KPMG

PHOSPHATE HOLDINGS, INC. AND SUBSIDIARY

Consolidated Financial Statements

December 31, 2008, 2007 and 2006

(With Independent Auditors' Report Thereon)

PHOSPHATE HOLDINGS, INC. AND SUBSIDIARY

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KPMG LLP
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Independent Auditors' Report

The Board of Directors
Phosphate Holdings, Inc.:

We have audited the accompanying consolidated balance sheets of Phosphate Holdings, Inc. and Subsidiary (the Company) as of December 31, 2008 and 2007, and the related consolidated statements of operations, stockholders' equity, and cash flows for each of the years in the three-year period ended December 31, 2008. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards as established by the Auditing Standards Board (United States) and in accordance with the auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Phosphate Holdings, Inc. and Subsidiary as of December 31, 2008 and 2007, and the results of their operations and their cash flows for each of the years in the three-year period ended December 31, 2008, in conformity with U.S. generally accepted accounting principles.

KPMG LLP

Jackson, Mississippi
April 22, 2009

PHOSPHATE HOLDINGS, INC. AND SUBSIDIARY

Consolidated Balance Sheets

(In thousands, except share data)

Assets		**December 31, 2008**	**2007**
Current assets:			
Cash and cash equivalents	$	2,153	43,576
Trade accounts receivable		7,400	10,041
Income taxes receivable		21,414	—
Other receivables		1,863	1,682
Inventories		47,645	18,103
Prepaid expenses and other		5,079	4,957
Deferred income taxes		—	1,059
Total current assets		85,554	79,418
Restricted investments held in trust, at fair value		2,990	3,348
Property, plant and equipment, net		50,593	41,417
Other		130	120
Total assets	$	139,267	124,303
Liabilities and Stockholders' Equity			
Current liabilities:			
Accounts payable	$	2,658	2,236
Accrued expenses		11,760	18,703
Current maturities of long-term debt		600	—
Short-term financing obligations		2,181	2,185
Deposits on future sales		24,600	—
Revolving credit agreement		11,494	—
Deferred income taxes		573	—
Total current liabilities		53,866	23,124
Long-term debt, less current maturities		2,400	—
Asset retirement obligations		4,841	5,086
Deferred income taxes		7,940	10,863
Total liabilities		69,047	39,073
Stockholders' equity:			
Common stock ($0.01 par; 30,000,000 shares authorized at December 31, 2008, 11,000,000 shares authorized at December 31, 2007, 7,654,290 shares issued and outstanding at December 31, 2008 and 2007)		77	77
Additional paid-in capital		33,880	33,880
Retained earnings		36,263	51,273
Total stockholders' equity		70,220	85,230
Commitments and contingencies (notes 16 and 18)			
Total liabilities and stockholders' equity	$	139,267	124,303

See accompanying notes to consolidated financial statements.

PHOSPHATE HOLDINGS, INC. AND SUBSIDIARY

Consolidated Statements of Operations

(In thousands, except per share data)

		Years ended December 31,		
		2008	2007	2006
Net sales:				
DAP	$	432,852	219,569	130,579
Other		12,989	2,805	985
Total net sales		445,841	222,374	131,564
Cost of sales		441,170	169,952	128,684
Gross profit		4,671	52,422	2,880
Selling, general and administrative expenses		8,373	12,301	4,472
Reduction in asset retirement obligations		(732)	—	—
Impairment of assets		1,572	—	—
Operating income (loss)		(4,542)	40,121	(1,592)
Other income (expense):				
Interest, net		297	301	(735)
Hurricane related gain		—	37,830	—
Other, net		(913)	176	533
Total other income (expense)		(616)	38,307	(202)
Income (loss) before income taxes		(5,158)	78,428	(1,794)
Income tax expense (credit)		(1,629)	29,539	—
Net income (loss)	$	(3,529)	48,889	(1,794)
Earnings (loss) per share – basic	$	(0.46)	6.39	(0.24)
Earnings (loss) per share – diluted		(0.46)	6.04	(0.24)
Weighted average common shares outstanding – basic		7,654	7,654	7,369
Weighted average common shares outstanding – diluted		7,654	8,089	7,369

See accompanying notes to consolidated financial statements.

PHOSPHATE HOLDINGS, INC. AND SUBSIDIARY

Consolidated Statements of Stockholders' Equity

Years ended December 31, 2008, 2007, and 2006

(In thousands, except share data)

	Common Stock			Additional Paid-in Capital	Retained Earnings	Total
	Shares		Par Value			
Balance, December 31, 2005	7,312,330	$	73	14,234	4,178	18,485
Net loss	—		—	—	(1,794)	(1,794)
Share-based compensation expense	—		—	74	—	74
Capital contributions from exercise of stock options	341,960		4	801	—	805
Balance, December 31, 2006	7,654,290		77	15,109	2,384	17,570
Net income	—		—	—	48,889	48,889
Share-based compensation expense	—		—	223	—	223
Recognition of pre-bankruptcy deferred tax assets	—		—	16,398	—	16,398
Excess income tax benefit of employee stock option exercises	—		—	2,150	—	2,150
Balance, December 31, 2007	7,654,290		77	33,880	51,273	85,230
Net loss	—		—	—	(3,529)	(3,529)
Cash dividends paid	—		—	—	(11,481)	(11,481)
Balance, December 31, 2008	7,654,290	$	77	33,880	36,263	70,220

See accompanying notes to consolidated financial statements.

PHOSPHATE HOLDINGS, INC. AND SUBSIDIARY

Consolidated Statements of Cash Flows

(In thousands)

		Years ended December 31,		
		2008	2007	2006
Cash flows from operating activities:				
Net income (loss)	$	(3,529)	48,889	(1,794)
Adjustments to reconcile net income (loss) to net cash (used in) provided by operating activities:				
Depreciation of property, plant and equipment		5,596	4,199	2,561
Amortization of prepaid maintenance turnaround costs		3,693	2,891	1,011
Accretion of asset retirement obligation		487	459	418
Deferred loan cost amortization		48	52	106
Reduction in asset retirement obligation		(732)	—	—
Deferred income taxes		(1,291)	26,202	—
Hurricane related gain		—	(37,830)	—
Proceeds from insurance reimbursements - property, plant and equipment related		—	(8,437)	(19,581)
Share-based compensation		11	223	74
Impairment charges		1,572	—	—
Unrealized restricted investment loss (gain)		1,158	67	(256)
Other		2	(27)	(6)
Changes in operating assets and liabilities:				
Trade and other accounts receivable		2,460	(6,185)	(5,241)
Income taxes receivable		(21,414)	—	—
Inventories		(29,542)	(4,497)	(2,323)
Prepaid expenses and other		(4,650)	(3,176)	(1,758)
Accounts payable and accrued expenses		(6,532)	11,524	(6,215)
Advances from insurance carrier, net		—	14,346	31,809
Net cash (used in) provided by operating activities		(52,663)	48,700	(1,195)
Cash flows from investing activities:				
Purchases of restricted investments held in trust		(800)	(800)	(800)
Purchases of property, plant and equipment		(15,509)	(10,397)	(24,099)
Proceeds from insurance reimbursements - property, plant and equipment related		—	8,437	19,581
Net cash used in investing activities		(16,309)	(2,760)	(5,318)
Cash flows from financing activities:				
Deposits on future sales		24,600	—	—
Net (payments) borrowings on revolving credit agreement		11,494	(4,875)	4,875
Payments of short-term financing obligations		(3,667)	(3,883)	(3,356)
Proceeds from short-term financing obligations		3,663	3,597	4,080
Excess income tax benefit of stock options exercised		—	2,150	—
Capital contributions from exercise of stock options		—	—	805
Payment of deferred loan costs		(60)	—	—
Proceeds from term loan		3,000	—	—
Cash dividends		(11,481)	—	—
Net cash provided by (used in) financing activities		27,549	(3,011)	6,404
Net (decrease) increase in cash and cash equivalents		(41,423)	42,929	(109)
Cash and cash equivalents at beginning of year		43,576	647	756
Cash and cash equivalents at end of year	$	2,153	43,576	647
Supplemental disclosure of cash flow information:				
Cash payments for interest	$	227	374	860
Cash payments (refunds) of income taxes		20,718	1,094	(1,275)

See accompanying notes to consolidated financial statements.

(1) Nature of Business and Significant Accounting Policies

(a) Nature of Business

Phosphate Holdings, Inc. (PHI) and its subsidiary, Mississippi Phosphates Corporation (MPC, or the Subsidiary), produces diammonium phosphate (DAP) fertilizer at its production facility in Pascagoula, Mississippi. PHI and MPC are referred to collectively as "the Company." The Company is organized and managed internally based on one reportable segment, phosphates, which includes the production and sales of DAP.

(b) Organization

PHI was incorporated on December 17, 2004, under the laws of the state of Delaware. Prior to June 20, 2007, all of the common stock of PHI was owned by the MPC Statutory Trust (the "Trust"). The beneficial ownership of the Trust was represented by Trust Units, which were freely tradable. On June 20, 2007, at a Special Meeting of the Trust Unit Holders, dissolution of the Trust was approved. As a result of the dissolution of the Trust, the Unit Holders received their proportionate interest in the assets of the Trust consisting of 7,654,290 shares of PHI common stock. PHI currently owns all of the outstanding common stock of MPC. MPC was incorporated on October 29, 1990, under the laws of the state of Delaware.

(c) Principles of Consolidation

The consolidated financial statements include the accounts of PHI and its wholly owned subsidiary, MPC. All significant intercompany balances and transactions have been eliminated in consolidation.

(d) Use of Estimates

The preparation of financial statements in conformity with U.S. generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Management evaluates its estimates and assumptions on an ongoing basis using historical experience and other factors, including the current economic environment, which management believes to be reasonable under the circumstances. Management adjusts such estimates and assumptions when facts and circumstances dictate. Illiquid credit and fertilizer markets have increased the uncertainty inherent in such estimates and assumptions. As future events and their effects cannot be determined with precision, actual results could differ from the estimates and assumptions used by management in the preparation of the accompanying financial statements and such differences could be significant. Changes in those estimates resulting from continuing changes in the economic environment will be reflected in the financial statements in future periods.

(e) Cash and Cash Equivalents

Cash equivalents include investments with maturities of three months or less when purchased. The carrying values of cash and cash equivalents approximates fair value.

(f) Inventories

Inventories are valued at the lower of cost or net realizable value on a moving average cost basis. Finished goods include material costs, labor costs, and manufacturing overhead.

(g) Replacement Parts

The Company maintains replacement parts at its production facility in order to minimize disruption in production in the event of part failures. Replacement parts which are considered expendable are included in inventories and are charged to cost of sales as they are placed in service. Replacement parts which are repairable are reported as a component of property, plant and equipment and are depreciated over their estimated useful lives.

(h) Allowances for Doubtful Accounts

The Company is subject to credit risk in connection with the collection of its accounts receivable and, accordingly, makes estimates related to the ultimate collection of accounts receivable. Specifically, the Company analyzes accounts receivable, bad debt experience, customer concentrations, customer credit-worthiness and current economic and market conditions, when evaluating the adequacy of the allowance for doubtful accounts. The Company's business is primarily with a small number of customers and the collection history with these customers has been favorable. All accounts receivable balances outstanding as of December 31, 2008 and 2007 were collected subsequent to year-end.

(i) Restricted Investments Held in Trust

In conjunction with producing DAP, the Company is required to maintain a phosphogypsum disposal facility for waste byproducts. The Company has developed a financial assurance mechanism with the Mississippi Department of Environmental Quality (MDEQ) in order to ensure that there will be adequate funds available to cover the estimated costs related to the closure of the Company's disposal facilities when they reach capacity levels. Quarterly payments in the amount of $200 are made into a restricted trust fund managed by a third-party trustee. The investments held within this trust fund represent debt and equity securities, which are classified as trading securities in accordance with Statement of Financial Accounting Standards (SFAS) No. 115, *Accounting for Certain Investments in Debt and Equity Securities*, as such securities are actively managed in order to maximize the portfolio's investment returns. The Company recognizes realized and unrealized gains or losses on these securities in the period incurred. The Company's investments are comprised of exchange traded securities and investment funds, which are recorded at fair value based upon daily quoted closing prices.

(Dollars in thousands unless otherwise indicated)

(j) Property, Plant, and Equipment

Property, plant, and equipment are stated at cost, less accumulated depreciation. Expenditures for major improvements are capitalized; expenditures for normal maintenance and repairs are charged to expense as incurred. Depreciation expense is computed using the straight-line method over the estimated useful lives of the assets as follows:

Buildings	6 to 40 years
Site improvements	5 to 15 years
Machinery and equipment	2 to 10 years
Replacement parts	10 years

(k) Impairment of Long-Lived Assets

In accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*, long-lived assets, such as property, plant, and equipment, are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable. If circumstances require that a long-lived asset be tested for possible impairment, the Company first compares undiscounted cash flows expected to be generated by an asset to the carrying value of the asset. If the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, an impairment is recognized to the extent that the carrying value of the asset exceeds its fair value. Fair value is determined through various valuation techniques, including discounted cash flow models, quoted market values and third-party independent appraisals, as considered necessary.

During 2008, two events occurred that caused one of the Company's two sulfuric acid plants to shut down for a significant portion of the first quarter.

As described more fully in Note 18(i), the Company hired a contractor to assemble and install replacement internal components of the boiler. The boiler in question failed on January 17, 2008. The boiler repairs were completed and the plant resumed production on February 19, 2008. During the quarter ended March 31, 2008, the Company recorded an impairment charge of approximately \$737 for property, plant and equipment and approximately \$835 for maintenance turnaround costs associated with the January 17, 2008 boiler failure.

On February 20, 2008, a converter in the plant suffered a failure related to a weld. The failure analysis conducted by the Company and its third-party consultants indicated that the failed weld, which dates back to the original construction of the plant in the mid-1970s, was defective. The weld rupture caused only minimal damage to the internals of the converter, and no apparent damage to other areas of the plant. A repair plan was developed and the Company completed the repairs and resumed production during March 2008.

During the fourth quarter of 2008, the Company incurred operating losses. Such losses required an assessment as to the recoverability of the Company's long-lived assets. Based upon an assessment of the undiscounted cash flows expected to be generated by the Company's long-lived assets, it was determined that the carrying value of such assets at December 31, 2008, was recoverable.

(l) Income Taxes

Income taxes are accounted for under the asset and liability method. Deferred tax assets and liabilities are recognized for the future tax consequences attributable to differences between the financial statement carrying amounts of existing assets and liabilities and their respective tax bases and operating loss and tax credit carryforwards. Deferred tax assets and liabilities are measured using enacted tax rates expected to apply to taxable income in the years in which those temporary differences are expected to be recovered or settled. The effect on deferred tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the enactment date. Beginning with the adoption of Financial Accounting Standards Board (FASB) Interpretation No. 48, *Accounting for Uncertainty in Income Taxes* (FIN 48) as of January 1, 2007, the Company recognizes the effect of income tax positions only if those positions are more likely than not of being sustained. Recognized income tax positions are measured at the largest amount that is greater than 50 percent likely of being realized. Changes in recognition or measurement are reflected in the period in which the change in judgment occurs. The Company reports tax-related interest and penalties as a component of income tax expense. Prior to the adoption of FIN 48, the Company recognized the effect of income tax positions only if such positions were probable of being sustained. Upon adoption and through December 31, 2007, the Company recorded no liability for uncertain tax positions, as all of the Company's tax positions were considered highly certain of being recognized for income tax purposes. As of and for the year ended December 31, 2008, the Company has recognized approximately $245 of accrued interest and penalties related to uncertain tax positions.

(m) Environmental Costs

Environmental expenditures that relate to existing conditions caused by past operations, and that do not contribute to current or future revenue generation, are expensed. Environmental costs are capitalized if the costs extend the life of the property, increase its capacity or mitigate or prevent contamination from future operations. Liabilities are recorded when environmental assessments and/or remedial efforts are required and the costs can be reasonably estimated.

(n) Asset Retirement Obligations

The Company is required to maintain a disposal facility for its by-product phosphogypsum. Under an agreement with the MDEQ, the Company is obligated to incur future costs associated with closure and related remediation of the disposal facilities. The Company develops estimates for the cost to close its disposal facility as well as the related environmental remediation requirements pursuant to the guidance set forth in SFAS No. 143, *Accounting for Asset Retirement Obligations*. The costs are adjusted for inflation and discounted based on a credit adjusted risk-free rate. Over time, the liability is accreted to its present value. The accretion expense is included as a component of cost of sales in the accompanying consolidated statements of operations.

(o) Revenue Recognition

Revenue is recognized when the earnings process is completed. The Company considers the earnings process to be complete when the risk of ownership and title passes to the customer, collection of the related receivable is probable, evidence of an arrangement exists and the sales price is fixed or determinable. Base prices for the Company's product are set pursuant to sales contracts based on current published prices or upon negotiated short-term prices with the customer. Shipping and handling costs incurred by the Company are included in cost of sales.

(p) DAP Trading Activities

The Company has entered into an agreement with a third party whereby the third party and the Company jointly identify opportunities to purchase and resell DAP in the domestic market. When an opportunity is identified, the third party purchases and ultimately resells the DAP. Under the terms of the agreement, the Company and the third party each share 50 percent of the gain or loss on the completed transaction. The Company is obligated to remit to the trading partner the Company's share of any losses incurred in conjunction with this activity but is not obligated to accept or make delivery of DAP pursuant to any of these trading positions. The Company marks open trading positions to market at each reporting period end based on its profit and loss sharing percentage. The income or loss related to this activity is reported as net sales - other.

(q) Maintenance Turnaround Costs

The Pascagoula facility schedules periodic maintenance turnarounds for the various plants within the facility. The associated costs of these turnarounds are capitalized and then amortized as part of cost of sales over the expected benefit period.

(r) Stock Offering Costs

On October 14, 2008, the Company filed a Form S-1 Registration Statement with the Securities and Exchange Commission pursuant to a planned public stock offering. As a result of volatility in the financial and fertilizer markets, these plans were indefinitely postponed. Included in selling, general and administrative expenses in the accompanying 2008 consolidated statement of operations are costs totaling $2,934 related to the planned stock offering and associated re-audit costs.

(s) Share-Based Compensation

The Company accounts for share-based compensation in accordance with SFAS No. 123R, *Share-Based Payment*, which requires the measurement and recognition of compensation expense for all share-based payment awards to be made based on estimated grant date fair values. Under the fair value recognition provisions of SFAS 123R, share-based compensation cost is measured at the grant date based on the fair value of the award and is recognized as expense on a straight-line basis over the requisite service period, which is the vesting period. The fair value of share-based payment awards on the date of grant is determined using an option-pricing model which is affected by assumptions regarding a number of complex and subjective variables, which include the expected life of the award, the expected stock price volatility over the expected life of the awards, expected dividend yield, and the risk-free interest rate.

(Continued)

(t) Fair Value of Financial Instruments

Due to their short-term nature, the Company's cash and cash equivalents, accounts receivable, accounts payable and short-term financing obligations are carried at cost, which approximates fair value. The revolving credit facility's recorded value approximates its fair value as it bears interest at a floating rate. At December 31, 2008, the fair value of the Company's long-term indebtedness approximated $2,730. The Company's restricted investments are recorded at fair value based upon quoted closing market prices.

(u) Recent Accounting Pronouncements

In May 2008, the FASB issued SFAS No. 162, *The Hierarchy of Generally Accepted Accounting Principles* (SFAS 162). SFAS 162 identifies the sources of accounting principles and the framework for selecting the principles to be used in the preparation of financial statements of nongovernmental entities that are presented in conformity with generally accepted accounting principles (GAAP) in the United States (the GAAP hierarchy). SFAS 162 is effective 60 days following the SEC's approval of the Public Company Accounting Oversight Board amendments to AU Section 411, *The Meaning of Present Fairly in Conformity With Generally Accepted Accounting Principles*. The Company does not anticipate any significant impact on its financial position or operating results in applying this statement.

In December 2007, the FASB issued SFAS No. 141 (Revised 2007), *Business Combinations* (SFAS 141R) and SFAS No. 160, *Noncontrolling Interests in Consolidated Financial Statements*, an Amendment of ARB No. 51 (SFAS 160). SFAS 141R and SFAS 160 significantly change the accounting for and reporting of business combination transactions and noncontrolling (minority) interests. Under SFAS 141R, an acquiring entity will be required to recognize all the assets and liabilities assumed in a transaction at the acquisition date fair value. In addition, SFAS 141R includes a substantial number of additional disclosure requirements. SFAS 160 changes the accounting and reporting for minority interests, which will be recharacterized as noncontrolling interests and classified as a component of equity. The Company will be required to apply the provisions of SFAS 141R and SFAS 160 prospectively effective January 1, 2009.

In March 2008, the FASB issued SFAS 161, *Disclosure about Derivative Instruments and Hedging Activities*, an Amendment of FASB Statement No. 133 (SFAS 161). SFAS 161 changes the disclosure requirements for derivative instruments and hedging activities. The Company will be required to provide enhanced disclosures about (a) how and why the Company uses derivative instruments, (b) how these derivative and related hedged items are accounted for pursuant to SFAS 133 and related interpretations, and (c) how these items will affect the Company's financial position, financial performance and cash flows. The Company must adopt SFAS 161 effective January 1, 2009. The Company does not anticipate any significant impact on its financial position or operating results in applying this statement.

On January 1, 2008, the Company adopted SFAS No. 157, Fair Value Measurements (SFAS 157) and FASB Staff Position (FSP) No. 157-2, which deferred the adoption of portions of SFAS 157. SFAS 157 establishes a single authoritative definition of fair value, sets out a framework for

(Continued)

measuring fair value, and provides a disclosure framework for assets and liabilities measured at fair value. The adoption of SFAS No. 157 did not have a significant impact on the Company's consolidated financial statements. FSP No. 157-2 defers for one year the effective date of SFAS 157 for nonfinancial assets and liabilities measured at fair value on a nonrecurring basis. The purpose of this deferral is to allow the FASB and constituents additional time to consider the effect of various implementation issues that have arisen, or may arise, from the application of SFAS 157. The assets and liabilities included in the consolidated balance sheet for which the adoption of SFAS 157 has been deferred include the Company's long-lived assets and asset retirement obligations.

On January 1, 2008, the Company adopted the provisions of SFAS No. 159, *The Fair Value Option for Financial Assets and Financial Liabilities* (SFAS 159). SFAS 159 permits entities to choose to measure many financial instruments and certain other items at fair value. The Company has not elected the fair value option for any assets or liabilities under SFAS No. 159.

(2) Current Market Conditions

The Company's operating results are highly dependent upon: business and economic conditions and policies affecting fertilizer demand and prices as well as the agricultural industry in general; DAP price and demand volatility, resulting from imbalances of supply and demand such as that experienced in late 2008; and price volatility and availability of raw materials. During late 2008, the Company saw a deterioration in the global phosphates market. The global credit crisis significantly reduced planting and crop input purchases in major agricultural markets throughout the world. In North America, demand for DAP was significantly reduced as a result of farmers delaying fall fertilizer application because of adverse fall weather conditions, declining grain prices, economic uncertainty, illiquid credit markets, high input costs, and the expectation of lower future input costs.

The global reduction in demand for DAP created high inventory levels within the industry which in turn led to sharp declines in sales prices and significant curtailment of fertilizer production. Demand and sales prices for the Company's DAP also significantly declined during late 2008. This caused the Company to reduce its DAP production as well as record an adjustment in the amount of $87,673 to write down its finished goods and raw materials to their net realizable values as of December 31, 2008. The losses resulting from these write-downs caused the Company to fail to comply with certain of the financial covenants under its credit facilities as discussed in Note 8.

The recent market conditions have required the Company to assess its operating cash flow needs and ability to fund necessary capital expenditures and debt service requirements. In response to these challenges, the Company has reduced its inventory levels and also negotiated alternative financing arrangements with certain of its business partners. As discussed in Note 8, the Company has also renegotiated certain aspects of its credit facility agreement in response to the impact that these market conditions have had on the Company's business. While there can be no assurances, management believes the Company's operating plans and available credit facilities should be adequate to meet its operating and other cash flow needs during 2009 and into the foreseeable future.

(Dollars in thousands unless otherwise indicated)

(3) Inventories

Inventories consisted of the following:

	December 31, 2008	December 31, 2007
Raw materials	$ 18,716	5,104
Finished goods	11,411	7,740
DAP inventory delivered pursuant to deposit arrangement	11,791	—
Replacement parts	5,727	5,259
	$ 47,645	18,103

Inventories are valued at the lower of cost or net realizable value. As a result of declines in the market prices for the Company's raw materials and finished goods during late 2008 and early 2009, the Company recorded inventory valuation write-downs totaling $87,673 during 2008, to reduce its raw materials and finished goods to their estimated net realizable values. These write-downs are included as a component of cost of sales in the Company's 2008 consolidated statement of operations. If market conditions continue to deteriorate, the Company may have additional write-downs of its inventories in the future.

DAP inventory of $11,791 represents the net realizable value of 45,194 tons of DAP inventory delivered to a customer under a deposit arrangement. The terms of the deposit arrangement required the Company to deliver the DAP to the customer at a provisional price. The Company is also required to bear the cost of delivery, storage and interest (carrying costs) until the earlier of the time the customer re-markets the product in the open market at a fixed and determinable price, or March 15, 2009. During 2008, the Company recorded carrying costs related to this arrangement of approximately $609, which are included as a component of cost of sales in the Company's 2008 consolidated statement of operations. The Company received approximately $24,600 in deposits related to this arrangement, which are recorded as a current liability in the Company's 2008 consolidated balance sheet. At the time the customer re-markets the DAP in the open market and receives payment from a third party, the Company will reimburse the customer the per-ton price differential between the provisional price plus carrying costs and the final sales price negotiated with the customer. The Company will then reduce its DAP inventory and associated liability related to the deposit arrangement as well as record net sales and all remaining costs associated with the arrangement.

Phosphate rock is a primary raw material in the manufacture of DAP. Effective January 1, 2005, the Company entered into a contract with OCP S.A. (OCP) in Morocco to import its full requirement of phosphate rock through December 31, 2008. The purchase price of rock was fixed for the period January 1, 2005 through June 30, 2006. The purchase prices for the periods July 1, 2006 through December 31, 2008, were each established periodically based on negotiation between the parties. On June 6, 2008, OCP notified the Company that, rather than extend the current contract, it desired to enter into a new agreement. Management is currently negotiating a new contract and believes a new long-term supply arrangement with OCP will be achieved. In the interim, the Company and OCP have reached an agreement on the supply of phosphate rock to the Company through June 30, 2009. There can be no assurances that a phosphate rock supply agreement can be reached beyond June 30, 2009.

(Dollars in thousands unless otherwise indicated)

(4) Prepaid Expenses and Other

Prepaid expenses and other consisted of the following:

		December 31,	
		2008	2007
Prepaid insurance	$	2,636	2,465
Prepaid maintenance turnaround costs		1,894	1,469
Deposits		531	384
Prepaid income taxes		—	113
Other		18	526
	$	5,079	4,957

Amortization expense related to maintenance turnaround costs was $3,693, $2,891 and $1,011, for the years ended December 31, 2008, 2007, and 2006, respectively. These expenses are included as a component of cost of sales. In addition, maintenance turnaround costs of $835 were written off in 2008 as a result of the failure of a boiler in one of the Company’s sulfuric acid plants.

(5) Property, Plant and Equipment, Net

Property, plant, and equipment consisted of the following:

		December 31,	
		2008	2007
Buildings	$	4,998	2,044
Site improvements		4,121	3,757
Machinery and equipment		47,977	38,004
Replacement parts		2,309	1,690
Construction in progress		3,559	2,697
		62,964	48,192
Less accumulated depreciation		12,371	6,775
Property, plant and equipment, net	$	50,593	41,417

Depreciation expense totaled $5,596, $4,199, and $2,561, for the years ended December 31, 2008, 2007, and 2006, respectively.

(Continued)

(Dollars in thousands unless otherwise indicated)

(6) Accrued Expenses

Accrued expenses consisted of the following:

		December 31,	
		2008	2007
Accrued raw material purchases	$	2,943	5,182
Accrued freight and storage		2,485	652
Accrued DAP trading losses		1,954	—
Accrued compensation		457	7,597
Accrued self-insurance claims		683	294
Accrued property taxes		602	538
Accrued utilities		601	522
Accrued environmental settlements		—	1,950
Other		2,035	1,968
	$	11,760	18,703

Approximately $6,983 of the accrued compensation at December 31, 2007, related to cash bonuses payable to two officers of the Company pursuant to their employment agreements, which were entered into effective as of MPC's emergence from bankruptcy on December 21, 2004 (the Emergence Date). The bonuses were based on the Company's net cash flow (earnings before bonuses, interest, taxes, depreciation and amortization less capital expenditures of a normal and customary nature and net cash payments for interest, federal, state and local taxes) for the period from the Emergence Date through December 31, 2007. Effective January 1, 2008, the two officers entered into new employment agreements. Under the new agreements, bonuses are calculated based on return on equity, as defined in the agreements and are shared with additional members of management with the approval of the Company's Board of Directors. There were no bonuses accrued at December 31, 2008.

(7) Short-term Financing Obligation

The Company has financed its property and liability insurance premiums for policy periods ranging from June 2008 through December 2009. The premiums are financed at interest rates ranging from 4.53 percent to 5.48 percent. The notes are payable in monthly installments and mature at dates ranging from May 2009 through November 2009.

(8) Credit Facilities

As of December 31, 2008 and 2007, the Company had a revolving credit agreement with PNC Bank, National Association (PNC), which provides for revolving advances based on specified percentages of accounts receivable and inventories. On May 5, 2008, the Company executed an amendment to its revolving credit agreement with PNC, which increased the maximum borrowing amount from $15,000 to $27,000. Prior to March 23, 2007, borrowings bore interest at a variable rate which was the greater of PNC's base rate plus 1.00 percent, or the Federal Funds Open Rate plus 1.50 percent. On March 23, 2007, the Company executed an amendment to its revolving credit agreement with PNC which changed interest charges to the Company's option of the Alternate Base Rate plus 0.50 percent or the Eurodollar Rate (both as defined in the credit agreement) plus 3.00 percent. The Company was charged an annual commitment fee of 0.50 percent on the unused portion of the revolving advances through May 5, 2008, at which time the facility was amended, reducing the annual commitment fee on the unused portion to 0.40 percent. The Company had $11,494 and $0 borrowings outstanding under this revolving credit agreement at December 31, 2008 and 2007, respectively. The Company had $11,247 available to borrow under the borrowing base limitations of the revolving credit agreement at December 31, 2008. The revolving credit agreement expires on March 31, 2011.

(Dollars in thousands unless otherwise indicated)

At December 31, 2008, the Company also had a $3,000 term loan outstanding under this agreement which funded the construction cost of its storm protection levee completed in 2007. The term facility bears interest consistent with the revolving credit facility and amortizes ratably over five years. The scheduled repayment of principal on the term facility as of December 31, 2008, is as follows:

Year ending December 31,		
2009	$	600
2010		600
2011		600
2012		600
2013		600
	$	3,000

The borrowings are collateralized by receivables, inventories, equipment, and other personal property. Financial covenants of the revolving credit agreement require the Company to maintain specified levels of tangible net worth and fixed charge coverage ratios and to limit capital expenditures. For fiscal years 2007 and 2008 only, the capital expenditure covenant excludes Katrina-related expenditures.

At December 31, 2008, the Company failed to comply with two covenants. The Company exceeded the capital expenditure limitation of $10,000 (excluding Katrina-related expenditures) and failed the fixed charge coverage ratio (as defined). On April 17, 2009, the Company executed an amendment to its revolving credit agreement with PNC, which waived noncompliance for both covenant violations. Additionally, the amended agreement extended the maturity to March 31, 2012, decreased the maximum borrowing amount from $27,000 to $17,000 and changed interest charges for domestic revolving advances to the Alternate Base Rate plus 2.00 percent, for Eurodollar Rate revolving advances to the Eurodollar Rate plus 3.00 percent, for domestic rate term loans to the Alternate Base Rate plus 2.50 percent and for Eurodollar Rate term loans to the Eurodollar Rate plus 3.50 percent. The capital expenditure limitation was increased to $15,000 in 2009 but is limited to $10,000 for fiscal year 2010 and thereafter. The annual commitment fee on the unused portion of the revolving advances was increased from 0.40 percent to 0.50 percent. The fixed charge coverage ratio reporting periods were amended whereby the Company will report to PNC beginning the three month period ending June 30, 2009, then report the six month period ending September 30, 2009, the nine month period ending December 31, 2009, and the twelve month period ending March 31, 2010 and for the four quarter period ending as of each fiscal quarter thereafter. Prior to the fixed charge coverage ratio reporting periods, the Company will be required to report certain

(Dollars in thousands unless otherwise indicated)

Consolidated EBITDA (as defined) levels for the one month period ending April 30, 2009 and the two month period ending May 31, 2009. The amended agreement also requires the Company to execute a long-term contract for the purchase of phosphate rock on or before March 31, 2010. While there can be no assurances, management believes the Company will comply with these covenants in 2009 and into the foreseeable future.

(9) Asset Retirement Obligations

In conjunction with producing DAP, the Company is required to maintain a phosphogypsum disposal facility for its waste byproducts. The Company's East disposal facility became fully operational during 2003. Prior to 2003, the Company maintained a West disposal facility for its waste byproducts. The closure of the West facility was completed in 2005. There is no asset retirement obligation recorded for the West facility, as the closure is complete and the related water leachate is being used by the Company in production. The Company has a legal obligation to incur future costs associated with the closure of the East disposal facility. Accordingly, the Company has recorded the estimated fair value of the asset retirement obligations in accordance with SFAS No. 143. The liability for the East disposal facility costs include closure, post-closure monitoring and related water treatment. The actual amounts to be spent will depend on factors such as the timing of activities, refinements in scope, technological developments, cost inflation, changes in regulations, as well as, the Company's business plans. It is possible that these factors could change and that such changes could have a significant impact on the estimates included in the accompanying consolidated financial statements. Closure expenditures for the East disposal facility are currently estimated to occur in the 2025 to 2033 timeframe.

The balance of the Company's asset retirement obligations and changes thereto are summarized below. Accretion expense is reported in cost of sales in the accompanying consolidated statements of operations.

Obligations at December 31, 2005	$	4,209
Changes in estimated obligations		—
Accretion expense		418
Obligations at December 31, 2006		4,627
Changes in estimated obligations		—
Accretion expense		459
Obligations at December 31, 2007		5,086
Changes in estimated obligations		(732)
Accretion expense		487
Obligations at December 31, 2008	$	4,841

As of October 1, 2008, the Company reassessed its future costs of closure, post-closure monitoring and related water treatment costs of its East disposal facility. Based upon this assessment, the Company determined that the present value of the future costs would be lower by $732 and, accordingly, reduced its asset retirement obligation liability in accordance with SFAS No. 143. The original retirement asset associated with this obligation was reduced to zero in conjunction with the allocation of the Company's enterprise value upon emergence from bankruptcy in 2004, pursuant to Statement of Position 90-7,

 (Continued)

Financial Reporting by Entities in Reorganization under the Bankruptcy Code (SOP 90-7). Accordingly, the reduction of the asset retirement obligation has been reflected as a separate component of operating income in the accompanying 2008 consolidated statement of operations, which increased operating income in 2008.

As described in Note 1, the Company has developed a financial assurance mechanism with the MDEQ to ensure funds will be available to satisfy the Company's asset retirement obligations. Quarterly payments in the amount of $200 are made into a trust fund managed by a third-party trustee and will be used to fund closure, post-closure monitoring and remediation of the East disposal facility.

(10) Stockholders' Equity

Prior to June 20, 2007, all of the common stock of PHI was owned by the Trust. The beneficial ownership of the Trust was represented by Trust Units, which were freely tradable. At a special meeting of the stockholders of PHI on June 19, 2007, the Trust voted to amend the Certificate of Incorporation of PHI to increase the authorized shares of PHI to 11,000,000 shares of common stock, $0.01 par value, and to effectuate a 7,654.29-to-1 split of all issued and outstanding shares of PHI. On June 20, 2007, at a Special Meeting of the Trust Unit Holders, dissolution of the Trust was approved. As a result of the dissolution of the Trust, the Unit Holders received their proportionate interest in the assets of the Trust consisting of 7,654,290 shares of PHI common stock. On April 29, 2008, PHI amended its Certificate of Incorporation to increase the authorized shares of PHI to 30,000,000 shares of common stock, $0.01 par value. All share information included in the accompanying consolidated financial statements and related notes, including reported earnings per share, have been adjusted to reflect the Company's capital structure as of December 31, 2008.

On December 5, 2007, the Board of Directors of the Company adopted a stockholders' rights plan. Under the plan, the Company declared a dividend of one common stock purchase right for each share of the Company's common stock outstanding payable on December 17, 2007, to stockholders of record at the close of business on such date. Under the plan, the rights will initially trade together with the Company's common stock and will not be exercisable. The rights generally will become exercisable to acquire the Company's common stock (or, in certain circumstances, shares of an acquirer) at a discounted price if a person or group becomes an "acquiring person" through the acquisition of 20 percent or more of the Company's outstanding common stock or the announcement of a tender or exchange offer that would result in ownership of 20 percent or more of the Company's common stock on terms not approved by the Company. If a person or group already owned 20 percent or more of the Company's outstanding common stock on the date the rights plan was adopted, the rights will become exercisable if that person or group acquires any additional shares of the Company's outstanding common stock after the date of the adoption of the plan. Rights held by an "acquiring person" will become void and will not be exercisable to purchase shares at the bargain purchase price. The Company, at its option, may redeem the rights for $0.01 per right for a limited time after a person becomes an "acquiring person." The plan also permits the Company to issue to holders of its common stock, other than an "acquiring person," one share of common stock in exchange for each right, which is then exercisable. The rights will expire on December 31, 2009, unless earlier redeemed, exchanged, or amended.

On January 29, 2008, the Company's Board of Directors declared a special dividend of $1.50 per share. The dividend was paid on March 7, 2008, to stockholders of record on February 25, 2008.

(11) Earnings (Loss) Per Share

SFAS No. 128, *Earnings Per Share* (SFAS 128), requires the presentation of basic and diluted earnings per share. Basic earnings (loss) per share is calculated based on the weighted-average shares of common stock outstanding during the period. Diluted earnings (loss) per share is calculated to include any dilutive effect of common stock equivalents. The Company's common stock equivalents consist of stock options. The dilutive effect of the stock options is calculated using the treasury stock method in accordance with the provisions of SFAS 128.

The weighted-average number of common shares outstanding for the purpose of computing basic and diluted earnings per share is as follows (in thousands):

	Years ended December 31,		
	2008	**2007**	**2006**
Weighted-average number of common shares outstanding - basic	7,654	7,654	7,369
Common stock equivalents	—	435	—
Weighted-average number of common shares outstanding - diluted	7,654	8,089	7,369

Pursuant to the provisions of SFAS 128, common stock equivalents totaling 433 and 130 have been excluded from the computation of diluted net loss per share for the years ended December 31, 2008 and 2006, respectively, because their inclusion would have reduced the reported net loss per share.

(12) Concentration of Business

Effective January 1, 2007, all of the Company's sales of DAP into international markets are made through a single wholesale broker, while all domestic sales of DAP are made through the Company's internal sales staff. Approximately 73 percent, 35 percent and 29 percent of the Company's DAP sales were made into international markets in 2008, 2007, and 2006, respectively.

Customers which account for over 10 percent of total net sales are shown below:

	2008		2007		2006	
	Sales amount	**Percent of total**	**Sales amount**	**Percent of total**	**Sales amount**	**Percent of total**
Customer A	$ 324,845	73%	$ 112,733	51%	$ 21,904	17%
Customer B	—	—	29,628	13%	24,286	18%
Customer C	—	—	26,910	12%	17,944	14%
Customer D	—	—	—	—	37,746	29%

(Dollars in thousands unless otherwise indicated)

Customers which account for over 10 percent of trade accounts receivable are shown below:

	2008		2007	
	Outstanding receivables	**Percent of total**	**Outstanding receivables**	**Percent of total**
Customer A	$ 5,656	76%	$ 2,231	22%
Customer B	—	—	2,270	23%
Customer C	948	13%	—	—
Customer E	792	11%	—	—
Customer F	—	—	1,577	16%
Customer G	—	—	1,479	15%

(13) Interest, Net

Interest, net, consisted of the following for the years ended December 31:

	2008	2007	2006
Interest expense	$ (332)	(421)	(1,004)
Interest income	629	722	269
Net interest income (expense)	$ 297	301	(735)

(14) Income Taxes

Income tax expense consisted of the following for the years ended December 31:

	2008	2007	2006
Current:			
Federal	$ 99	2,619	—
State	(437)	718	—
Deferred:			
Federal	(1,662)	23,239	—
State	371	2,963	—
Total income tax expense	$ (1,629)	29,539	—

(Dollars in thousands unless otherwise indicated)

The differences between income tax expense at the federal statutory rate of 35 percent and reported income tax expense were as follows for the years ended December 31:

	2008		2007		2006	
	Amount	**Percent of pre-tax income**	**Amount**	**Percent of pre-tax income**	**Amount**	**Percent of pre-tax income**
Expected income tax expense (benefit)	$ (1,805)	(35.0)%	$ 27,450	35.0%	$ (628)	35.0%
State income taxes, net	(43)	(0.8)%	2,459	3.1%	(67)	3.7%
Increase (decrease) in valuation allowance	—	—	(773)	(1.0)%	773	(43.1)%
Accrual for uncertain tax position	245	4.7%	—	—	—	—
Other, net	(26)	(0.5)%	403	0.6%	(78)	4.4%
Total income tax expense	$ (1,629)	(31.6)%	$ 29,539	37.7%	$ —	—%

Deferred income tax assets and liabilities consisted of the following at December 31:

	2008	2007
Deferred tax liabilities:		
Property, plant and equipment	$ 4,657	2,048
Gain on involuntary conversion	14,470	14,470
Prepaid and other assets	1,051	1,001
Total deferred tax liabilities	20,178	17,519
Deferred tax assets:		
Net operating loss carryforwards	7,891	3,629
Tax credit carryforwards	1,385	1,456
Asset retirement obligation	1,852	1,946
Accrued expenses and other liabilities	369	246
Other	168	438
Total deferred tax assets	11,665	7,715
Net deferred tax liabilities	$ 8,513	9,804

(Dollars in thousands unless otherwise indicated)

As of December 31, the net deferred tax liabilities are presented in the accompanying consolidated balance sheets as follows:

		2008	2007
Current deferred income tax assets	$	—	1,059
Current deferred income tax liabilities		(573)	—
Long-term deferred income tax liabilities		(7,940)	(10,863)
	$	(8,513)	(9,804)

A valuation allowance was provided on the associated deferred tax assets as of December 31, 2006, due to the uncertainty of realization of the tax benefits associated with the Company's net deferred tax assets. During 2007, management reduced the valuation allowance associated with these net deferred tax assets by $17,171, based upon the determination that it is more likely than not that the net operating loss carryforwards will be realized in future years based upon an evaluation of the reversal of existing taxable temporary differences as well as projected future income resulting from the significant increase in the price of DAP at that time. Of the total reduction in the valuation allowance in 2007, $16,398 was applicable to the valuation allowance established as of the Emergence Date and, accordingly, was recorded as an addition to additional paid-in capital in accordance with SOP 90-7. As of December 31, 2008, the Company had net operating loss carryforwards totaling approximately $6,789 which are subject to annual utilization limitations pursuant to Internal Revenue Code section 382 of approximately $453 through 2022.

Certain previously reported deferred tax liabilities and assets disclosed in the table above have been corrected to reflect the amounts actually reported on the Company's 2007 income tax returns. These immaterial corrections did not impact the deferred income tax related balances reported in the accompanying consolidated financial statements.

The Company had no significant unrecognized tax benefits at the date of adoption of FIN 48. If interest or penalties were to be incurred related to uncertain tax positions, such amounts would be recognized in income tax expense. Tax periods for all years after 2004 remain open for examination by the federal and state taxing jurisdictions to which the Company is subject. The following table is a reconciliation of the beginning and ending amounts of unrecognized tax benefits including interest and penalties. These unrecognized tax benefits are included as a component of accrued expenses in the Company's 2008 consolidated balance sheet.

Amounts of unrecognized tax benefits at December 31, 2007	$	—
Increases as a result of interest and penalties		245
Amounts of unrecognized tax benefits at December 31, 2008	$	245

(15) Thrift Plan

The Company has a contributory thrift plan that covers substantially all regular full-time employees who have elected to participate in the plan. The Company matches a certain percentage of each employee's contributions to the plan up to a maximum percentage of the employee's base compensation. The

(Dollars in thousands unless otherwise indicated)

Company's expense related to this plan totaled approximately $289, $283, and $237 in 2008, 2007, and 2006, respectively.

(16) Commitments

(a) Operating Leases

The Company has commitments under operating leases for equipment and office space. The following is a schedule of the future minimum rental payments required as of December 31, 2008, under operating leases having noncancelable lease terms in excess of one year as of the respective lease's inception:

Years ending December 31:		**Amount**
2009	$	118
2010		55
2011		18
2012		1
	$	192

Rental expense for all operating leases was $748, $367, and $362 for the years ended December 31, 2008, 2007, and 2006, respectively.

(b) Open DAP Trading Positions

As discussed in Note 1 to the consolidated financial statements, the Company engages in DAP trading activities pursuant to which the Company is exposed to market price risk. The Company's exposure and opportunity related to open trading positions is limited based on a negotiated profit and loss sharing percentage with a third party who is responsible for executing and settling the trading positions, including taking physical delivery of DAP, when necessary. The Company is not obligated to accept or make delivery of DAP pursuant to the trading positions executed by its trading partner. As of December 31, 2008 and 2007, the Company and its trading partner had open long positions in DAP totaling 3,037 tons and 4,689 tons, respectively, which had a market value of approximately $873 and $2,579, respectively. At December 31, 2008 and 2007, the Company's share of the mark-to-market gain (loss) related to these open trading positions totaled $(1,263) and $99, respectively. As of December 31, 2008, the Company had liabilities related to DAP trading of $1,954, which consists of a realized loss on a closed but unpaid DAP trading position of $691 and the unrealized losses of $1,263 on open DAP trading positions.

Net trading gains, which include the mark-to-market adjustments discussed above for the open positions as of each year end, totaled $406 and $451 for the years ended December 31, 2008 and 2007, respectively. The Company did not engage in DAP trading activity during 2006.

(Continued)

(17) Share-based Compensation

(a) Stock Options

On the Emergence Date, the Company granted options covering a total of 841,960 shares to two executive employees. Of this total, 459,251 of the options were subject to time-based vesting during the 12 months subsequent to the Emergence Date (the Tranche 1 Options) and 382,709 of the Options were subject to a performance condition which was satisfied on January 1, 2005 (the Tranche 2 Options). Tranche 1 and Tranche 2 Options covering 500,000 shares were exercised in 2005 and the remaining 341,960 of these Options were exercised in 2006. The strike price on the Tranche 1 Option grant was greater than the market value of the Company's stock as of the grant. Additionally, the strike price of the Tranche 2 Option grant was greater than the market value of the Company's stock as of the date the performance condition was satisfied. Accordingly, pursuant to the provisions of APB 25, no compensation expense has been recorded related to the Tranche 1 and Tranche 2 Options.

In addition to the Options discussed above, as of the Emergence Date, the Company also granted Options covering a total of 757,018 shares (the Tranche 3 and Tranche 4 Options) to the same two executive employees discussed above. These Options include performance conditions related to the achievement of certain investor rate of return targets and the achievement of certain stock liquidity objectives, as specified in the respective agreements. As discussed in Note 1, these Options were accounted for pursuant to the provisions of APB 25 prior to the adoption of SFAS 123R on January 1, 2006. Under APB 25, options which contain performance conditions are accounted for as variable awards until the measurement date is determined, which occurs when the performance condition or conditions are satisfied. As a variable award, compensation expense is recognized as of the end of each reporting period prior to the measurement date based on (1) the intrinsic value of the option, and (2) management's assessment of the probability of satisfying the performance condition. Based on an evaluation of the stock option performance conditions, management determined that the Options were not probable of exercise, and as such, recorded no compensation expense related to these Options for the year ended December 31, 2005. Beginning on January 1, 2006, pursuant to the adoption of SFAS 123R, the Company has recorded compensation expense for the Tranche 3 and Tranche 4 Options based on their grant date fair value. As of July 31, 2007, the performance conditions were satisfied and the Options became fully vested, which resulted in the remaining unrecognized compensation expense measured pursuant to SFAS 123R being charged to earnings at that time.

Recorded share-based compensation expense related to the Company's stock options totaled $223 and $74 for the years ended December 31, 2007 and 2006, respectively. Tax benefits related to the share-based compensation expense has been recorded using a blended federal and state income tax rate of 38.25 percent.

(Dollars in thousands unless otherwise indicated)

A summary of the Company's stock option activity during the year ended December 31, 2008 is as follows:

	Options	Weighted-average exercise price	Weighted-average remaining contractual life	Aggregated intrinsic value
Outstanding as of December 31, 2007	757,018	$ 2.36	2	$ 29,251
Granted	—			
Exercised	—			
Forfeited	—			
Outstanding as of December 31, 2008	757,018	2.36	1	3,717
Exercisable as of December 31, 2008	757,018	2.36	1	3,717

The intrinsic value of options exercised during 2008, 2007, and 2006 was $0, $0, and $2,339, respectively.

(b) Stock Appreciation Rights (SARs)

On April 29, 2008, the Company granted 21,703 Stock Appreciation Rights (SAR) to the Directors of the Company (the Director SARs). The Director SARs are to be settled with a cash payment equal to the intrinsic value of the SAR as of the exercise date. One-third of the Director SARs vest on each of the first three anniversary dates following the grant date. The Director SARs expire on the fifth anniversary of the grant date.

On May 5, 2008, the Company granted 25,000 SARs to a key employee (the Employee SARs). The Employee SARs vest on the second anniversary of the grant date and are to be settled with a cash payment equal to the intrinsic value of the SAR as of the exercise date. In the event that the Company's shares become registered with the Securities Exchange Commission, the Employee SARs shall immediately convert to stock options on the same terms as the Employee SARs except that there will no longer be a cash settlement feature.

Both the Director SARs and the Employee SARs are accounted for as liability awards with compensation cost measured as of the end of each reporting period based on the then-current fair value of the SAR. Compensation costs recognized in the accompanying consolidated financial statements related to the Director and Employee SARs were not material for 2008.

(c) Phantom Stock

On May 5, 2008, the Company issued a phantom stock award valued at $100 as of the grant date to a key employee. As of the grant date, the award equated to 2,723 shares of the Company's stock. On each of the first two anniversary dates of the grant, the employee is to receive a cash payment equal to the then fair value of 50 percent of the 2,723 shares. This award is accounted for as a liability award with compensation cost measured as of the end of each reporting period based on the market value of the Company's stock. Compensation costs recognized in the accompanying consolidated financial statements related to the phantom stock award were not material for 2008.

(18) Contingencies

(a) Phosphate Industry Investigation

In 2003, the U.S. Environmental Protection Agency (EPA) announced a nationwide review of all mineral processing facilities. As a result, the EPA selected the mineral processing industry as a National Enforcement and Compliance Priority for fiscal years 2005 and 2006. One focus of this initiative is to examine the scope of applicability of the Bevill Amendment to Subtitle C of the Resource Conservation Recovery Act (RCRA), which exempts waste generated during phosphate mining beneficiation and processing activities from regulation under RCRA. As a part of the EPA initiative, between 2005 and 2007, the EPA visited all phosphate industries in the United States. In January and March 2005, the EPA conducted site visits of the Company's facility in Pascagoula, Mississippi. In September 2005, the EPA issued a Notice of Violation (NOV) to the Company alleging that the reuse of low pH process water as DAP scrubber water and other uses within the facility is not protected by the Bevill Amendment and therefore violates RCRA. The Company believes that it has meritorious defenses against the allegations of the NOV, including prior written guidance and interpretations from the EPA inconsistent with its assertions in the NOV. The EPA has issued similar NOVs to other U.S. phosphate producers. The Company intends to cooperate with the EPA and to work toward a negotiated resolution of this matter. If no resolution is achieved, the Company intends to aggressively defend the issues raised in the NOV. The Company has entered into a Joint Defense Agreement with certain other phosphate producers with respect to this EPA initiative.

(b) RCRA 3013 Consent Order

On June 8, 2007, the Company and the EPA entered into a RCRA 3013 Consent Order which requires the Company to prepare a plan for groundwater and surface water sampling around the facility. The 3013 Consent Order is part of the Phosphate Industry Investigation, pursuant to which the EPA is requiring all the phosphate-producing facilities to conduct groundwater and surface water sampling. The Company has submitted its sampling plan to the EPA for review. To date, there is no indication from current groundwater and surface sampling that there has been any offsite impact from the Company's operations. Because the Company is already conducting a majority of the sampling requested by the EPA under existing MDEQ permits, the cost of complying with the EPA consent order is not deemed material.

(c) NPDES Permit Renewal

In accordance with MDEQ regulations, the Company, on December 22, 2006, submitted its renewal application for its wastewater discharge permits (NPDES permit) to the MDEQ. The application was submitted 180 days prior to the permit's expiration date and although the MDEQ has yet to reissue the NPDES permit, the facility may continue to operate under the state of Mississippi's permit shield until the MDEQ takes final action on the permit application.

On April 16, 2007, the EPA issued the final Total Maximum Daily Load (TMDL) for Bayou Casotte, a body of water adjacent to the Company's plant and the receiving stream for the facility's wastewater effluent. The TMDL established a concentration limit or water quality standard for free un-ionized ammonia in Bayou Casotte. The established limit will result in new lower discharge permit limits once the NPDES is renewed. The current wastewater treatment plant cannot meet the new lower permit limits at the current outfall location, because the current outfall location has insufficient water volume to satisfy the water quality standard.

Anticipating the issuance of the final TMDL, the Company proposed in its NPDES permit renewal application to relocate its primary wastewater discharge location to a point further out into Bayou Casotte. The relocation of the outfall will allow the existing wastewater treatment plant to satisfy the TMDL requirements by creating a larger mixing zone to satisfy the water quality standard. The Company has retained the services of HydroQual, Inc., to conduct a Mixing Zone Study and to design a diffuser system to distribute the treated wastewater into Bayou Casotte. The Company continues to work with the MDEQ to establish a compliance schedule which will allow the Company time, approximately three years from the reissuance of the NPDES permit, to design and relocate the outfall. The Company estimates that the cost to relocate the outfall is less than $1,000.

(d) Hazardous Air Pollutants Notice of Potential Violation

On May 8, 2008, the EPA issued a Notice of Potential Violation, or NOPV, to the Company, alleging potential violations under the National Emission Standards for Hazardous Air Pollutants for Phosphoric Acid Manufacturing Plants and National Emission Standards for Hazardous Air Pollutants for Phosphate Fertilizer Production Plants.

According to the EPA's compliance guidelines for related field activities, an NOPV does not constitute a compliance order, a penalty assessment or any other administrative or judicial enforcement action. Although the EPA routinely monitors the compliance of regulated entities and issues Notices of Violation for documented violations of applicable environmental regulations, the NOPV that the Company received merely alleges potential violations of regulations that may ultimately be deemed inapplicable to the Company.

The EPA based the NOPV on the premise that the Company is a "major source" for emission of a single hazardous air pollutant, hydrogen fluoride, in excess of ten tons per year. The EPA concedes that it has relied exclusively on its own calculations to support its contention that all known phosphate fertilizer and phosphoric acid plants are major sources of hydrogen fluoride. The Company has produced records to the EPA and to the MDEQ and as part of their Title V Air Operating permit which indicates a maximum potential emission of 9.7 tons of hydrogen fluoride per year and actual emissions that have never exceeded more than three tons per year. The Company intends to cooperate with the EPA in any investigations related to this issue. The Company intends to aggressively defend the issues raised in the NOPV.

The Company and the EPA have signed a Tolling Agreement to suspend all action on this matter until March 2010.

(e) Dike Failure

As a byproduct of phosphoric acid production, phosphogypsum is produced at the Pascagoula plant. Phosphogypsum and untreated process water are stored at the plant in “stacks” surrounded by a dike system. Due to unusually heavy rainfall in late March and early April 2005, a small portion of the dike system was severely weakened and collapsed on April 14, 2005. This breach resulted in the uncontrolled release of untreated low pH process water which flowed into, and adversely affected aquatic life and vegetation in, Bangs Lake and Bayou Casotte, a shallow lake contiguous to the plant site. The Company believes both bodies of water have substantially recovered from the impact of this incident.

Pursuant to an Agreed Order with the MDEQ dated January 31, 2008, the Company agreed to resolve this issue. Under the Agreed Order, the Company paid $1,000 (which was fully reimbursed by the Company’s pollution liability insurance provider) for the restoration of environmental damage caused to Bangs Lake and the Grand Bay National Estuarine Research Reserve as a result of the April 2005 dike failure. In addition, the Agreed Order required the Company to prepare a revised plan to provide greater protection against the release of untreated wastewater from the phosphogypsum storage system. In accordance with the Agreed Order, the Company has submitted its proposed plan to the MDEQ for review. The proposed plan includes revised best management practices for managing wastewater within the gypsum system and proposes to increase the emergency storage capacity of the water system to provide greater retention capacity in the event of a breach or overflow of a gypsum pond dike. The Company has received approval from the MDEQ to begin construction activities to raise the outer dike of the east gypsum pond by three feet. The increased retention capacity will be used solely as secondary containment in the event of a breach or overflow of a gypsum dike. The Company anticipates that construction of the dike will be completed by September 2009. The Company is currently working with the MDEQ regarding the remaining items in the proposed plan. The Company estimates that the costs to implement the proposed recommendations are approximately $1,000.

The Agreed Order resolves all issues with the MDEQ regarding the April 14, 2005 dike failure.

(f) Regional HAZE Regulations and BART

In 2006, the MDEQ notified the Company that the facility may be subject to the Regional Haze Regulations which were adopted by EPA on July 6, 2005. The Regional Haze Regulations and accompanying Best Available Retrofit Technology (BART) rule, required operations of facilities which began operation after August 7, 1962, and built before August 7, 1977, to determine whether the facility contributes to visibility impairments at federally protected Class 1 areas. Such air sources are termed “BART-eligible sources” if a single source contributes more than 0.5 deciviews (dv) of impact to the Class 1 area. Based upon air modeling conducted by Trinity Consultants, the Company determined that the two sulfuric acid plants were the only air emitting sources at the Company’s facilities which were BART-eligible facilities for the nearest Class 1 area, Breton Wildlife Refuge.

In January 2007, the Company submitted to the MDEQ a BART analysis to identify and assess technically feasible and cost-effective air pollution control equipment which could be used to retrofit the existing sulfuric acid plants. Based upon the BART analysis, the Company identified no cost-effective air pollution control equipment which satisfied the BART requirements. After extensive review, the MDEQ agreed with the Company's BART assessment; however, in January 2008, the EPA requested that the Company reconsider its BART assessment to evaluate the use of cesium catalysts to replace the current catalysts.

In October 2008, the Company submitted to the MDEQ a construction permit application to replace and upgrade existing equipment in the sulfuric acid plant to increase reliability of the existing plants. As part of this construction permit, the Company submitted a revised BART analysis, which called for the replacement of a portion of the current catalyst with cesium catalyst. The supporting air modeling demonstrated that replacement of the catalyst would reduce yearly sulfur dioxide emissions from 1,992 tons per year to approximately 1,700 tons per year and would satisfy the BART regulations. The United States Fish and Wildlife Department which manages the Breton Wildlife Refuge has approved the proposed construction permit. The MDEQ and the EPA are continuing their evaluation of the proposed construction permit. Once the permit application is approved, the Company would have until the end of 2012 to replace the existing catalyst with cesium catalyst. The Company estimates that the cost for replacement of the catalysts is $2,200.

(g) National Pollutant Discharge Elimination System (NPDES) Permit Violations from 2000-2004

Operations from 2000 through 2004 resulted in numerous violations of the Company's NPDES (wastewater) permits. Most of these violations are attributable to the contemporaneous operation of two phosphogypsum disposal facilities. After closure of the West disposal facility, the frequency and degree of permit violations materially declined.

By Agreed Order dated January 31, 2008, as discussed above, the Company agreed with the MDEQ to resolve all NPDES permit violations from January 1, 2000 to January 31, 2008.

The terms of the settlement called for a monetary penalty in the amount of $950, of which $550 was paid directly to the MDEQ. The remaining $400 was paid to the Jackson County Utility Authority (the Authority) to establish a trust fund to assist the Authority with the costs associated with connecting low-to-moderate income residents in Jackson County, Mississippi, to the regional sewer system. The Company recorded this penalty of $950 as a component of selling, general and administrative expenses in its 2007 consolidated statement of operations.

(h) Contractor Litigation

In July 2007, the internals (boiler tubes and tube sheets) of the boiler in one of the Company's two sulfuric acid plants reached the end of their useful lives. The Company hired a contractor to assemble and install the replacement components of the boiler. The installation and replacement of the components required a number of repairs and unexpected downtime at the sulfuric acid plant. In the fourth quarter of 2007, the Company filed a lawsuit against the contractor and one of its subcontractors asserting negligence in replacing and repairing the boiler components and breach of contract which led to lost profits and unexpected downtime suffered by the Company. The Company is seeking in excess of $17,000 in damages from the contractor and subcontractor. The contractor has counterclaimed against the Company for $872 for amounts allegedly owed by the Company for work performed. Discovery has now concluded, several dispositive motions have been filed and are being briefed, and the matter is currently set for trial in September 2009.

(Dollars in thousands unless otherwise indicated)

Subsequent to December 31, 2008, the Company received $1,500 from its insurance carrier related to this claim.

(i) Other

Additionally, the Company, in the ordinary course of its business, is the subject of, or party to, various pending or threatened legal actions. The Company believes that any ultimate liability arising from these actions will not have a material impact on the financial position or operating results of the Company.

(19) Hurricane Katrina

On August 29, 2005, Hurricane Katrina made landfall and damaged certain of the Company's assets and disrupted the Company's operations. Effective as of March 30, 2007, the Company and its insurers agreed to a $55,200 global settlement of the Company's claims related to the storm. The following is a schedule showing the Company's hurricane-related expenses, insurance proceeds, and related net gain:

		Years ended December 31,	
		2007	2006
Beginning balance - advances (receivable) from insurance companies, net	$	23,484	(8,326)
Hurricane-related expenses		—	(1,483)
Insurance proceeds		14,346	33,293
Recognition of hurricane related gain		(37,830)	—
Ending balance - advances (receivable) from insurance companies, net	$	—	23,484

For consolidated statement of cash flow purposes, the Company estimated the components of the insurance proceeds attributable to operating activities and investing activities based on the nature of the insurance claims filed, the related insurance policy deductibles, and the factors influencing the negotiation of the final insurance settlement.