior year. The increase in distillery products sales largely resulted from higher unit sales and prices for food grade alcohol for industrial and beverage applications and increased prices for fuel grade alcohol, which offset a small decline in fuel alcohol unit sales. The increase in ingredients sales for the first nine months of fiscal 2006 principally resulted from increased unit sales of specialty ingredients for food applications together with higher unit sales of commodity gluten. These increases offset a decline in unit sales of specialty ingredients for non-food applications. The increase in commodity gluten sales during the first nine months of fiscal 2006 resulted from higher unit sales compared to the prior year's first nine months. This increase adversely affected our profitability, as market prices for gluten have been below our cost of production. Although we have deemphasized gluten sales because of such poor market conditions, gluten remains a co-product from the processing of flour for starch. Because increases in sales of our specialty proteins have not grown proportionately with increases in our specialty starch sales, we had more gluten available for sale during the first nine months of fiscal 2006 than in the first nine months of the prior fiscal year, as less gluten has been processed into specialty proteins.

## **Cost of Sales**

The cost of sales in the third quarter of fiscal 2006 rose by approximately \$7.1 million, or nearly 11 percent, over cost of sales in the third quarter of fiscal 2005. This increase was mainly due to a 56 percent increase in energy costs and, to a significantly lesser extent, higher raw material costs for grain and higher

costs of supplies used in our manufacturing processes. The increase was partially offset by reduced depreciation expense resulting from a lower depreciable asset base due to certain assets being fully depreciated at our Pekin, Illinois facility. The increased energy costs primarily resulted from higher natural gas prices, which were up approximately 62 percent compared to the prior fiscal year's third quarter. The higher costs of manufacturing-related grain and supplies were primarily due to increased production. Wheat prices were approximately 13 percent higher than those experienced in the third quarter of fiscal 2005 and corn prices averaged nearly 2 percent higher compared to a year ago.

The cost of sales for the first nine months of fiscal 2006 increased by approximately \$23.7 million, or 13 percent, primarily due to higher energy costs, which were partially offset by a decrease in raw material costs for grain .

In connection with the purchase of raw materials, principally corn and wheat, for anticipated operating requirements, we enter into commodity contracts to hedge the risk of future grain price increases. During the third quarter of fiscal 2006, we hedged approximately 42 percent of corn processed compared with approximately 27 percent of corn hedged in the third quarter of fiscal 2005. Of the wheat that we processed in the current year's third quarter, approximately 5 percent was hedged. No wheat was hedged in the third quarter of fiscal 2005. During the first nine months of fiscal 2006, we hedged approximately 40 percent of corn processed compared with 45 percent of corn hedged in the first nine months of fiscal 2005. Of the wheat that we processed in the first nine months of fiscal 2006, 1.8 percent was hedged compared to no wheat hedged in the first nine months of fiscal 2005.

In the third quarter of fiscal 2006, raw material costs included a net hedging loss of approximately \$223,000 compared to a net hedging loss of nearly 1.2 million in the third quarter of fiscal 2005. From time to time, we also use gasoline or ethanol futures to hedge fuel alcohol sales made under contracts with price terms based on gasoline futures. No gasoline or ethanol futures were used to hedge fuel alcohol sales during the third quarter of fiscal 2006 or the third quarter of fiscal 2005.

In the first nine months of fiscal 2006, raw material costs included a net hedging loss of approximately \$1.6 million compared to a net hedging loss of \$3.4 million in the first nine months of fiscal 2005. During the first nine months of fiscal 2006, we experienced a loss of \$24,000 on ethanol futures. No gasoline or ethanol futures were used to hedge fuel alcohol sales during the first nine months of fiscal 2005.

These hedge transactions are highly effective. Accordingly, all related losses were entirely offset by reduced raw materials costs.

### **Selling, General and Administrative Expenses**

In the third quarter of fiscal 2006, our selling, general and administrative expenses increased by approximately \$607,000 , or nearly 13 percent, above selling, general and administrative expenses in the third quarter of fiscal 2005. This increase was mainly due to increased costs associated with incentives along with expenses related to the Company's stock incentive plans, computer technology costs, including costs largely related to the development and implementation of our Enterprise Resource Planning System, outside labor and consulting fees, and miscellaneous. These increases were partially offset by a reduction in fees associated with professional services and lower research and development costs.

Selling, general and administrative expenses in the first nine months of fiscal 2006 rose by approximately \$2.0 million, or nearly 14 percent, compared to selling, general and administrative expenses in the first

nine months of fiscal 2005. The reasons for this increase were essentially the same as those cited above combined with bad debt charge-offs of approximately \$162,000 in the second quarter of fiscal 2006.

### **Other Income**

The decrease of \$88,000 in other income in the third quarter of fiscal 2006 compared to the third quarter of fiscal 2005 was principally attributable to changes in interest capitalized, as well as the effect of certain other non-recurring, non-operating revenue items. It is the Company's practice to credit other income for interest incurred that is capitalized.

### **Interest Expense**

For the three months ended March 31, 2006 interest expense remained relatively unchanged compared to the three months ended March 31, 2005.

Interest expense in the nine months ended March 31, 2006 increased compared to the nine months ended March 31, 2005 primarily due to the payment of a make whole premium in connection with the refinancing of our notes to the Principal Mutual Life Insurance Company and increases in borrowing rates.

### **Taxes and Inflation**

The consolidated effective income tax rate of the provision for income taxes for the third quarter of fiscal 2006 was 26.1 percent compared to 31.0 percent for the same period in fiscal 2005. This decrease was primarily attributable to the recognition of certain non-recurring Kansas State income tax credits in the third quarter. The consolidated effective income tax rate of the provision for income taxes for the first nine months of fiscal 2006 was 35.3 percent compared to 33.5 percent for the same period in fiscal 2005 primarily as a result of timing differences and applicable marginal income tax rates related to taxable income levels. The general effects of inflation during the quarter were minimal.

### **Net Income**

As the result of the foregoing factors, we experienced net income of \$2,083,000 in the third quarter of fiscal 2006 compared to net income of \$1,627,000 in the third quarter of fiscal 2005. Our net income for the first nine months of fiscal 2006 was \$6,632,000 compared to net income of \$3,272,000 for the first nine months of fiscal 2005.

## LIQUIDITY AND CAPITAL RESOURCES

The following table is presented as a measure of the Company's liquidity and financial condition:

	March 31, 2006	June 30, 2005
<b>(Dollars in Thousands)</b>		
Cash and cash equivalents	\$ 3,586	\$ 10,384
Working capital	38,842	40,628
Amounts available under lines of credit	14,000	20,000
Notes payable and long-term debt	23,074	21,490
Stockholders' equity	<u>126,739</u>	<u>120,527</u>

### Cash Flow.

Cash flow from operations increased by \$150,000 during the nine month period ended March 31, 2006 compared to the same period in fiscal 2005. This change in operating cash flow was a result of numerous factors. Operating cash flow was positively affected by an increase in net income of \$3.4 million related primarily to increased sales volume during the nine month period ended March 31, 2006 compared to the same period in 2005. Operating cash was also positively impacted by the effects of an increase in accounts payable and accrued expenses related to increased production activity as well as an increase in the accrual for income taxes payable. These factors, which led to an increase in operating cash flow, were partially offset by an \$8.2 million increase in inventories during the nine month period ended March 31, 2006. This increase in inventories was primarily related to increased alcohol inventories and increases in grain inventories (primarily corn) related to increased distillery production activity, compared to an increase of \$4.9 million in the same period in fiscal 2005 related to wheat and commodity wheat protein inventories. Operating cash flows were also reduced by an increase in accounts receivable related to higher sales for the nine months ended March 31, 2006 compared to a decrease in accounts receivable of \$2.3 million in the same period in fiscal 2005.

### Capital Expenditures.

During the year to date period ended March 31, 2006, we made \$13.7 million in capital expenditures, including expenditures with respect to a feed dryer in Atchison, Kansas and a molecular sieve in Pekin, Illinois. As of March 31, 2006, our Board of Directors had approved \$17.5 million in capital expenditures which we expect to make over the next twelve months, and of that amount, we had contracts to acquire capital assets of approximately \$6.3 million. On March 16, 2006, we announced the approval of plans for an \$11.1 million capital project that is expected to improve production efficiencies and fulfill air emission control requirements at our Pekin, Illinois production facility. We anticipate that we may require additional external financing for some of these capital expenditures. As of March 31, 2006, we have not determined the amount, type, or source of such financing.

### Stock Purchase and Sales.

During the year to date ended March 31, 2006, our employees exercised options on 154,810 shares of common stock and the company received proceeds of \$1,477,000. As of March 31, 2006 the Board has authorized the purchase of approximately 1,613,716 additional shares of common stock. No purchases were made under this authority during the quarter.

## **Contractual Obligations.**

As of March 31, 2006, we had outstanding long term debt of \$17.1 million compared to \$21.5 million at June 30, 2005.

We borrowed an additional \$7,000,000 from General Electric Capital Corporation (GECC) during the first quarter of fiscal year 2006 and paid the unsecured senior notes payable to The Principal Mutual Life Insurance Company of \$6,816,000. Our obligations to GECC are evidenced by a promissory note bearing interest at 5.92% per annum and payable in 60 consecutive monthly payments, with the first payment on November 1, 2005 being \$138,525, the next 58 payments being \$135,071 and the final payment on October 1, 2010 being the remaining amount of outstanding principal and interest. The note may be prepaid at any time in its entirety subject to the payment of a prepayment premium equal to 3% of the original principal amount if the note is prepaid prior to the first anniversary, declining to 1% if paid prior to the third anniversary and 0% thereafter.

We also entered a security agreement to secure the note. The security agreement grants a security interest in all of our equipment located or to be located at our KCIT facility in Kansas City, Kansas. Under the security agreement, we have agreed to indemnify the secured party against any claim arising in connection with the collateral.

Indebtedness under the note can be accelerated if any payment is not made within 10 days of its due date or if there is an event of default under the security agreement, certain acts of bankruptcy or insolvency, defaults by the Company under any other obligations and the merger or consolidation of the Company without the consent of GECC, which consent may not be unreasonably withheld.

At the time of the loan from GECC, our Company's other indebtedness included a note payable to GE Capital Public Finance ("GECPF"), an affiliate of GECC, which is also secured by equipment at our Kansas City, Kansas facility. In connection with the loan from GECC, we also entered into a cross-collateral and cross default agreement with GECC and GECPF in which we agreed, among other matters, that all collateral in which either creditor has a security interest will secure the payment of liabilities to both creditors.

As previously reported, we had an obligation to purchase \$6.2 million of our potato-based resistant starch product by August 2005 from Penford Corporation. At the request of Penford, this obligation was extended. As of December 31, 2005, we had completed our obligation to Penford. Although this will result in excess inventories of the product for a period of time, we anticipate that we will be able to sell those inventories by the end of December, 2006.

## **Financial Covenants**

In connection with our line of credit and capital lease agreements, we are required, among other things, to maintain certain financial ratios, including a current ratio (current assets to current liabilities) of 1.5 to 1, minimum consolidated tangible net worth (stockholders' equity less intangible assets) equal to the greater of (i) \$86 million or (ii) the sum of \$86 million plus 50 percent of consolidated net income since September 30, 2001, debt to tangible net worth not to exceed 2.5 to 1, and a fixed charge ratio (generally, the ratio of (x) the sum of (a) net income [adjusted to exclude gains or losses from the sale or other disposition of capital assets and other matters] plus (b) provision for taxes plus (c) fixed charges, to (y) fixed charges) for the period of the four consecutive fiscal quarters ended as of the measurement date of 1.5 to 1. In addition, we may not permit consolidated funded debt (generally, asset acquisition related debt plus capitalized lease obligations) to exceed 60 percent of total capitalization .

## **Line of Credit**

We have a \$20 million line of credit, of which \$14 million was available at March 31, 2006, for general corporate purposes. We amended the line of credit on September 9, 2005 so that it now extends to July 1, 2006. As of March 31, 2006, we had \$6.0 million outstanding borrowings under the line.

## **Working Capital**

Our working capital decreased by \$1.8 million from June 30, 2005 to March 31, 2006. This decrease was primarily due to a decrease of \$6.8 million in cash; a \$3.8 million net decrease in income taxes payable, increased borrowings on our line of credit and an increase in our liability for accrued expenses. These factors, which led to a decrease in our working capital, were partially offset by an increase of \$8.8 million in inventories, a \$0.3 million increase in our current deferred tax asset, a \$3.9 million increase in accounts receivable (net of an allowance of \$0.3 million at March 31, 2006) and a \$0.9 million decrease in the current portion of our long-term debt.

## **ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK**

The Company produces its products from wheat, corn and milo and, as such, is sensitive to changes in commodity prices. Grain futures and/or options are used as a hedge to protect against fluctuations in the market. The information regarding inventories and futures contracts at June 30, 2005, as presented in the annual report, is not significantly different from March 31, 2006.

## **ITEM 4. CONTROLS AND PROCEDURES.**

### **(a) Evaluation of disclosure controls and procedures.**

Our Chief Executive Officer and Chief Financial Officer, after evaluating the design and effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) or 15d-15(e)) as of the end of the period covered by this report (the "Evaluation Date"), have concluded that as of the Evaluation Date, the Company's disclosure controls and procedures were adequately designed and operating effectively to ensure that material information relating to the Company would be made known to them by others within the Company, particularly during the period in which this Form 10-Q Quarterly Report was being prepared.

### **(b) Changes in Internal Controls .**

There was no change in our internal control over financial reporting identified in connection with the evaluation required by paragraph (d) of Securities Exchange Act Rule 13a-15 or 15d-15 that occurred during our third fiscal quarter that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

## PART II — OTHER INFORMATION

### ITEM 1. LEGAL PROCEEDINGS.

Reference is made to Item 3. *Legal Proceedings* in the Company's Annual Report on Form 10-K for the year ended June 30, 2005 and to Part II, Item 1. Legal Proceedings in the Company's Quarterly Report on Form 10-Q for the quarters ended September 30, 2005 and December 31, 2005 for information regarding certain legal proceedings to which the Company or its Illinois subsidiary are subject.

One of the matters mentioned was *National Starch and Chemical Investment Holding Corporation, Penford Australia, Ltd. and Penford Holdings Pty v. Cargill, Inc. and MGP Ingredients, Inc.*, Civil Action 04-1442, U.S. District Court, District of Delaware. In March, Plaintiff's voluntarily withdrew their claims with respect to one of the two patents in suit, U.S. Patent No. 6,409,840.

Another matter referred to was a USEPA enforcement initiative relating to our Illinois facility. As reported in our 10-Q for the quarter ended September 30, 2005, we have entered the Consent Decree referred to in our Form 10-K for the year ended June 30, 2005 and agreed to pay the federal penalty of \$172,000 referred to therein. The Court has now approved the Consent Decree and we will pay the penalty on or before May 19, 2006.

Another matter referred to in our annual report on Form 10K and 10-Q for the quarter ended December 31, 2005 was an administrative proceeding brought in 1997 by the Illinois Attorney General on behalf of the Illinois Environmental Protection Agency relating to our Pekin facility. We have completed stack height extensions sought by the State and now have a construction permit for an additional Swiss Combi Dryer. We remain engaged in settlement discussions with the State regarding the amount of the penalty which it seeks. It's latest proposal was that we make either a \$500,000 lump sum payment of a \$600,000 payment over time.



**ITEM 2. UNREGISTERED SALES OF EQUITY SECURITIES AND USE OF PROCEEDS.**

As shown in the following table, the Company did not repurchase any shares of stock during the three months ended March 31, 2006.

<b>Period</b>	<b>Total Number Of Shares) or Units) Purchased</b>	<b>Average Price Paid per Share (or Unit)</b>	<b>Total Number of shares (or Units) Purchased as Part of Publicly Announced Plans or Programs</b>	<b>Maximum Number (or Approximate Dollar Value) of Shares (or Units (that May Yet Be Purchased Under the Plans or Programs</b>
January 1 – January 31, 2006	0	—		
February 1 – February 28, 2006	0			
March 1 – March 31, 2006	0			1,613,716(a)

- (a) On various dates, the Board of directors authorized the purchase of an aggregate of 6,000,000 shares of Common Stock of which 4,386,284 shares had been purchased as of March 31, 2006. This program was first announced on June 5, 1997. During the three months ended March 31, 2006, no shares were purchased under the program. The program has no expiration date.

**ITEM 6. EXHIBITS**

- 3.1 Amended and Restated Articles of Incorporation (incorporated by reference to Exhibit 3.1 of the Company's Quarterly Report on Form 10-Q for the quarter ended September 30, 2004.)
- 3.2 Bylaws of the Company (Incorporated by reference to Exhibit 3.2 of the Company's Current Report on Form 8-K filed March 16, 2005 (File Number 0-17196))
- \*10.1 Consent Decree relating to Registrant's Pekin facility entered on April 19, 2006
- \*10.2 Consent Agreement between the Registrant and the Kansas Department of Health and Environment dated January 11, 2006.
- \*15.1 Letter from independent public accountants pursuant to paragraph (d) of Rule 10-01 of Regulation S-X (incorporated by reference to Independent Accountants' Review Report at page 2 hereof).
- \*15.2 Letter from independent public accountants concerning the use of its Review Report in the Company's Registration Statement Nos. 333-51849 and 333-119860
- \*31.1 Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Acts of 2002
- \*31.2 Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
- \*32.1 Certification of Chief Executive Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
- \*32.2 Certification of Chief Financial Officer furnished pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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\* Filed herewith

## SIGNATURES

Pursuant to the requirements on the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

MGP INGREDIENTS, INC.

Date: May 10, 2006

By /s/ Ladd M. Seaberg  
Ladd M. Seaberg, President  
and Chief Executive Officer

Date: May 10, 2006

By /s/ Brian T. Cahill  
Brian T. Cahill, Vice President  
and Chief Financial Officer



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## CONSENT DECREE

WHEREAS, Plaintiff, the United States of America (hereinafter “Plaintiff” or “the United States”), on behalf of the United States Environmental Protection Agency (herein, “U.S. EPA”), has, simultaneously with lodging of this Consent Decree, filed a Complaint alleging that Defendant, MGP Ingredients of Illinois, Inc. (“MGP” or “Defendant”) commenced construction of major modifications to a major emitting facility in violation of the Prevention of Significant Deterioration (“PSD”) requirements at Part C of the Clean Air Act (the “Act”), 42 U.S.C. §§ 7470-7492, and the regulations promulgated thereunder at 40 C.F.R. § 52.21 (the “PSD Rules”);

WHEREAS, Plaintiff further alleged that Defendant commenced construction of major modifications to a major emitting facility and thereafter operated the facility without first obtaining the appropriate preconstruction permits and installing the appropriate air pollution control equipment required by 40 C.F.R. § 52.21 and the Illinois State Implementation Plan (“SIP”) approved pursuant to 42 U.S.C. § 7410;

WHEREAS, Plaintiff further alleged that potential air emissions from the Defendant’s facility were underestimated by MGP for purposes of determining the applicable permit requirements;

WHEREAS, the State of Illinois, (“Plaintiff-Intervenor” or “Illinois”), has, simultaneously with lodging of this Consent Decree, filed a Complaint in Intervention, alleging that MGP was and is in violation of PSD requirements and the Illinois SIP, by failing to obtain the appropriate pre-construction permits and state permits, and by failing to install appropriate pollution control technology, in violation of applicable federal and state laws, including Sections 9(b) and 9.1 of the Illinois Environmental Protection Act;

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WHEREAS, MGP has operated a grain processing facility in Pekin, Illinois (the Facility) since at least 1980;

WHEREAS, MGP has made various modifications to its grain processing facility, including changes in 1988 and 1993, pursuant to permits 88010011 and 93080045, respectively, issued by the Illinois Environmental Protection Agency ("IEPA"), which resulted in significant increases in its production capacity;

WHEREAS, on June 3, 2002, the U.S. EPA met with representatives of the ethanol plants in Illinois, including MGP, to discuss VOC testing and test results, VOC emissions, and related compliance issues;

WHEREAS, on April 2, 2003, MGP met with U.S. EPA and IEPA and agreed to negotiate with U.S. EPA and Illinois for the installation of controls on the Facility to address the alleged violations of the PSD requirements;

WHEREAS, MGP has worked cooperatively with U.S. EPA and IEPA regarding the alleged violations;

WHEREAS, the Defendant does not admit the facts or violations alleged in the Complaints;

WHEREAS, the United States and Plaintiff-Intervenor (collectively "Plaintiffs") and the Defendant have agreed that settlement of this action is in the best interest of the parties and in the public interest, and that entry of this Consent Decree without further litigation is the most appropriate means of resolving this matter; and

WHEREAS, Plaintiffs and the Defendant consent to entry of this Consent Decree without trial of any issues;

NOW, THEREFORE, without any admission of fact or law, and without any admission of the violations alleged in the Complaints, it is hereby ORDERED AND DECREED as follows:

### I. JURISDICTION AND VENUE

1. The Complaints state claims upon which relief can be granted against the Defendant under Sections 113 and 167 of the Act, 42 U.S.C. §§ 7413 and 7477, and 28 U.S.C. § 1355. This Court has jurisdiction of the subject matter herein and over the parties consenting hereto pursuant to 28 U.S.C. § 1345 and pursuant to Sections 113 and 167 of the Act, 42 U.S.C. §§ 7413 and 7477. Venue in this District is proper under Section 113(b) of the Act, 42 U.S.C. § 7413(b), and under 28 U.S.C. § 1391(b) and (c).

### II. APPLICABILITY

2. The provisions of this Consent Decree shall apply to and be binding upon the Plaintiffs and upon the Defendant as well as the Defendant's officers, employees, and those agents who are charged with implementing the terms of this Consent Decree, and the Defendant's successors and assigns. In the event Defendant proposes to sell or transfer the Facility before termination of this Consent Decree, it shall advise each proposed purchaser or successor-in-interest in writing of the existence of this Consent Decree, and shall send a copy of such written notification by certified mail, return receipt requested, to the U.S. EPA before such sale or transfer, if possible, but no later than the closing date of such sale or transfer. The Defendant shall provide a copy of the Consent Decree and the Control Technology Plan required in Paragraph 9 of this Consent Decree to the proposed purchaser or successor-in-interest. In the event the Defendant sells or otherwise assigns any of its right, title, or interest in its facility, prior to termination of the Consent Decree, the conveyance shall not release the Defendant from any obligation



imposed by this Consent Decree unless the party to whom the right, title or interest has been transferred agrees to enter into a written agreement with the U.S. EPA to fulfill the remaining obligations of this Consent Decree.

### III. FACTUAL BACKGROUND AND APPLICABLE DEFINITIONS

3. (a). MGP is a “person” as defined in Section 302(e) of the Act, 42 U.S.C. § 7602(e), and the federal and state regulations promulgated pursuant to the Act.

(b). MGP owns and operates a grain processing facility in Pekin, Illinois (the Facility), for the manufacture of various products from flour and grain, including fuel and beverage ethanol. The Plaintiffs allege that in the course of MGP’s manufacturing activities significant quantities of particulate matter (“PM”), particulate matter at or below 10 microns (“PM<sub>10</sub>”), carbon monoxide (“CO”), volatile organic compounds (“VOCs”), nitrogen oxides (“NOx”) and other pollutants are generated, including hazardous air pollutants (“HAPs”) listed under Section 112(b)(1), 42 U.S.C. § 7412(b)(1) of the Act. The primary sources of these emissions are the feed dryers, fermentation tanks, distillation units, and load-out of ethanol into trucks.

(c). Plaintiffs allege that the Facility is a “major emitting facility,” as defined by Section 169(1) of the Act, 42 U.S.C. § 7479(1), and the federal and state regulations promulgated pursuant to the Act.

(d). Unless otherwise defined herein, terms used in this Consent Decree shall have the meaning given to those terms in the Act, and the federal and state regulations promulgated pursuant to the Act.

### IV. COMPLIANCE PROGRAM SUMMARY

4. MGP shall implement a program of compliance at the Facility to meet the emission levels required under this Consent Decree for emissions of VOC, PM, PM<sub>10</sub>,

CO, and NOx. MGP's compliance program is summarized below in Paragraphs 5 through 10, and implemented through Paragraphs 11 through 14 and 17 of this Consent Decree.

5. MGP shall implement a program to control and minimize fugitive particulate matter emissions from the Facility as set forth in the approved Control Technology Plan required under Part V of this Consent Decree and which is Attachment 1 to this Consent Decree.

6. MGP shall demonstrate compliance with the required emission levels on a unit-by-unit basis as set forth in the approved Control Technology Plan.

7. MGP shall demonstrate compliance with the emission limits established under this Consent Decree by the use of performance testing, parametric monitoring, recordkeeping and reporting, where appropriate, as set forth in the approved Control Technology Plan.

8. MGP shall maintain records to demonstrate compliance with New Source Performance Standards ("NSPS"), Part 60, Subparts Kb and VV as provided in the listed NSPS standards.

9. In conformance with the time schedules specified in the approved Control Technology Plan, MGP shall complete and submit for IEPA action, appropriate application(s) to allow the construction of new and modified control equipment, and revise its operating permit for the Facility to include the compliance requirements of this Consent Decree.

10. Upon execution of the Consent Decree, MGP shall comply with the provisions of 40 C.F.R. Part 52 where such part is applicable to MGP's operations.

## V. COMPLIANCE PROGRAM REQUIREMENTS

### A. INSTALLATION OF CONTROLS AND APPLICABLE EMISSION LIMITS

11. MGP shall implement a plan for the installation of air pollution control technology (“Control Technology Plan”) to meet the following emission limits for the identified units in subparagraphs (a) through (e). MGP’s Control Technology Plan, which has been approved by Plaintiffs, is Attachment 1 to this Consent Decree:

- a. Feed Dryers : 95 percent reduction of VOC or emissions no higher than 10 parts per million (“PPM”) VOC, 90 percent reduction of CO emissions or emissions no higher than 100 PPM CO, and 0.01 grain/dry standard cubic foot for filterable PM.
- b. Fermentation Units : 97.5 percent reduction of VOC or if the inlet is less than 200 PPM VOC, then 20 PPM or lower VOC.
- c. Distillation Units : 97.5 percent reduction of VOC for scrubber 561 and 95% percent reduction of VOC for scrubber 501.
- d. Non-Dedicated Ethanol Loadout : 95 percent reduction of VOC or emissions no higher than 10 parts per million (“PPM”) VOC from the loading of transport vessels in which the interior has not been cleaned prior to use at MGP or are not dedicated to ethanol transport.
- e. New Source Performance Standards (NSPS) : Identify and implement applicable NSPS requirements codified at 40 C.F.R. Part 60. The following NSPS apply: NSPS Subpart Kb (Volatile Organic Liquid Storage Vessels); and NSPS subpart VV (Synthetic Organic Chemicals Manufacturing Industry Leak Detection, Monitoring and Repair Requirements).

12. MGP shall implement the approved Control Technology Plan in accordance with the schedule set forth in that plan. MGP’s approved Control Technology Plan is incorporated by reference herein and made directly enforceable by Plaintiffs under this Consent Decree.

B. PERMITTING AND MODIFICATIONS

13. Permitting : By no later than 180 days following the start-up of the last piece of control equipment required in the approved Control Technology Plan, MGP shall complete and submit for IEPA action an appropriate application to revise its operating permit to include all the compliance requirements of this Consent Decree and the emission limits and emission level reductions specified in Part V (“Installation of Controls and Applicable Emission Limits”) of this Consent Decree.

14. Upon execution of this Consent Decree, MGP shall comply with the provisions of 40 C.F.R. Part 52 where such part is applicable to MGP’s operations.

15. In determining whether a future modification will result in a significant net emissions increase, MGP cannot take credit for any emission reductions required by this Consent Decree and the approved Control Technology Plan for netting purposes as defined by 40 C.F.R. § 52.21(b)(3). VOC emission reductions up to 98 percent of the uncontrolled feed dryer emissions may not be used for any emissions offset, banking, selling or trading program. In addition, any emission reductions required under this Consent Decree and the applicable NSPS of VOC at units other than the feed dryers, and any emission reductions under this Consent Decree of PM, PM<sub>10</sub>, NO<sub>x</sub>, or CO may not be used for any emissions offset, banking, selling or trading program.

16. For purposes in establishing whether a future modification (after the implementation of the measures specified in the approved Control Technology Plan) will result in a significant net emissions increase, MGP shall use, as its baseline for establishing actual emissions, the average rate of the actual emissions of the pollutant after full implementation of, and demonstration of compliance with, the emission limits set by this Consent Decree and the provisions of the approved Control Technology Plan.

C. EMISSION LIMITS

17. Emission Limits for VOC, CO and PM : Beginning no later than 180 days following the start-up of each piece of control equipment required in its approved Control Technology Plan, whenever the associated emission unit(s) is/are in operation, MGP shall operate the control equipment within the operating parameters set forth in the approved Control Technology Plan and MGP's operating permit(s).

D. DEMONSTRATION OF COMPLIANCE

18. MGP shall demonstrate continuous compliance with the emission limits established under this Consent Decree by the use of parametric monitoring, recordkeeping and reporting, as set forth in the approved Control Technology Plan.

19. By no later than 180 days following the initial start-up of each piece of control equipment required in the approved Control Technology Plan, except the feed dryer, MGP shall demonstrate through emissions testing of each emissions unit, as specified in the approved Control Technology Plan, conducted in accordance with an IEPA and U.S. EPA approved test protocol, that it has met the required destruction efficiency and/or emission limit. If the approved Control Technology Plan indicates such testing is already complete, the test does not need to be repeated within the 180 day period. By no later than 180 days following the initial start-up, or within 60 days of achieving maximum production rate, whichever occurs first, of the feed dryers as required in the approved Control Technology Plan, MGP shall demonstrate through emissions testing of each feed dryer emissions unit modified or constructed pursuant to the approved Control Technology Plan, as specified in the approved Control Technology Plan, conducted in accordance with an IEPA and U.S. EPA approved test protocol, that it has met the required destruction efficiency and/or emission limit. MGP shall retest the

feed dryers modified or constructed pursuant to the approved Control Technology Plan for VOCs, CO, PM, and PM<sub>10</sub> no less than annually for the two years following the effective date of this Consent Decree, and after that, by permit requirement. MGP shall retest all other units in accordance with the provisions of its Title V permit that address performance testing.

20. MGP shall retain at the Facility all control technology performance criteria monitoring data and records required under the approved Control Technology Plan, and shall make any such data and records available to the Plaintiffs upon demand as soon as practicable.

E. RECORDKEEPING AND REPORTING REQUIREMENTS

21. Beginning with the first full calendar quarter following lodging of this Consent Decree, MGP shall submit written reports within 30 days following each calendar quarter to IEPA and U.S. EPA that itemize Consent Decree requirements and the approved Control Technology Plan requirements, the applicable deadlines, the dates the tasks were completed, unit emissions data and data to support MGP's compliance status with the terms of this Consent Decree. Reports shall be sent to the addresses identified in Paragraph 56 ("Notice").

22. MGP shall preserve and retain all records and documents in its possession or control, or which come into its possession or control, that are submitted to Plaintiff or Illinois as part of the reporting and compliance requirements under this Part, and all underlying data used and/or relied upon for those submittals, for a period of three years following the termination of this Consent Decree, unless other regulations require the records to be maintained longer.

23. All notices, reports or any other submissions from MGP shall contain the following certification and may be signed by an owner or operator of the company responsible for environmental management and compliance:

“I certify under penalty of law that I have personally examined the information submitted herein and that I have made a diligent inquiry of those individuals immediately responsible for obtaining the information and that to the best of my knowledge and belief, the information submitted herewith is true, accurate, and complete. I am aware that there are significant penalties for submitting false information, including the possibility of fine and imprisonment.”

#### VI. CIVIL PENALTY

24. Within thirty (30) calendar days of entry of this Consent Decree, the Defendant shall pay to the Plaintiffs a civil penalty pursuant to Section 113 of the Act, 42 U.S.C. § 7413, in the amount of One Hundred Seventy-One Thousand and Eight Hundred Dollars (\$171,800).

25. Of the total penalty, \$85,900, shall be paid to the United States by Electronic Funds Transfer (“EFT”) to the United States Department of Justice, in accordance with current EFT procedures, referencing the USAO File Number and DOJ Case Number 90-5-2-1-08180, and the civil action case name and case number of the District of Illinois. The costs of such EFT shall be MGP’s responsibility. Payment shall be made in accordance with instructions provided to MGP by the Financial Litigation Unit of the U.S. Attorney’s Office in the District of Illinois. Any funds received after 11:00 a.m. (EST) shall be credited on the next business day. MGP shall provide notice of payment, referencing the USAO File Number and DOJ Case Number 90-5-2-1-08180 and the civil action case name and case number, to the Department of Justice and to U.S. EPA, as provided in Paragraph 56 (“Notice”). The total remaining amount, \$85,900 in civil penalties, shall be paid to the Plaintiff-Intervenor the State of Illinois, in the form of

a certified check payable to the Illinois Environmental Protection Agency and delivered to:

Illinois Environmental Protection Agency  
Fiscal Services Section  
1021 North Grand Avenue East  
P.O. Box 19276  
Springfield, IL 62794-9276

Defendant's Federal Employer's Identification Number ("FEIN") is 48-0911013 and shall be set forth on each certified check or certified fund transfer.

26. The Defendant shall pay statutory interest on any over due civil penalty or stipulated penalty amount at the rate specified in 31 U.S.C. § 3717. Upon entry of this Consent Decree, this Consent Decree shall constitute an enforceable judgment for purposes of post-judgment collection in accordance with Rule 69 of the Federal Rules of Civil Procedure, the Federal Debt Collection Procedure Act, 28 U.S.C. § 3001-3308, and other applicable federal and state Authority. The Plaintiffs shall be deemed judgment creditors for purposes of collection of any unpaid amounts of the civil and stipulated penalties and interest.

27. No amount of the \$171,800 civil penalty to be paid by MGP shall be used to reduce its federal or state tax obligations.

#### VII. STIPULATED PENALTIES

28. The Defendant shall pay stipulated penalties in the amounts set forth below to the Plaintiffs, to be paid 50 percent to the United States and 50 percent to the State for the following:

(a) for each day of failure to meet a deadline, including any modified deadline agreed to in writing by the Plaintiffs, for installation of control technology set



forth in the Control Technology Plan or applying for a revised operating permit under Paragraph 13:

1st through 30th day after deadline	\$ 800
31st through 60th day after deadline	\$ 1,200
Beyond 60th day	\$ 2,000

(b). for failure to conduct a compliance test as required by Paragraph 19, per unit per day:

1st through 30th day after deadline	\$ 250
31st through 60th day after deadline	\$ 500
Beyond 60th day	\$ 1,000

(c). for failure to demonstrate compliance with emission limits set forth in the approved Control Technology Plan or emission limits set pursuant to Part V Section C (“Emission Limits”): \$500 per day per test for each pollutant.

(d). for each failure to submit reports as required by Part V Section E (“Recordkeeping and Reporting Requirements”) of this Consent Decree, per day per report or notice:

1st through 30th day after deadline	\$ 250
31st through 60th day after deadline	\$ 500
Beyond 60th day	\$ 1,000

(e). for failure to pay or escrow stipulated penalties, as specified in Paragraphs 32 and 33 of this section, \$500 per day per penalty demand.

(f). for failure to notify the Plaintiffs pursuant to Paragraph 2 of MGP’s sale or transfer of the Facility, \$250 per day.

29. MGP shall pay stipulated penalties upon written demand by the Plaintiffs no later than thirty (30) days after Defendant receives such demand. Stipulated penalties shall be paid to the Plaintiffs in the manner set forth in Part VI ("Civil Penalty") of this Consent Decree.

30. Should MGP dispute its obligation to pay part or all of a stipulated penalty, it may avoid the imposition of the stipulated penalty for failure to pay a penalty due to the Plaintiffs by placing the disputed amount demanded by the Plaintiffs, not to exceed \$20,000 for any given event or related series of events at any one plant, in a commercial escrow account pending resolution of the matter and by invoking the Dispute Resolution provisions of Part X within the time provided in Paragraph 29 for payment of stipulated penalties. If the dispute is thereafter resolved in Defendant's favor, the escrowed amount plus accrued interest shall be returned to the Defendant. Otherwise the Plaintiffs shall be entitled to the escrowed amount that was determined to be due by the Court plus the interest that has accrued on such amount, with the balance, if any, returned to the Defendant.

31. The Plaintiffs reserve the right to pursue any other remedies for violations of this Consent Decree to which they are entitled. The Plaintiffs will not seek stipulated penalties and civil or administrative penalties for the same violation of the Consent Decree. Either Plaintiff may, in its unreviewable discretion, waive all or any portion of a stipulated penalty due to it under this Consent Decree.

#### VIII. RIGHT OF ENTRY

32. Any authorized representative of the U.S. EPA or IEPA, or an appropriate federal or state agency, including independent contractors, upon presentation of proper credentials, shall have a right of entry upon the premises of MGP's facility identified

herein at Paragraph 3(b) at any reasonable time for the purpose of monitoring compliance with the provisions of this Consent Decree, including inspecting facility equipment, and inspecting and copying all records maintained by Defendant pursuant to this Consent Decree. Nothing in this Consent Decree shall limit the authority of U.S. EPA and IEPA to request and obtain records and information maintained by MGP, and conduct tests and inspections under Section 114 of the Act, 42 U.S.C. § 7414, and any other applicable state or federal law.

#### IX. FORCE MAJEURE

33. If any event occurs which causes or may cause a delay or impediment to performance in complying with any provision of this Consent Decree, Defendant shall notify the Plaintiffs in writing as soon as practicable, but in any event within twenty (20) business days of when Defendant first knew of the event or should have known of the event by the exercise of due diligence. In this notice Defendant shall specifically reference this Paragraph of this Consent Decree and describe the anticipated length of time the delay may persist, the cause or causes of the delay, and the measures taken or to be taken by Defendant to prevent or minimize the delay and the schedule by which those measures will be implemented. Defendant shall adopt all reasonable measures to avoid or minimize such delays.

34. Failure by Defendant to provide notice to Plaintiffs of an event which causes or may cause a delay or impediment to performance shall render this Part IX voidable by the Plaintiffs as to the specific event for which the Defendant has failed to comply with such notice requirement, and, if voided, is of no effect as to the particular event involved.

35. Plaintiffs shall notify the Defendant in writing regarding the Defendant's claim of a delay or impediment to performance as soon as practicable, but in any event within thirty (30) days of receipt of the Force Majeure notice provided under Paragraph 33. If the Plaintiffs agree that the delay or impediment to performance has been or will be caused by circumstances beyond the control of the Defendant, including any entity controlled by the Defendant, and that the Defendant could not have prevented the delay by the exercise of due diligence, the parties shall stipulate to an extension of the required deadline(s) for all requirement(s) affected by the delay by a period equivalent to the delay actually caused by such circumstances. The Defendant shall not be liable for stipulated penalties for the period of any such delay.

36. If the Plaintiffs do not accept the Defendant's claim that a delay or impediment to performance is caused by a force majeure event, to avoid payment of stipulated penalties, the Defendant must submit the matter to this Court for resolution within twenty (20) business days after receiving notice of the Plaintiffs' position, by filing a petition for determination with this Court. Once the Defendant has submitted this matter to this Court, the Plaintiffs shall have twenty (20) business days to file a response or responses to said petition. If the Defendant submits the matter to this Court for resolution and the Court determines that the delay or impediment to performance has been or will be caused by circumstances beyond the control of the Defendant, including any entity controlled by the Defendant, and that the Defendant could not have prevented the delay by the exercise of due diligence, the Defendant shall be excused as to that event(s) and delay (including stipulated penalties), for a period of time equivalent to the delay caused by such circumstances.

37. The Defendant shall bear the burden of proving that any delay of any requirement(s) of this Consent Decree was caused by or will be caused by circumstances beyond its control, including any entity controlled by it, and that the Defendant could not have prevented the delay by the exercise of due diligence. The Defendant shall also bear the burden of proving the duration and extent of any delay(s) attributable to such circumstances. An extension of one compliance date based on a particular event may, but does not necessarily, result in an extension of a subsequent compliance date or dates.

38. Unanticipated or increased costs or expenses associated with the performance of the Defendant's obligations under this Consent Decree shall not constitute circumstances beyond the control of the Defendant, or serve as a basis for an extension of time under this Part. However, failure of a permitting authority to issue a necessary permit in a timely fashion is an event of Force Majeure where the Defendant has taken all steps available to it to obtain the necessary permit including but not limited to:

- (a). submitting a timely and complete permit application;
- (b). responding to requests for additional information by the permitting authority in a timely fashion; and
- (c). prosecuting appeals of any disputed terms and conditions imposed by the permitting authority in an expeditious fashion.

39. Notwithstanding any other provision of this Consent Decree, this Court shall not draw any inferences nor establish any presumptions adverse to either party as a result of Defendant delivering a notice of Force Majeure or the parties' inability to reach agreement.

40. As part of the resolution of any matter submitted to this Court under this Part IX, the parties by agreement, or this Court, by order, may in appropriate circumstances extend or modify the schedule for completion of work under this Consent Decree to account for the delay in the work that occurred as a result of any delay or impediment to performance agreed to by the Plaintiffs or approved by this Court. Defendant shall be liable for stipulated penalties for its failure thereafter to complete the work in accordance with the extended or modified schedule.

#### X. DISPUTE RESOLUTION

41. The dispute resolution procedure provided by this Part X shall be the exclusive means of resolving any disputes arising under this Consent Decree, including but not limited to emission limits established in Part V Section C (“Emission Limits”), except as otherwise provided in Part IX regarding Force Majeure.

42. Any party may invoke the dispute resolution procedure required herein by giving written notice to the other parties advising of a dispute pursuant to this Part X. The notice shall describe the nature of the dispute, and shall state the noticing party’s position with regard to such dispute. The party receiving such a notice shall acknowledge receipt of the notice and the parties shall expeditiously schedule a meeting to discuss the dispute informally not later than fourteen (14) days from the receipt of such notice.

43. Disputes submitted to dispute resolution shall, in the first instance, be the subject of informal negotiations between the parties. Such period of informal negotiations shall not extend beyond thirty (30) calendar days from the date of the first meeting between representatives of the Plaintiffs and the Defendant, unless the parties’ representatives agree to shorten or extend this period.

44. In the event that the parties are unable to reach agreement during such informal negotiation period, the Plaintiffs shall provide the Defendant with a written summary of their position regarding the dispute. The position advanced by the Plaintiffs shall be considered binding unless, within thirty (30) calendar days of the Defendant's receipt of the written summary of the Plaintiffs position, the Defendant files with this Court a petition which describes the nature of the dispute, and includes a statement of the Defendant's position and any supporting data, analysis, and/or documentation relied on by the Defendant. The Plaintiffs shall respond to the petition within thirty (30) calendar days of filing.

45. Where the nature of the dispute is such that a more timely resolution of the issue is required, the time periods set out in this Part X may be shortened upon motion of one of the parties to the dispute.

46. Notwithstanding any other provision of this Consent Decree, in dispute resolution, this Court shall not draw any inferences nor establish any presumptions adverse to either party as a result of invocation of this Part X or the parties' inability to reach agreement. The final position of the Plaintiffs shall be upheld by the Court if supported by substantial evidence in the record as identified by all the Parties.

47. As part of the resolution of any dispute submitted to dispute resolution, the parties, by agreement, or this Court, by order, may, in appropriate circumstances, extend or modify the schedule for completion of work under this Consent Decree to account for the delay in the work that occurred as a result of dispute resolution. Defendant shall be liable for stipulated penalties for its failure thereafter to complete the work in accordance with the extended or modified schedule.

## XI. GENERAL PROVISIONS

48. Effect of Settlement. This Consent Decree is not a permit; compliance with its terms does not guarantee compliance with any applicable federal, state or local laws or regulations. To the extent that the terms of this Consent Decree conflict with the terms of any air quality permit, the terms of this Consent Decree shall control during the effective period of the Consent Decree.

49. Resolution of Claims. Satisfaction of all of the requirements of this Consent Decree constitutes full settlement of and shall resolve all past civil and administrative liability of the Defendant to the Plaintiffs for the violations alleged in the United States' and Plaintiff-Intervenor's Complaints and occurring through the lodging date of this Consent Decree.

50. Reservation of Specific Claims. The release of liability granted by this Consent Decree under Paragraph 49 above specifically excludes pending claims in the State of Illinois regarding alleged violations at the Pekin facility which are addressed by Illinois administrative case number PCB 97-179, and Plaintiff-Intervenor expressly reserves its rights to proceed with those claims.

51. Other Laws. Except as specifically provided by this Consent Decree, nothing in this Consent Decree shall relieve Defendant of its obligation to comply with all applicable federal, state and local laws and regulations. Subject to Paragraphs 31, 49 and 50, nothing contained in this Consent Decree shall be construed to prevent or limit the United States' or Illinois' rights to obtain penalties or injunctive relief under the Act or other federal, state or local statutes or regulations, including but not limited to, Section 303 of the Act, 42 U.S.C. § 7603.



52. Third Parties. Except as otherwise provided by law, this Consent Decree does not limit, enlarge or affect the rights of any party to this Consent Decree as against any third parties. Nothing in this Consent Decree should be construed to create any rights, or grant any cause of action, to any person not a party to this Consent Decree.

53. Costs. Each party to this Consent Decree shall bear its own costs and attorneys' fees through the date of entry of this Consent Decree.

54. Public Documents. All information and documents submitted by the Defendant to the Plaintiffs pursuant to this Consent Decree shall be subject to public inspection, unless, identified at the time of submission and properly supported by the Defendant in response to any challenge, as subject to legal privileges or as business confidential by the Defendant in accordance with 40 C.F.R. Part 2 and applicable state law.

55. Public Comments - Federal Approval. The parties agree and acknowledge that final approval by the United States and entry of this Consent Decree are subject to the requirements of 28 C.F.R. § 50.7, which provides for notice of the lodging of this Consent Decree in the Federal Register, an opportunity for public comment, and consideration of any comments. The United States reserves the right to withdraw or withhold consent if the comments regarding this Consent Decree disclose facts or considerations which indicate that this Consent Decree is inappropriate, improper or inadequate. The Defendant and the Plaintiff-Intervenor consent to the entry of this Consent Decree.

56. Notice. Unless otherwise provided herein, notifications to or communications with the United States, U.S. EPA, IEPA or the Defendant shall be

deemed submitted on the date they are postmarked and sent either by overnight receipt mail service or by certified or registered mail, return receipt requested. Except as otherwise provided herein, when written notification to or communication with the United States, U.S. EPA, IEPA or the Defendant is required by the terms of this Consent Decree, it shall be addressed as follows:

As to the United States:

Chief  
Environmental Enforcement Section  
Environment and Natural Resources Division  
U.S. Department of Justice  
P.O. Box 7611, Ben Franklin Station  
Washington, DC 20044-7611

As to the U.S. EPA:

Director, Air Enforcement Division  
U.S. Environmental Protection Agency  
Ariel Rios Building  
1200 Pennsylvania Avenue, N.W.  
Mail Code 2242-A  
Washington, DC 20004

Region 5:

Compliance Tracker  
Air Enforcement Branch, AE-17J  
U.S. EPA, Region 5  
77 W. Jackson Blvd.  
Chicago, IL 60604

As to MGP Ingredients of Illinois, Inc.:

Robert Taphorn  
MGP Ingredients of Illinois, Inc.  
1301 S. Front Street  
Pekin, IL 61555

and

(Counsel for MGP)

Amy L. Wachs  
Husch & Eppenberger, L.L.C.  
190 Carondelet Plaza  
Suite 600  
St. Louis, MO 63105

As to Plaintiff-Intervenor the State of Illinois:

Julie K. Armitage  
Illinois Environmental Protection Agency  
Compliance and Enforcement Section, Manager  
1021 North Grand Avenue East  
Springfield, Illinois 62794

and

(Illinois Attorney General's Office)

Jane McBride  
Assistant Attorney General  
Office of the Attorney General  
500 South Second Street  
Springfield, IL 62706

57. Change of Notice Recipient. Any party may change either the notice recipient or the address for providing notices to it by serving all other parties with a notice setting forth such new notice recipient or address.

58. Modification. There shall be no modification of this Consent Decree without written agreement of all the parties. There shall be no material modification of this Consent Decree without the written agreement of the parties and by Order of the Court. Prior to complete termination of the requirements of this Consent Decree pursuant to Paragraph 60, the parties may, upon motion to the Court, seek to terminate provisions of this Consent Decree.

59. Continuing Jurisdiction. The Court retains jurisdiction of this case after entry of this Consent Decree to enforce compliance with the terms and conditions of this

Consent Decree and to take any action necessary or appropriate for its interpretation, construction, execution, or modification.

## XII. TERMINATION

60. This Consent Decree shall be subject to termination upon motion by any party after the Defendant has satisfied all requirements of this Consent Decree and has operated the control technologies identified in the approved Control Technology Plan in compliance with the emission limits established under this Consent Decree for 12 months. At such time, if the Defendant believes that it is in compliance with the requirements of this Consent Decree, and has paid the civil penalty and any stipulated penalties required by this Consent Decree, then the Defendant shall so certify to the Plaintiffs, and unless the Plaintiffs object in writing with specific reasons within forty-five (45) days of receipt of the certification, the Court shall order that this Consent Decree be terminated on Defendant's motion. If the United States or Illinois objects to the Defendant's certification, then the matter shall be submitted for resolution under Part X ("Dispute Resolution") of this Consent Decree. In such case, the Defendant shall bear the burden of proving that this Consent Decree should be terminated.

So ordered in accordance with the foregoing this 19th day of April, 200[6].

/s/ Michael M. Mihm

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United States District Court Judge  
Central District of Illinois

FOR PLAINTIFF, UNITED STATES OF AMERICA:

**s/: Sue Ellen Wooldridge**

Sue Ellen Wooldridge  
Assistant Attorney General  
Environment and Natural Resources Division  
U.S. Department of Justice  
10<sup>th</sup> & Pennsylvania Avenue, N.W.  
Washington, DC 20530

Date **December 5, 2005**

**s/: William D. Brighton**

William D. Brighton  
Assistant Chief  
Environment and Natural Resources Division  
U.S. Department of Justice  
1425 New York Avenue, N.W.  
Washington, DC 20005

Date **December 14, 2005**

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U.S. and the State of Illinois v. MGP, Ingredients of Illinois, Inc.

RODGER A. HEATON  
United States Attorney  
Central District of Illinois

s/: GERARD A. BROST  
BY: Gerard A. Brost  
Assistant U.S. Attorney  
Peoria Division  
One Technology Plaza  
211 Fulton Street, Suite 400  
Peoria, Illinois 61602

Date **December 21, 2005**

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U.S. and the State of Illinois v. MGP, Ingredients of Illinois, Inc.

FOR U.S. ENVIRONMENTAL PROTECTION AGENCY:

**s/: Granta Y. Nakayama**

Granta Y. Nakayama

Assistant Administrator

Office of Enforcement and Compliance Assurance

U.S. Environmental Protection Agency

Ariel Rios Building

1200 Pennsylvania Avenue, N.W.

Washington, DC 20460

Date **December 14, 2005**

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FOR THE PLAINTIFF-INTERVENOR, THE STATE OF ILLINOIS

**s/: Thomas Davis**

Illinois Attorney General's Office  
Thomas Davis, Chief  
Environmental Bureau  
Office of the Attorney General  
500 South Second Street  
Springfield, IL 62706

Date **September 27, 2005**

**s/: William Ingersoll**

William Ingersoll  
Illinois Environmental Protection Agency  
Chief Legal Counsel  
1021 North Grand Avenue East  
Springfield, Illinois 62794

Date **October 19, 2005**

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U.S. and the State of Illinois v. MGP, Ingredients of Illinois, Inc.

FOR DEFENDANT, MGP INGREDIENTS OF ILLINOIS, INC.:

**s/: David L. Wilbur**

David L. Wilbur,

General Manager

MGP Ingredients of Illinois, Inc.

Date **September 22, 2005**

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# **CONTROL TECHNOLOGY PLAN**

**June 30, 2005**

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## 1.0 INTRODUCTION.

MGP Ingredients of Illinois, Inc. has entered into a consent decree with the United States and the State of Illinois that requires MGP Ingredients of Illinois, Inc. to implement a program of compliance at the corn dry mill ethanol plant it operates in Pekin, Illinois. MGP Ingredients of Illinois, Inc. prepared and submitted this Control Technology Plan (CTP) as an integral part of the consent decree. This CTP fulfills the requirements of the consent decree and has been reviewed and approved by the US Environmental Protection Agency (USEPA) and the Illinois Environmental Protection Agency (IEPA) as part of the consent decree.

The CTP includes the following items:

- Identification of all units to be controlled;
- Engineering design criteria for all the controls capable of meeting the emission levels required by Part V of the Consent Decree;
- Emission limits and controlled outlet concentrations for each pollutant as appropriate;
- A schedule for expedited installation with specific milestones applicable on a unit-by-unit basis;
- Monitoring parameters for all control equipment and parameter ranges;
- Identification of all units to be emission tested under Paragraph 11 of the Consent Decree and schedule for initial tests and retest;
- The test methods that will be used to demonstrate compliance with the emissions levels set forth by the Consent Decree;
- Program for minimization of fugitive dust emissions from facility operations.

**2.0 EMISSION UNITS REQUIRING POLLUTION CONTROL EQUIPMENT**

The following emission units, fugitive sources, and control equipment have been designated as affected units in the consent decree and have emission limits requiring pollution control technology.

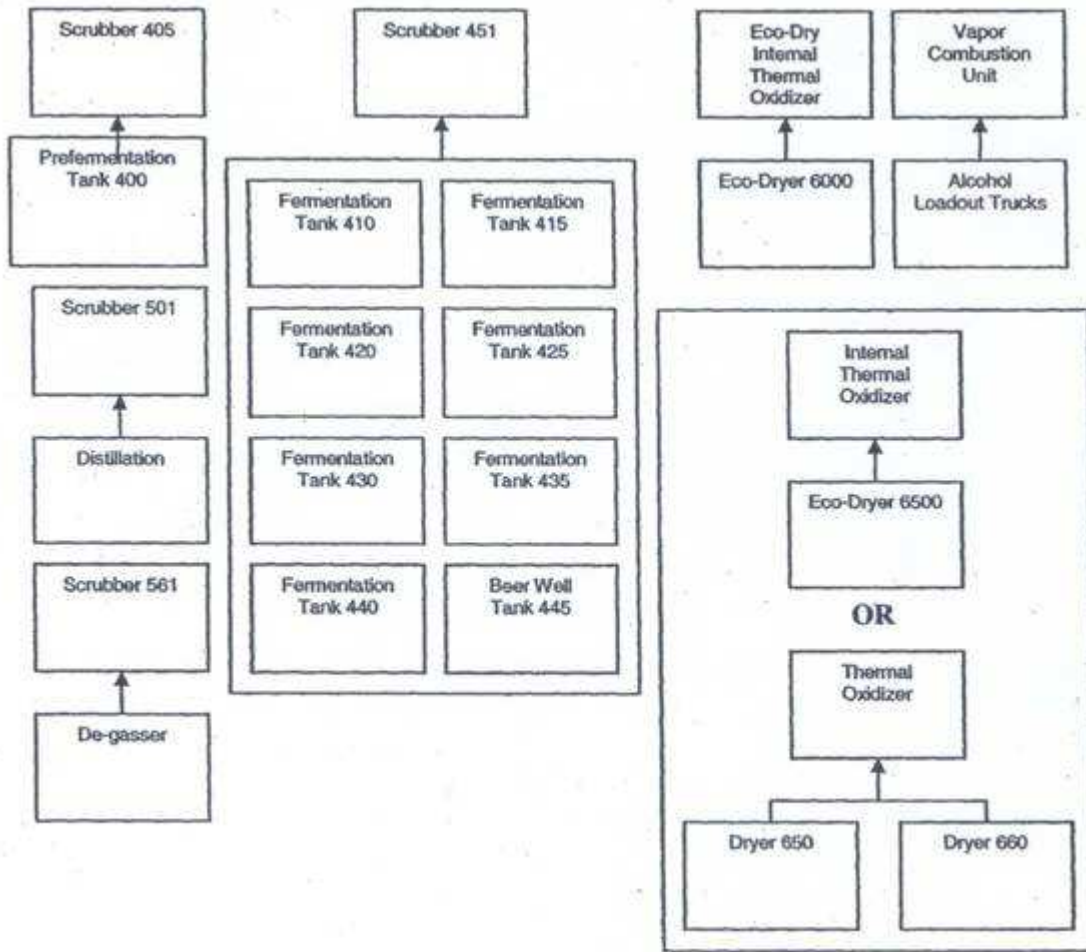
<b>Unit Description</b>	<b>Control Equipment Description</b>
Prefermentation Tank #400	Fermentation Scrubber #405
Fermentation Tank #410	
Fermentation Tank #420	
Fermentation Tank #430	
Fermentation Tank #415	Fermentation Scrubber #451
Fermentation Tank #425	
Fermentation Tank #435	
Fermentation Tank #440	
Beerwell Tank #445	
Distillation	Distillation Scrubber #501
De-Gasser	Degasser Scrubber #561
DDGS Dryer #6000	Internal Thermal Oxidizer
DDGS Dryers #660	Thermal Oxidizer/Replace dryer(s) with add-on thermal oxidizer or with dryer equipped with an internal thermal oxidizer such as the Swiss Control Eco-Dry System
DDGS Dryers #650	
Ethanol Truck Loadout	Vapor Combustion Unit
Rail & Barge Loadout	Dedicated Fleet
Valve, Flange, and Seal Fugitive Emissions	LDAR Program under 40 CFR 60 Subpart VV

### 3.0 ENGINEERING DESIGN CRITERIA FOR POLLUTION CONTROL EQUIPMENT

After identifying the affected units that require installation of air pollution control technology, MGP Ingredients conducted a design and engineering review of each unit to select the pollution control technology that would achieve the emission level reductions identified in the consent decree.

<u>Process Description</u>	<u>Control Device Description</u>	<u>Operating Parameters</u>
Prefermentation	Packed Bed Scrubber — Scrubber #405 (existing)	Water flow rate > 30 GPM
Fermentation	Packed Bed Scrubber — Scrubber #451 (existing)	Water flow rate > 45 GPM
Distillation	Packed Bed Scrubber — Scrubber #501 (existing)	Water flow rate $\geq$ 3 GPM
Degasser	Packed Bed Scrubber — Scrubber #561 (existing)	Water flow rate $\geq$ 17 GPM
DDGS Dryer #6000	Internal Thermal Oxidizer (existing)	$\geq$ 1500 ° F
DDGS Dryers #650 & #660	Thermal Oxidizer(s) or New dryer(s) with thermal oxidizer(s) or internal thermal oxidizer (proposed)	$\geq$ 1500 ° F
Dedicated Fleet	Submerged Loading (existing)	Not Applicable
Ethanol Truck Loadout	Vapor Combustion Unit (existing)	Presence of Pilot Flame

The following flow diagram presents the affected units and associated control technology as determined by the results of engineering design criteria.



#### **4.0 PROPOSED EMISSION LIMITS FROM POLLUTION CONTROL EQUIPMENT**

The consent decree specifies the emission reductions or emission limits allowable for each affected unit. After evaluating the pollution control technology engineering and design, MGP Ingredients of Illinois, Inc. agrees to meet the following emission limits.

Unless otherwise stated, all controlled emission limitations apply at all times except during periods when the process equipment is not operating or if the construction or operating permit contains alternative limits for startup, shutdowns or malfunction, at which point the permit provisions shall prevail.

Any deviations from the requirements of section 4.0, 4.1 and/or 4.2 shall be reported in quarterly reports and as required by state or federal regulations.



<b>Process Description</b>	<b>Control Device Description</b>	<b>Pollutant</b>	<b>Emission Rate</b>
Prefermentation	Packed Bed Scrubber #405	VOC	95% reduction or not to exceed 20 ppm if inlet concentration is less than 200 ppm
Fermentation	Packed Bed Scrubber #451	VOC	97.5% reduction
Distillation	Packed Bed Scrubber #501	VOC	95% reduction or not to exceed 20 ppm if inlet concentration is less than 200 ppm
Degasser	Packed Bed Scrubber #561	VOC	95% reduction or not to exceed 20 ppm if inlet concentration is less than 200 ppm
DDGS Dryer #6000	Internal Thermal Oxidizer / Replacement Dryer(s) with Internal Thermal Oxidizer or Thermal Oxidizer*	CO	90% reduction or emissions no higher than 100 PPM
DDGS Dryers #650 & #660		PM	0.01 gr/dscf
		VOC	95% reduction of VOC or emissions no higher than 10 ppm
		NO <sub>x</sub>	0.15lb/mmbtu*
Ethanol Truck Loadout	Vapor Combustion Unit	VOC	95% reduction of VOC

\*The NO<sub>x</sub> limit of 0.15 lb/mmbtu applies to a feed dryer with an internal thermal oxidizer, as present in the DDGS Dryer #6000 and proposed by MGP to replace existing DDGS. Dryers #650 and #660. If MGP decides to replace DDGS Dryer #650 and #660 with new dryer(s) equipped with add-on thermal oxidation (or retrofit add-on thermal oxidizers to the existing dryers), the NO<sub>x</sub> limit for the dryer burner is 0.04 lb/mmbtu. For this purpose, compliance may be determined for the dryer without the oxidizer, i.e., NO<sub>x</sub> emissions in the ductwork prior to the oxidizer and only the heat input to the dryer burner, or at MGP's option, for the dryer as a whole, i.e., NO<sub>x</sub> at the stack and the actual heat input to the burners in the dryer and the thermal oxidizer.

#### **4.1 Alternate Operating Scenarios**

The facility may continue to operate and produce wet cake during periods of dryer control device downtime.

If thermal oxidizer for existing dryers DDGS Dryer 660 and DDGS Dryer 650 is installed there will be no more than 50 hours per year for bake-out of the Regenerative Thermal Oxidizer (RTO) with each individual bake-out lasting no longer than 12 hours while the dryers are in operation. Off-line RTO regeneration while the associated dryers are shutdown is not included in these operating limitations. MGP may petition USEPA and IEPA to adjust these operating limitations for a specific RTO based on operating experience with the RTO and the dryers on which the RTO is installed. Changes to these regeneration hour limitations shall be considered non-material modifications under paragraph 57 of the Consent Decree, provided MGP obtains written approval of the change(s) from USEPA and IEPA.

## **4.2 Interim Operating Scenario**

If MGP continues to pursue installation of a replacement dryer, Dryers 650 and D660 will continue to operate during construction of the new dryer. Once the new dryer is installed Dryers D650 and D660 will continue to operate as standby dryers for a period of one (1) year from the official start up date of the new dryer. At this time, MGP will physically disable D650 and D660 by removing the fuel and preventing wet feed supply to the dryers.

MGP will operate Dryers D650 and D660 in their present configuration to minimize PM emissions to the greatest extent reasonably possible.

MGP will not operate D650 and D660 in conjunction with the new dryer and the existing Swiss-combi dryer to facilitate increased feed production by the plant beyond 851 tons per day. Total feed production by the plant during the day when existing feed dryers D650 and D660 operate shall not exceed 851 tons per day. MGP will maintain daily records documenting compliance with the above mentioned limit.

**5.0 POLLUTION CONTROL EQUIPMENT INSTALLATION SCHEDULE**

The following table presents the schedule for procurement, installation and startup of new control equipment specified by this plan for DDGS Dryers D650 and D660. MGP’s preferred approach for these dryers, which it is currently pursuing, is installation of a replacement feed dryer with an internal thermal oxidizer. The schedule also addresses other approaches to the dryers, i.e., replacement of dryers with new dryers equipped with add-on thermal oxidizers or retrofit of thermal oxidizers to the existing dryers.

	<b>Replacement Dryer with Internal Thermal Oxidizer or Thermal Oxidizer</b>
Apply for Construction Permit	June 1 <sup>st</sup> 2004
Construction Permit Issuance	Actual Date (a)
Order Equipment	Permit Date plus 90 days (b)
Commence On-Site Construction	Permit Date plus 12 months (b)
Startup	Permit Date plus 23 months (b)

a). Actual date of issuance of the Construction Permit, or the date the permit becomes effective, if the permit is not effective when issued. MGP shall take reasonable efforts to support the expeditious issuance of the Construction Permit by the Illinois EPA. The expected date for this to occur is July 15, 2005.

b). Specific dates will be set based on actual date a construction permit is issued or becomes effective, if the permit is not effective when issued. The project is expected to be complete by December 31, 2007, or later, depending on the issuance date of the construction permit.

## 6.0 PROPOSED MONITORING PARAMETERS FOR POLLUTION CONTROL DEVICES

Unit/Control Description	Parameter Monitored	Operating Range	Monitoring Frequency
Prefermentation/ Scrubber #405	Water flow rate	≥ 30 GPM	Daily when operating
Fermentation/ Scrubber #451	Water flow rate	≥ 45 GPM	Daily when operating
Distillation/ Scrubber #501	Water flow rate	≥ 3 GPM	Daily when operating
Degasser/ Scrubber #561	Water flow rate	≥ 17 GPM	Daily when operating
DDGS Dryer #6000/ Internal Thermal Oxidizer	Temperature Combustion Chamber	≥ 1500 ° F	Daily when operating
DDGS Dryer #650 & #660/Thermal Oxidizer or Eco-Dry System with Internal Thermal Oxidizer	Temperature Combustion Chamber	≥ 1500 ° F	Daily when operating
Ethanol Truck Loadout/Vapor Combustion Unit	Flame Present	Per 40 CFR 60.18(f)(2)	Daily when operating
Valve, Flange, and Seal Fugitive Emissions	As described in 40 CFR 60 Subpart VV: Standards of Performance for Equipment Leaks of VOC in the Synthetic Organic Chemicals Manufacturing industry	As described in 40 CFR 60 Subpart VV: Standards of Performance for Equipment Leaks of VOC in the Synthetic Organic Chemicals Manufacturing industry	As described in 40 CFR 60 Subpart VV: Standards of Performance for Equipment Leaks of VOC in the Synthetic Organic Chemicals Manufacturing industry

**7.0 POLLUTION CONTROL DEVICE PERFORMANCE TEST SCHEDULE AND TEST METHODS USED**

The following schedule and methods will be used to demonstrate initial compliance with the emission limits contained in Section 4.0 of this Control Technology Plan.

<b>Process Description</b>	<b>Unit/Control Device Description</b>	<b>Proposed Performance Test Date</b>	<b>Pollutants</b>	<b>Proposed Methods Used</b>
Replacement Dryer with Internal Thermal Oxidizer or DDGS Dryers #650 & #660	Internal Thermal Oxidizer or Thermal Oxidizer	Performance tests 60 days after full production or no later than 180 days after initial start-up of thermal oxidizer or replacement dryer with internal thermal oxidizer	Total VOC	Methods 1, 2, 3A, 4, 18, 25, or 25A if less than 50 ppm
			PM/PM <sub>10</sub>	Methods 1, 2, 3A, 4 5
			CO	Methods 1, 2, 3A or 3B, 4, 10
			HAPS	Methods 1, 2, 3A, 4, 18, for specified HAPS
			NO <sub>x</sub>	Methods 1, 2, 3A or 3B, 4, 7E

All testing for the Prefermentation, Fermentation, Distillation and Vapor Combustion processes are complete. No testing is required for the Degasser at this time. In the event at some future date testing is required for one of these units, the parties agree that the following methods shall be used for that future testing.

<b>Process Description</b>	<b>Unit/Control Device Description</b>	<b>Pollutant</b>	<b>Proposed Methods Used</b>
Prefermentation	Scrubber #405	Total VOC	Method 1, 2, 3A, 4, 18, 25, or 25A if less than 50 ppm
Fermentation	Scrubber #451	Total VOC	Method 1, 2, 3A, 4, 18, 25, or 25A if less than 50 ppm
Distillation	Scrubber #501	Total VOC	Method 1, 2, 3A, 4, 18, 25, or 25A if less than 50 ppm
Degasser	Scrubber #561	Total VOC	Method 1, 2, 3A, 4, 18, 25, or 25A if less than 50 ppm
Vapor Combustion Unit	Flare	Total VOC	Proper Operation Per 40 CFR 60.18 as applicable

## **8.0 FUGITIVE DUST EMISSION CONTROL PROGRAM**

Asphalt paving on specified unpaved roadways as shown on attached site plan will be completed by December 15, 2005. Paved and unpaved roadways are to be inspected on a weekly basis and observations conducted for emissions of fugitive dust and inspections recorded. Paved roads are to be swept, flushed or otherwise treated to minimize fugitive dust as needed based on inspections. Water and/or dust suppressant agent is to be applied to unpaved roadways to minimize fugitive dust as needed based on inspections.



[SITE MAP]

[ 9.0 PAVED ROADWAY SITE PLAN ]

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**BEFORE THE KANSAS DEPARTMENT OF HEALTH AND ENVIRONMENT**

IN THE MATTER OF:  
MGP Ingredients, Inc.  
1300 Main Street  
P.O. Box 130  
Atchison, Kansas 66002-0130

Case No. 04-E-0034

Source ID No. 0050002

**CONSENT AGREEMENT AND FINAL ORDER OF THE SECRETARY**

The parties hereto, the Kansas Department of Health and Environment (KDHE) and MGP Ingredients, Inc. (MGP), having agreed that settlement of this matter is in the best interests of the parties and the public health and the environment, hereby represent and state as follows:

**JURISDICTION**

1. The KDHE is a duly authorized agency of the State of Kansas created by an act of the legislature.
2. The Secretary of the KDHE (Secretary) has general jurisdiction over matters involving the environment and the public health and safety of the people of Kansas, K.S.A. 65-101 et seq., including general jurisdiction of matters involving air quality pursuant to the Kansas air quality act, K.S.A. 65-3001 et seq.
3. MGP is a Kansas corporation licensed to do business in the state of Kansas in accordance with Kansas laws and is subject to K.S.A. 65-3001 et seq.
4. The Secretary has authority and jurisdiction to issue this Consent Agreement and Final Order of the Secretary (CAO) and to enforce same. In any action by KDHE to enforce the terms of this CAO, MGP agrees not to contest the authority or jurisdiction of the Secretary to issue this CAO. The terms of this CAO shall be construed by the law of the state of Kansas.

**STATEMENT OF PURPOSE**

5. In entering into this CAO it is the mutual objective of KDHE and MGP to: (1) resolve all claims against MGP for all identified violations of the Kansas air quality act, K.S.A. 65-3001 et seq. and regulations adopted thereunder, addressed in this CAO; (2) establish a schedule by which MGP will achieve regulatory compliance; and (3) assess an appropriate civil penalty for those violations cited in the CAO.

### **PARTIES BOUND**

6. This CAO shall apply to and be binding upon the parties, their agents, successors, and assigns and upon all persons, contractors, and consultants acting under or for either the KDHE or MGP or both.
7. The parties agree to undertake all actions required of them by the terms and conditions of this CAO.
8. Notwithstanding the terms of any contract, MGP is responsible for compliance with this CAO and for insuring that its contractors and agents comply with this CAO.
9. The activities conducted under this CAO are subject to approval by KDHE. MGP shall provide all necessary information consistent with this CAO requested by KDHE.

### **LIABILITY**

10. Nothing in this CAO shall be construed as an admission of any fact or an acknowledgment of any liability by any party. Nothing herein shall be legally binding or have any effect on the position of the parties on any matter that may be included in any other agreements negotiated between them. Neither the State of Kansas, nor any agency thereof shall be held out as a party of any contract entered into by MGP in carrying out activities pursuant to this CAO.

### **FINDINGS OF FACT**

11. MGP owns and operates an ethanol production facility in Atchison. MGP receives corn and milo which is then milled, mixed with water and starch water, cooked, and fermented. After fermentation, the raw material is distilled to produce ethanol. Distillation separates the liquid ethanol from the corn meal, which MGP may dry or sell as wet mash for animal feed. KDHE alleges that the ethanol plant was modified in such a manner that may have resulted in a significant net emission increase in accordance with 40 C.F.R. Part 52 or the Prevention of Significant Deterioration (PSD) regulations. KDHE adopted the PSD regulations at K.A.R. 28-19-350. KDHE further alleges that MGP failed to obtain a PSD permit authorizing the modification.
12. KDHE alleges that the emissions of volatile organic compounds (VOCs) from the distilled dried grain with solubles (DDGS) dryers had been historically underestimated.
13. KDHE further alleges that MGP may have failed to comply with K.A.R. 28-19-720, which adopts by reference 40 C.F.R. Part 60 Subparts Db, Kb and VV; and K.A.R. 28-19-750, which adopts by reference 40 C.F.R. Part 63 for the equipment described in paragraph 23 of this CAO.

## CONCLUSIONS OF LAW

14. MGP is a person within the meaning of K.S.A. 65-3002(i).
15. The Secretary is authorized to issue orders for compliance with air quality statutes and regulations as set forth in K.S.A. 65-3011.
16. K.S.A. 65-3025(c) states it is unlawful for any person to violate any provision of an approval or permit issued and any rule or regulation promulgated under the Kansas air quality act.
17. K.S.A. 65-3018(a) provides that the Secretary, upon finding a person has violated any provision of K.S.A. 65-3025, may impose a penalty not to exceed \$10,000 per day which shall constitute an actual and substantial economic deterrent to the violation for which it is assessed.
18. K.A.R. 28-19-350(a), *Prevention of significant deterioration of air quality* , applies to the construction of major stationary sources and major modifications of stationary sources as defined in 40 C.F.R. 52.21 in areas of the state designated as attainment areas or unclassified areas for any pollutant under the procedures prescribed by section 107(d) of the federal clean air act.
19. K.A.R. 28-19-350(b) adopts by reference 40 C.F.R. 52.21, as in effect on July 1, 2000.
20. K.A.R. 28-19-720, *New source performance standards* , adopts by reference 40 C.F.R. Part 60, Subparts Db, Kb and VV.
21. K.A.R. 28-19-750, *Hazardous air pollutants; maximum achievable control technology* , adopts by reference 40 C.F.R. Part 63.
22. Based on the above finding of facts and conclusions of law, the Secretary alleges that MGP may have violated K.A.R. 28-19-350, K.A.R. 28-19-720, K.A.R. 28-19-750 and K.S.A. 65-3025.

## SCHEDULE OF COMPLIANCE

### Emission Limits

23. MGP shall implement a plan for the installation of air pollution control technology (Control Technology Plan or CTP) capable of meeting the following emission level reductions for the identified units in subparagraphs (a) through (1). MGP's CTP, which has been approved by MGP, is Attachment 1 to this CAO.
  - a. DDGS Dryer : The existing DDGS dryers shall be removed or made inoperable and replaced with a new Swiss Combi dryer. The new Swiss Combi dryer shall meet the following requirements. Either 95% reduction of VOC emissions or emissions no higher than 10 parts per million (PPM)

of VOC, at MGP's option; either 90% reduction of carbon monoxide (CO) emissions or emissions no higher than 100 PPM of CO, at MGP's option; and reduction of particulate matter (PM) and PM with an aerodynamic diameter less than or equal to a nominal 10 micrometers (PM<sub>10</sub>) based on operation of the new dryer system as specified in Paragraph 26 and the approved CTP and as established after initial performance testing pursuant to Paragraph 31 of this CAO. The dryer shall be equipped with Low-NO<sub>x</sub> burners with an emission limit equal to or less than 0.08 lb/MMBtu. MGP may continue to operate and produce wet cake during periods of DDGS dryer downtime.

- b. Centrate Tank (Defined as Whole Slop Tanks and Centrifuge Vents) : Either 95% reduction of VOC emissions or emissions no higher than 20 PPM of VOC, at MGP's option.
- c. Fermentation Units (Including the Beer Well) : Either 95% reduction of VOC emissions or emissions no higher than 20 PPM of VOC, at MGP's option.
- d. Distillation Units (Including Miscellaneous Process Vents) : Either 95% reduction of VOC emissions or emissions no higher than 20 PPM of VOC, at MGP's option. Insignificant process vents are not required to meet this VOC limitation.
- e. Existing Boilers (Boilers #6, #7 and #8) : MGP shall comply with the oxides of nitrogen (NO<sub>x</sub>) limits specified in Paragraphs 27 and 28 of this CAO. In addition, beginning on the date the CAO is issued MGP shall discontinue the use of fuel oil in Boilers #6 and #7.
- f. Ethanol Loadout (Truck) : Install equipment for the total capture of VOCs and operate a closed loop system vented to a flare for the destruction of captured VOCs. Emissions from trucks dedicated to non-fuel use do not need to be muted to a closed vent system and flare, provided MGP provides documentation to the satisfaction of KDHE that the trucks are dedicated to non-fuel use. Fuel, for the purpose of this CAO and the attached CTP, shall be defined as a petroleum based product such as gasoline. Denatured ethanol and pure ethanol shall be defined as non-fuels.
- g. Ethanol Loadout (Railcar) : All railcars shall be dedicated as non-fuel use only.
- h. New Source Performance Standards (NSPS) : Identify and implement applicable NSPS requirements codified at 40 C.F.R. Part 60. The following NSPS apply: NSPS Subpart Db (Industrial-Commercial-Institutional Steam Generating Units); NSPS Subpart Kb (Volatile Organic Liquid Storage Vessels); and NSPS Subpart VV (Equipment

Leaks of VOC in the Synthetic Organic Chemicals Manufacturing Industry).

The following storage vessels are subject to NSPS Kb: T4324 and T4325.

At the time of CAO issuance, the following units, and auxiliary equipment associated with each unit, were determined not to be subject to NSPS Subpart VV because the equipment was used for the sole purpose of producing beverage alcohol: (1) DC1520 ED Column; (2) DC1530 HQ Rectifier; (3) DC1550 Demethylizer; (4) DC1590 Recycle Rectifier; (5) DC1580 and DC1581 Gin Stills; (6) DC1587 Low Proof Gin Still; (7) ADS1591 and ADS1592 Mole Sieves; (8) T1582 and T1583 Gin Still Product Tanks; and (9) T1586 Low Proof Gin Still Product Tank. At the time of CAO issuance, the DC1510 Beer Still was not subject to NSPS Subpart VV because the unit was installed in 1976 and had not been modified or reconstructed since the effective date of NSPS Subpart VV.

All equipment not specifically listed in the above paragraph is subject to NSPS Subpart VV including the following units, and auxiliary equipment associated with each unit: (1) T1560 5,000 Gallon Recovery Rectifier Feed Tank; (2) DC1560 Recovery Rectifier; and (3) ADS1571 and ADS1572 Mole Sieves.

- i. Fugitive Dust Control PM/PM<sub>10</sub> : The program described in the approved CTP shall be implemented to minimize fugitive dust emissions from the facility operations.
  
- j. Additional Requirements for Hazardous Air Pollutants (HAPs) : Beginning April 1, 2007, MGP shall continually operate the facility so as not to exceed source-wide allowable emissions of 9.0 TPY for any single HAP or 24.0 TPY for all HAPs based on a 12-month rolling sum, rolled monthly, and recorded monthly, or comply with applicable sections of 40 C.F.R. Part 63. For the first eleven months, beginning April 1, 2007, compliance with the 12-month rolling sum will be demonstrated based on the schedule to meet applicable emission caps as set forth in the approved CTP. If, based on emissions testing as set forth in the approved CTP, additional control measures are required to meet the 9.0 or 24.0 TPY emission caps, such control measures shall be implemented and included in the permit application required under Paragraph 39, or comply with applicable sections of 40 C.F.R. Part 63.
  
- k. New Gas Boiler (Alternative Scenario) : In lieu of retrofitting existing boilers with Low-NO<sub>x</sub> burner(s), MGP may elect to install a new boiler and permanently disconnect the existing boiler(s) that will not be retrofitted with Low-NO<sub>x</sub> burner(s). The new boiler shall be installed with Low-NO<sub>x</sub> burner(s) and a NO<sub>x</sub> emission limit equal to or less than 0.04 lb NO<sub>x</sub>/MMBtu shall apply to the new boiler.

1. Grain Unloading and Feed Loading Source Dust Control: Install a PM control system on the north and south grain unloading systems that limits emissions of PM to less than or equal to 0.01 grains/dscf. Install a “dead box” to reduce the velocity of feed to the loadout containers.
  
24. MGP shall install air pollution control technology capable of meeting the emission level reductions for the Swiss Combi DDGS dryer, centrate tank, the fermentation units, the distillation units, existing boilers, ethanol truck and railcar loadout (with the exception of vehicles dedicated to non-fuel use) and grain unloading and feed loading systems in accordance with the schedule in the approved CTP. Beginning no later than 180 days following the start-up of each piece of control equipment required in the CTP for these units, MGP shall operate each unit only in accordance with the operating parameters set forth in the CTP. MGP may utilize existing control equipment to meet the limits set forth in the CAO.
  
25. By no later than October 1, 2006, MGP shall replace the existing DDGS dryers with a DDGS dryer capable of meeting the emission limits set forth in paragraph 23(a).
  
26. PM and PM<sub>10</sub> Emission Limit for DDGS Dryer: By no later than 90 days following the initial performance test of the DDGS dryer as required in Paragraphs 23(a) and 31, MGP shall propose PM and PM<sub>10</sub> emission limits for the DDGS dryer based on the data collected from initial performance testing and other available pertinent information. MGP shall immediately comply with the proposed emission limit. KDHE will use the data collected and other available pertinent information to establish limits for PM and PM<sub>10</sub>. KDHE shall provide written notice to MGP of the established limit and the established limit shall be incorporated into and enforceable under this CAO. If the limit established by KDHE is more stringent than the limit proposed by MGP, then MGP shall have 60 days from the date of written notice to comply with the established limit, unless within the 60 day period, MGP contests the KDHE proposed limit, by invoking the Dispute Resolution process as described in this CAO. Until a limit is established under the Dispute Resolution process herein, MGP shall comply with the emission limit it proposed under this Paragraph.
  
27. NO<sub>x</sub> Emission Limit for Boilers #6 and #7: By no later than 30 days after the existing DDGS dryers are removed or made inoperable, the owner or operator shall limit the NO<sub>x</sub> emissions from Boilers #6 and #7 to 184 tons during each consecutive 12-month period. MGP shall use the following equation to calculate the monthly NO<sub>x</sub> emissions:

$${}^E NO_x = Q \times EF \times CF$$

Where:  ${}^E NO_x$  = Monthly NO<sub>x</sub> emissions (tons/month)

Q = Monthly fuel gas usage (mmscf/month)

EF = NO<sub>x</sub> emission factor (lbs/mmscf). The emission factor

at the time of CAO issuance was 280 lbs/mmssf.

CF = Weight conversion factor (1 ton/2000 lbs)

MGP shall maintain records of the compliance determination for the NO<sub>x</sub> limit. These records shall be updated no later than the last day of the month following the last month of each consecutive 12-month period.

As indicated in the CTP, this 184 tons per year NO<sub>x</sub> limit is an interim limit. By no later than September 1, 2008, MGP shall remove or make inoperable Boilers #6 and #7 or equip the boilers with Low-NO<sub>x</sub> burners with a NO<sub>x</sub> emissions limit of 0.04 lbs/MMBtu.

28. NO<sub>x</sub> Emission Limit for Boiler #8 : By no later than July 1, 2006, MGP shall equip Boiler #8 with a Low-NO<sub>x</sub> burner and the boiler shall be subject to a NO<sub>x</sub> emissions limit of 0.04 lbs/MMBtu.
29. Source-wide VOC Emission Cap : MGP shall accept source-wide allowable emission caps for the facility equivalent to 95 TPY for VOCs for a period of twenty-four months or until termination of this CAO whichever is later. Beginning April 1, 2007, MGP shall continually operate the Facility so as not to exceed the source-wide allowable emission caps of 95 TPY for VOCs based on a 12-month rolling sum, rolled monthly, and recorded monthly. For the first eleven months, beginning April 1, 2007, compliance with the 12-month rolling sum will be demonstrated based on a schedule to meet applicable emission caps as set forth in the approved CTP.

#### Compliance Demonstration

30. MGP shall demonstrate continuous compliance with the emission limits established under this CAO by the use of performance testing, parametric monitoring, recordkeeping and reporting, or initial and periodic compliance testing, as appropriate, as set forth in the approved CTP. Until termination of the CAO, MGP shall (1) conduct annual performance tests on the DDGS dryer and (2) conduct performance tests on all other units in accordance with the frequency set forth in Attachment 2. All such tests shall be conducted using the methods set forth in 7.0 of the approved CTP to demonstrate compliance with the emission limits therein unless this requirement is waived in writing by KDHE.
31. By no later than 180 days following the start-up of the last piece of control equipment or by no later than 180 days after the installation of the new DDGS dryer, as required in the approved CTP, whichever is later, MGP shall demonstrate through an initial performance test that it has met the required destruction efficiency and/or emission limit of each emissions unit as specified in the approved CTP.
32. All performance testing protocol shall be submitted to KDHE for review at least thirty (30) days prior to testing. The performance testing shall be conducted in accordance with EPA promulgated methods and any other test protocols approved



by the parties. Within sixty (60) days of the test date, test results shall be submitted to KDHE.

#### Record Keeping/Reporting

33. Beginning with the first full calendar quarter following lodging of this CAO, MGP shall submit written reports within 30 days following each calendar quarter to KDHE that itemize CAO requirements and the approved CTP requirements, the applicable deadlines, the dates the tasks were completed, unit emissions data and data to support MGP's compliance status with the terms of this CAO. Reports shall be sent to Mr. Victor Cooper, Bureau of Air & Radiation, 1000 SW Jackson, Suite 310, Topeka, Kansas 66612. Emissions data may be submitted in electronic format.
34. MGP shall maintain records to demonstrate compliance with New Source Performance Standards (NSPS), 40 C.F.R., Part 60, Subparts Db and Kb; and MGP's fugitive dust management program as described in the approved CTP.
35. MGP shall maintain records to demonstrate compliance with the source wide VOC cap required under paragraph 29.
36. MGP shall maintain control technology performance criteria monitoring data and records as set forth in the approved CTP, and shall make them available to KDHE upon demand as soon as practicable.
37. MGP shall preserve and retain all records and documents now in its possession or control, or which come into its possession or control, that support the reporting and compliance requirements in this CAO for a period of three years following the termination of this CAO, unless other regulations require the records to be maintained longer.
38. All notices and reports from MGP required under this CAO shall contain the following certification and may be signed by an owner or operator of the company responsible for environmental management and compliance:

"I certify under penalty of law that I have personally examined the information submitted herein and that I have made a reasonable inquiry of those individuals immediately responsible for obtaining the information and that to the best of my knowledge, the information submitted herewith is true, accurate, and complete. I am aware that there are significant penalties for submitting false information, including the possibility of fine and imprisonment."

#### Permitting

39. By no later than 180 days after the execution of this CAO, MGP shall apply for a federally-enforceable construction permit. MGP shall include in its application the emission limits, monitoring and record keeping requirements of the approved

CTP and this CAO as applicable. These emission limits, monitoring and record keeping requirements shall remain applicable to the source for the life of its operation or until changed through a permit modification.

40. By no later than 180 days following start-up of the last piece of control equipment or replacement of the dryer, whichever is later, MGP shall apply to KDHE for modification to its federally enforceable permits to incorporate those emission limits, monitoring parameters, and record keeping set forth in this CAO that have not already been incorporated into the appropriate permits as required in Paragraph 39. MGP does not waive any rights it has to appeal or otherwise contest any permit requirements that it did not specifically include in its applications required under Paragraphs 39 and 40.

#### **ASSESSMENT OF A CIVIL PENALTY**

41. Pursuant to K.S.A. 65-3018 and K.S.A. 65-3025, it is the intent of KDHE to assess a civil penalty in this matter. In consideration of the facts surrounding this event, KDHE has concluded that MGP shall pay a civil penalty in the amount of \$26,000.00 for the alleged violations of K.A.R. 28-19-350, K.A.R. 28-19-720, K.A.R. 28-19-750 and K.S.A. 65-3025.

A check or money order in the amount of \$26,000.00, made payable to the Kansas Department of Health and Environment, is to be submitted to Mr. Victor Cooper, Bureau of Air and Radiation, Kansas Department of Health and Environment, 1000 SW Jackson, Suite 310, Topeka, Kansas 66612-1366, within 30 days of execution of this CAO by the parties.

42. Failure or refusal to comply with this CAO, or any portion thereof, shall subject MGP to the imposition of further civil penalties and court action to enforce the terms of the CAO. MGP reserves the right to contest such penalties and court action.

#### **FORCE MAJEURE, EXCUSABLE DELAY, MODIFICATION**

43. The following shall constitute the governing terms for force majeure, excusable delay and modification of the CAO.
- a. MGP shall perform the requirements under this CAO within the time limits set forth herein unless, the performance is prevented or delayed solely by events which constitute a force majeure. For purposes of this CAO a force majeure is defined as any event beyond the control of MGP which could not be overcome by due diligence and which delays or prevents performance by a date required by this CAO. Such events do not include increased costs of performance or changed economic circumstances. Any delay caused in whole or in part by action or inaction by state authorities shall be considered a force majeure and shall not be deemed a violation of any obligations required by this CAO.

- b. MGP shall have the burden of proving all claims of force majeure. Failure to comply by reason of force majeure shall not be construed as a violation of this CAO.
- c. MGP shall notify KDHE in writing within seven days after becoming aware of an event which MGP knew, or should have known, constituted force majeure. Such notice shall estimate the anticipated length of delay, its cause, measures to be taken to minimize the delay, and an estimated timetable for implementation of these measures. Failure to comply with the notice provision of this section shall constitute a waiver of the MGP right to assert a force majeure claim and shall be grounds for KDHE to deny MGP an extension of time.
- d. Within seven days of the receipt of written notice from MGP of a force majeure event, KDHE shall notify MGP of the extent to which modifications to this CAO are necessary. In the event that KDHE and MGP cannot agree that a force majeure event has occurred, or if there is no agreement on the length of the extension, the dispute shall be resolved as set forth in a paragraph numbered 44 Dispute Resolution.
- e. Any modifications to any provision of this CAO shall not alter the schedule for performance or completion of other tasks required by this CAO unless specifically agreed to by the parties in writing and incorporated into this CAO.
- f. This CAO may be amended by mutual agreement of KDHE and MGP. Such amendments shall be in writing, shall have as their effective date the date on which they are signed by both parties and shall be incorporated into this CAO.

#### **DISPUTE RESOLUTION**

- 44. The parties recognize that a dispute may arise between them regarding implementation of the action to be taken as herein set forth or other terms or provisions of this CAO.
  - a. If such dispute arises, the parties will endeavor to settle it by informal negotiations between themselves. If the parties cannot resolve the issue informally within a reasonable period of time, either of the parties may notify the other in writing stating its position with regard to the dispute and the reasons therefor. A party receiving such a notice of dispute will respond in writing within five (5) business days stating its position. KDHE or MGP shall then have an additional five (5) business days period to respond. If the parties are still unable to reach an agreement, the matter shall be referred to the KDHE Director of Environment, who shall decide the matter and provide a written statement of his decision which shall be incorporated into the CAO.

- b. This dispute resolution procedure shall not preclude any party from having direct recourse to court if otherwise available by applicable law.

**BEST PROFESSIONAL JUDGMENT**

45. The requirements of this CAO represent the best professional judgment of KDHE at this time based on the available information. If circumstances change significantly so that data indicates an immediate threat of danger to the public health or safety or the environment or a significantly different threat other than the alleged deficiencies addressed herein, then KDHE reserves the right to modify dates or requirements herein as it deems reasonably necessary and MGP reserves the right to appeal any such modifications or additional requirements.

**OTHER CLAIMS AND PARTIES**

46. Nothing in this CAO shall constitute or be construed as a release for any claim, cause of action or demand in law or equity against any person, firm, partnership, or corporation not a signatory to this CAO for any liability it may have arising out of or relating in any way to the subject violations alleged in this CAO.

**EFFECTIVE DATE, TERMINATION**

47. This CAO shall become effective when signed by the Secretary of the Department of Health and Environment.
48. This CAO will be terminated upon written notice by KDHE to MGP that all provisions of the CAO have been completed. Such notice shall not be unreasonably withheld.

**AUTHORIZATION OF SIGNATORIES TO EXECUTE THE CONSENT ORDER AND BIND THE PARTIES**

49. The parties hereto have affixed their signatures on the dates inserted below to acknowledge their agreement to this CAO. The signatories to this CAO certify that they are authorized to execute and legally bind the parties they represent to this CAO.

/s/ Roderick L. Bremby  
Roderick L. Bremby, Secretary  
Kansas Department of Health &  
Environment

/s/ David E. Rindom  
David E. Rindom, VP of HR  
MGP Ingredients, Inc.

1/11/06  
Date

12/21/05  
Date

**ATTACHMENT 1**

**Control Technology Plan**

**For**

**MGP Ingredients, LLC**

**1300 Main Street**

**Atchison, Kansas 66002**

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## 1.0 INTRODUCTION

This Control Technology Plan (CTP) is an integral part of the CAO. This CTP contains:

- a) Identification of all units to be controlled;
- b) Engineering design criteria for all proposed controls capable of meeting the emission levels required by the CAO;
- c) Proposed short-term and long-term emission limits and controlled outlet concentrations for each pollutant as appropriate;
- d) A schedule for expedited installation with specific milestones applicable on a unit-by-unit basis;
- e) Proposed monitoring parameters for all control equipment and parameter ranges;
- f) Identification of all units to be emission tested and a schedule for initial tests and retests;
- g) The test methods that will be used to demonstrate compliance with the emission levels set forth in the CAO;
- h) Program for minimization of fugitive dust emissions from facility operations.

**2.0 EMISSION UNITS REQUIRING POLLUTION CONTROL EQUIPMENT**

The following emission units, fugitive sources, and control equipment have been designated as affected units in the CAO and have emission limits requiring pollution control technology.

<b>Unit Description</b>	<b>Control Equipment Description</b>
DDGS Dryer	Replace existing DDGS dryers with a Swiss Combi dryer equipped with Low-NO <sub>x</sub> burner(s)
Centrate Tank (Defined as Whole Slop Tanks and Centrifuge Vents)	Scrubber
Fermentation Units (Including the Beer Well)	Scrubber
Distillation Unit (Including Miscellaneous Process Vents)	Scrubber
Existing Boilers #6 and #7	<ol style="list-style-type: none"> <li>(1) Interim NO<sub>x</sub> limit; and</li> <li>(2) Either retrofitting with Low-NO<sub>x</sub> burner(s) or removal of the boiler; and</li> <li>(3) Discontinuation of the use of fuel oil.</li> </ol>
Existing Boiler #8	Retrofit with Low-NO <sub>x</sub> burner
Cooling Cyclone	Replace existing DDGS dryers with a Swiss Combi dryer equipped with Low-NO <sub>x</sub> burner(s).
Ethanol Truck Loadout	Flare, unless truck is dedicated to non-fuel use
Truck/Car Traffic	Fugitive Dust Control Program
Grain Unloading Systems - North and South	PM Control System
Feed Loading Systems	“Dead Box”
New Gas Fired Boiler (Alternative Scenario)	Low-NO <sub>x</sub> Burner(s)



### 3.0 ENGINEERING DESIGN CRITERIA FOR POLLUTION CONTROL EQUIPMENT

Any deviation from the design criteria listed here shall be reported in the quarterly reports required under this CAO. The specific design criteria listed here are preliminary and subject to change pending development of additional data. Changes to the requirements listed in the following table shall be considered non-material modifications under this CAO, provided MGP obtains written approval of the change(s) from KDHE.

<u>Process Description</u>	<u>Control Device Description</u>	<u>Design Operating Parameters</u>
Centrate Tank	Scrubber	Gas Flow Rate: to be determined Water Flow Rate: to be determined Pressure Drop: to be determined
Fermentation Units (Including the Beer Well)	Scrubber	Gas Flow Rate: to be determined Water Flow Rate: to be determined Pressure Drop: to be determined
Distillation Units (Including Misc. Process Vents)	Scrubber	Gas Flow Rate: to be determined Water Flow Rate: to be determined Pressure Drop: to be determined
Ethanol Truck Loadout	Flare, unless truck is dedicated to non-fuel use	40 C.F.R. § 60.18 NSPS standards. Flare will be assisted by a pilot flame.
Grain Unloading Systems - North and South	PM Control System	To be determined
Feed Loading System	Dead box(es)	To be determined

#### 4.0 EMISSION LIMITS FROM POLLUTION CONTROL EQUIPMENT

Unless otherwise stated, all controlled emission limitations (including operating parameter ranges and limits) apply at all times except during periods of previously planned startup and shutdown periods or as otherwise provided under K.A.R. 28-19-11. These startup and shutdown periods shall not exceed the minimum amount of time necessary for these events, and during these events, MGP shall minimize emissions to the greatest extent practicable. To the extent practical, startup and shutdown of pollution control technology systems will be performed during times when process equipment is also shut down for routine maintenance. MGP shall also, to the extent practicable, control emissions during a malfunction event in a manner consistent with good air pollution control practice for minimizing emissions.

Any deviation from the requirements in 4.0 shall be reported in the quarterly reports and as required under other state and federal regulations.

Process Description	Control Device Description	Pollutant	Emission Limit(s)
New Swiss Combi DDGS Dryer(1)	New Dryer	VOC	95% reduction or $\leq 10$ ppm, at MGP's election
	New Dryer	CO	90% reduction or $\leq 100$ ppm, at MGP's election
	New Dryer	PM/PM <sub>10</sub>	Test and set limit pursuant to this CAO
	Low-NO <sub>x</sub> burners	NO <sub>x</sub>	NO <sub>x</sub> emission limit $\leq 0.08$ lb/MMBtu
Centrate Tank	Scrubber	VOC	95% reduction or $\leq 20$ ppm, at MGP's election
Centrate Tank and Distillation Units (Including Misc. Process Vents)	Scrubber	VOC	95% reduction or $\leq 20$ ppm, at MGP's election
Fermentation Units (Including Beer Well)	Scrubber	VOC	95% reduction or $\leq 20$ ppm, at MGP's election
Existing Boilers #6, #7 and #8 (Boilers #6 and #7, if applicable)	Low-NO <sub>x</sub> burners	NO <sub>x</sub>	NO <sub>x</sub> emission limit $\leq 0.04$ lb/MMBtu

( 1) MGP may continue to operate and produce wet cake during periods of DDGS dryer downtime.

<u>Process Description</u>	<u>Control Device Description</u>	<u>Pollutant</u>	<u>Emission Limit(s)</u>
	Discontinue the use of fuel oil	SO <sub>x</sub>	None
New Boiler (Alternative Scenario)	Low-NO <sub>x</sub> Burner(s)	NO <sub>x</sub>	NO <sub>x</sub> emission limit ≤ 0.04 lb/mmBtu
Ethanol Truck Loadout	Flare, unless truck is dedicated to non-fuel use	VOC	95% reduction
Grain Unloading Systems - North and South	PM Control System	PM/PM <sub>10</sub>	0.01 grains/dscf
Feed Loading System	Dead box(es)	PM/PM <sub>10</sub>	20% opacity

NO<sub>x</sub> Emission Limit for Boilers #6 and #7: By no later than 60 days after the new Swiss Combi DDGS dryer becomes operational, the owner or operator shall limit the NO<sub>x</sub> emissions from Boilers #6 and #7 to 184 tons during each consecutive 12-month period. MGP shall use the following equation to calculate the monthly NO<sub>x</sub> emissions:

$${}^E NO_x = Q \times EF \times CF$$

Where: <sup>E</sup>NO<sub>x</sub> = Monthly NO<sub>x</sub> emissions (tons/month)

Q = Monthly fuel gas usage (mmscf/month)

EF = NO<sub>x</sub> emission factor (lbs/mmscf). The emission factor at the time of CAO issuance was 280 lbs/mmscf.

CF = Weight conversion factor (1 ton/2000 lbs)

MGP shall maintain records of the compliance determination for the NO<sub>x</sub> limit. These records shall be updated no later than the last day of the month following the last month of each consecutive 12-month period.

This 184 tons per year NO<sub>x</sub> limit is an interim limit. By no later than September 1, 2008, MGP shall remove Boilers #6 and #7 or equip the boilers with Low-NO<sub>x</sub> burners with a NO<sub>x</sub> emissions limit of 0.04 lbs/MMBtu.

## 5.0 POLLUTION CONTROL EQUIPMENT INSTALLATION SCHEDULE

MGP shall install, shake down, and start up the following air pollution control equipment (or optimize existing equipment) and begin complying with the emission limits required by the CAO by the following dates:

Unit Description	Control Equipment	Date
New Swiss Combi DDGS Dryer	Replacement of existing DDGS dryers with a Swiss Combi dryer equipped with Low-NO <sub>x</sub> burners capable of meeting emission limits in CAO. The existing DDGS dryers shall be removed or made in operable.	October 1, 2006
Centrate Tank	Scrubber	8 months after the issuance of the CAO
Fermentation Units (Including Beer Well)	Scrubber	8 months after the issuance of the CAO
Distillation Units (Including Miscellaneous Process Vents)	Scrubber	8 months after the issuance of the CAO
Existing Boilers #6 and #7	Low-NO <sub>x</sub> Burner(s), remove boilers or make boilers inoperable	September 1, 2008
	Interim NO <sub>x</sub> limit as described in Section 4.0 of CTP	30 days after the date the existing DDGS dryers are removed or made inoperable.
	Discontinue the use of fuel oil	Upon issuance of the CAO
Existing Boiler #8	Low-NO <sub>x</sub> Burner and FGR	July 1, 2006
New Boiler (Alternative scenario)	Low-NO <sub>x</sub> Burner(s)	Upon start up of the boiler
Ethanol Truck Loadout	Flare	8 months after the issuance of the CAO
Grain Unloading Systems - North and South	PM Control System	16 months after the issuance of the CAO

<u>Unit Description</u>	<u>Control Equipment</u>	<u>Date</u>
Feed Loading System	"Dead Box"	12 months after the issuance of the CAO
Truck Traffic Fugitive Dust Program	Road Sweeper	4 months after issuance of the CAO

In accordance with the CAO, beginning April 1, 2007, MGP shall limit VOC emissions from the facility to less than 95 tons per year. Also beginning April 1, 2007, MGP shall limit emissions of each individual HAP to less than 9.0 tons per year and the combination of all HAPs to less than 24.0 tons per year. During the first 11 months, beginning April 1, 2007, the facility will maintain the following source-wide emission limits in Tons Per Year:

	<u>Mo 1</u>	<u>Mo 2</u>	<u>Mo 3</u>	<u>Mo 4</u>	<u>Mo 5</u>	<u>Mo 6</u>	<u>Mo 7</u>	<u>Mo 8</u>	<u>Mo 9</u>	<u>Mo 10</u>	<u>Mo 11</u>
Source-wide VOC	12	24	36	45	56	64	72	80	84	88	92
Individual HAP	1.6	3.2	4.0	4.8	5.6	6.4	7.2	8.0	8.2	8.5	8.8
Total HAPs	3.0	6.0	9.0	12	14	16	18	20	21	22	23

## 6.0 MONITORING PARAMETERS FOR POLLUTION CONTROL DEVICES

The CAO requires that monitoring parameters be established for affected pollution control devices. Beginning no later than 60 days following startup of a control device described below, MGP agrees to the following monitoring parameters for each of the affected pollution control devices. All monitoring data collected above shall be recorded and maintained on-site. Any deviations of monitoring frequency, record keeping and range shall be reported in the quarterly reports and as required under other state and federal regulations.

<b>Control Device Description</b>	<b>Parameter Monitored</b>	<b>Operating Range</b>	<b>Monitoring Frequency</b>
Scrubbers	Liquid Flow Rate	Varies based on design of the individual scrubbers	Continuously
	Pressure Drop	2 to 8 inches of water	Daily
Flare	Presence of a Flame	A device (including but not limited to a flame sensor interlock with truck pumping, a thermocouple, a ultraviolet beam sensor or infrared sensor) capable of detecting presence of a flame	Continuously during ethanol truck loading

**7.0 POLLUTION CONTROL DEVICE PERFORMANCE TEST SCHEDULE AND TEST METHODS USED**

The following schedule and methods will be used to demonstrate compliance with the emission limits contained in this CTP and the CAO. MGP shall conduct the following performance testing pursuant to the schedule under paragraphs 30, 31 and 32 of the CAO. The dryer shall be tested annually, and all other units in the CTP according to the schedule set forth in Attachment 2, unless specifically waived in writing by KDHE.

<b>Emission Unit/Control Device</b>	<b>Pollutant(s) Tested</b>	<b>Test Method</b>
Swiss Combi DDGS Dryer/New Dryer equipped with a Low-NO <sub>x</sub> burner	Total VOC, speciated VOCs and HAPs, NO <sub>x</sub> , CO, PM/PM <sub>10</sub>	Method 1, 2, 3, 3A, or 3B, 4, 5/202, 7E, 10, 18 (“as Total VOC Mass”) and 25 or 25A; another EPA promulgated method; in accordance with a test protocol approved by the parties.
Centrate Tank, Fermentation Units (Including Beer Well), and Distillation Units (Including Misc. Process Vents)/Scrubbers	Total VOC, speciated VOCs and HAPs.	Method 1, 2, 3, 3A, or 3B, 4, 18 (“as Total VOC Mass”) and 25 or 25A; another EPA promulgated method; in accordance with a test protocol approved by the parties.
Existing Boilers and New Boiler (Alternative Scenario)/Low-NO <sub>x</sub> burner (s)	NO <sub>x</sub> and CO	Method 7E and 10; another EPA promulgated method; in accordance with a test protocol approved by the parties.
Truck Loadout/Flare	VOCs and Visible Emissions	Per 40 CFR 60.18 for open flame flare. For enclosed flame flare, as applicable, Method 1, 2, 3, 3A, or 3B, 4, 18 (“as Total VOC Mass”) and 25 or 25A; another EPA promulgated method; in accordance with a test protocol approved by the parties.
Grain Unloading Systems - North and South/PM Control System	PM/PM <sub>10</sub>	Method 5; another EPA promulgated method; in accordance with a test protocol approved by the parties.
Feed Loading Systems/”Dead Box”	PM/PM <sub>10</sub>	Method 9; another EPA promulgated method; in accordance with a test protocol approved by the parties.

## 8.0 FUGITIVE DUST EMISSION CONTROL PROGRAM

The objectives of the Fugitive Control Program are to prevent and minimize the release of avoidable fugitive emissions as required by the CAO. The Program describes the procedure MGP will use to control emissions, to determine when emissions are at levels requiring corrective action, and to reduce excessive emissions to acceptable levels.

MGP has existing paved roads (all normal traffic routes) that are used for truck and car traffic at the ethanol plant. MGP will implement the following actions to minimize fugitive dust emissions:

1. MGP will perform weekly visual inspections of the roads.
2. MGP will document the inspection was performed and describe any corrective action taken.
3. MGP will sweep the roads within 48 hours of when fugitive emissions are observed that are caused by car/truck traffic on the roads.
4. In the event that sweeping is not possible due to weather conditions; MGP will use water or mechanical means of removal, if possible, to minimize fugitive dust emissions.



## ATTACHMENT 2

### PERFORMANCE TEST FREQUENCY CRITERIA

#### Proposed Testing Frequency for equipment with concentration or emission limits:

X = Pollutant emissions rate or concentration established during a performance test. Test results used to determine X ideally span three tests or more.

<u>Performance Test Results</u>	<u>Performance Test Frequency</u>
If $X \geq 90\%$ of the most stringent limit	The next performance test must be conducted within 12 months.
If $60\% \leq X < 90\%$ of the most stringent limit	The next performance test must be conducted within 36 months.
If $X < 60\%$ of the most stringent limit	The next performance test must be conducted within 60 months.

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**Accountants' Acknowledgement**

We acknowledge the incorporation by reference in the Registration Statements on Form S-8 (Registration Nos. 333-119860 and 333-51849) of MGP Ingredients, Inc. (Company) of our report dated May 2, 2006, included with the Quarterly Report on Form 10-Q for the quarter ended March 31, 2006. Pursuant to Rule 436(c) under the Securities Act of 1933, this report should not be considered part of the Registration Statement prepared or certified by us within the meaning of Sections 7 and 11 of the Act.

/s/ **BKD , LLP**

Kansas City, Missouri  
May 10, 2006

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**CERTIFICATION**

I, Laidacker M. Seaberg, certify that:

1. I have reviewed this quarterly report on Form 10-Q of MGP Ingredients, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonable likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 10, 2006

/s/ Laidacker M. Seaberg  
Laidacker M. Seaberg  
President and Principal Executive Officer

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**CERTIFICATION**

I, Brian T. Cahill, certify that:

1. I have reviewed this quarterly report on Form 10-Q of MGP Ingredients, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
  - c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonable likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent functions):
  - a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: May 10, 2006

/s/ Brian T. Cahill  
Brian T. Cahill  
Vice President and Treasurer and Principal Financial and  
Accounting Officer

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**CERTIFICATION**  
**OF**  
**PERIODIC REPORT**

I, Laidacker M. Seaberg, President and Chief Executive Officer of MGP Ingredients, Inc. (the “Company”), certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

(1) the Quarterly Report on Form 10-Q of the Company for the quarter ended March 31, 2006 (the “Report”) fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 10, 2006

/s/ Laidacker M. Seaberg  
Laidacker M. Seaberg  
President and Chief Executive Officer

[A signed original of this written statement required by Section 906 has been provided to MGP Ingredients, Inc. and will be retained by MGP Ingredients, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.]

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**CERTIFICATION**  
**OF**  
**PERIODIC REPORT**

I, Brian T. Cahill, Vice President and Chief Financial Officer of MGP Ingredients, Inc. (the "Company"), certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

(1) the Quarterly Report on Form 10-Q of the Company for the quarter ended March 31, 2006, (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934 (15 U.S.C. 78m or 78o(d)); and

(2) the information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Dated: May 10, 2006

/s/ Brian T. Cahill  
Brian T. Cahill  
Vice President and Chief Financial Officer

[A signed original of this written statement required by Section 906 has been provided to MGP Ingredients, Inc. and will be retained by MGP Ingredients, Inc. and furnished to the Securities and Exchange Commission or its staff upon request.]

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