



**Usina Caeté S/A**

Financial statements  
December 31, 2008 and 2007



## Usina Caeté S/A

### Financial statements

**December 31, 2008 and 2007**

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## Independent auditors' report

To  
The Shareholders  
Usina Caeté S/A  
Maceió - AL

1. We have examined the balance sheets of Usina Caeté S/A, as of December 31, 2008 and 2007, and the related statements of income, changes in shareholders' equity and changes in cash flows for the years then ended, which are the responsibility of its management. Our responsibility is to express an opinion on these financial statements.
2. Our examinations were conducted in accordance with auditing standards generally accepted in Brazil and included: (a) planning of the audit work, considering the materiality of the balances, the volume of transactions and the accounting systems and internal accounting controls of the Company; (b) verification, on a test basis, of the evidence and records which support the amounts and accounting information disclosed; and (c) evaluation of the most significant accounting policies and estimates adopted by Company management as well as the presentation of the financial statements taken as a whole.
3. In our opinion, the aforementioned financial statements present fairly in all material respects, the financial position of Usina Caeté S/A as of December 31, 2008 and 2007, and the results of its operations, changes in shareholders' equity and changes in its cash flows for the years then ended, in conformity with accounting practices adopted in Brazil.
4. The Company has not yet held the Ordinary and Extraordinary General Meeting, with the purpose of, among other matters, deciding to the accounts of the management, examining, discussing and voting the financial statements for the year ended December 31, 2007, on the result of the year 2007 and the proposal for capital increase, in non-compliance with the articles 132 and 134 of the Brazilian Corporation Law.



5. Previously, we have examined the financial statements of the Usina Caeté for the year ended December 31, 2007, including the balance sheet and the related statements of income, changes in shareholders' equity and changes in financial position for the year then ended, on which we issued an unqualified opinion dated on March 16, 2008, containing a paragraph relating to the issue mentioned in paragraph 4 applicable for the financial statements for the year ended December 31, 2006, issued solved with ordinary and extraordinary meeting on May 27, 2008. As mentioned in note 2, accounting practices adopted in Brazil were altered as of January 1, 2008. The financial statements for the year ended December 31, 2007, presented together with the financial statements of 2008, were prepared in accordance with accounting practices adopted in Brazil in force until December 31, 2007 and, as allowed by Technical Pronouncement CPC 13 - Initial Adoption of Law 11638/07 and of Provisional Measure 449/08, are not being re-submitted with the adjustments for purposes of comparison between the years.
6. The statement of cash flows corresponding to the year ended December 31, 2007, prepared in connection with the financial statements of the year 2008, was submitted to the same audit procedures described in paragraph 2 and, in our opinion, this statement is fairly presented in all material respects, in relation to the financial statements mentioned in paragraph 5, taken as a whole.

May 16, 2008

KPMG Auditores Independentes  
CRC 2SP014428/O-6 – F – SC - AL

**Claudio José BIASON**  
**Accountant CRC-1SP144806/O-7- AL**

## Usina Caeté S/A

### Balance sheets

December 31, 2008 and 2007

(In thousand of reais)

Assets	Note	2008	2007	Liabilities	Note	2008	2007
<b>Current assets</b>				<b>Current liabilities</b>			
Cash and cash equivalents	4	52,976	80,845	Accounts payable to suppliers	14	136,514	67,589
Trade accounts receivable	5	109,030	76,898	Bank loans and financing	15	344,525	195,990
Inventories	6	443,818	405,479	Salaries and charges		19,331	19,174
Advanced payments to sugar cane suppliers	7	73,816	74,467	Advances from customers	16	36,905	1,338
Other accounts receivable	10	35,328	8,887	Taxes and contributions payable	17	19,609	18,769
Recoverable taxes	8	45,070	18,941	Other accounts payable		6,770	817
Derivative financial instruments	23	4,382	-	Derivative financial instruments	23	171,500	-
Deferred income and social contribution taxes	19	59,486	-	Deferred income and social contribution taxes	19	1,490	-
		<u>823,906</u>	<u>665,517</u>			<u>736,644</u>	<u>303,677</u>
<b>Non current</b>				<b>Non current</b>			
Judicial deposits and other		8,812	7,814	Related parties	9	4,520	8,795
Advanced payments to sugar cane suppliers	7	8,916	13,711	Taxes and contributions payable	17	68,649	56,569
Recoverable taxes	8	21,680	17,430	Taxes and contributions	18	199,549	225,073
Other accounts receivable	10	968	17,602	Deferred income and social contribution taxes	19	16,097	16,829
Deferred income and social contribution taxes	19	77,938	-			<u>1,224,927</u>	<u>795,292</u>
		<u>131,766</u>	<u>70,632</u>				
<b>Investments</b>	11	16,713	17,249	<b>Shareholders' equity</b>	20		
<b>Property plant and equipment</b>	12	1,426,855	1,247,650 (*)	Capital		560,000	538,062
<b>Intangible</b>		2,188	1,430 (*)	Capital reserves		-	12,484
<b>Deferred charges</b>	13	10,166	3,608	Revaluation reserve		306,509	307,931
		<u>1,455,922</u>	<u>1,269,937</u>	Revenue reserves		8,987	14,445
		<u>2,411,594</u>	<u>2,006,086</u>	Retained earnings (accumulated losses)		(425,473)	34,195
						<u>450,023</u>	<u>907,117</u>
						<u>2,411,594</u>	<u>2,006,086</u>

(\*) Reclassified balances to allow a better presentation of the financial statements

See accompanying notes to the financial statements

# Usina Caeté S/A

## Statements of income

Years ended December 31, 2008 and 2007

(In thousand of reais)

	Note	2008	2007
<b>Gross income</b>			
<b>Sale of goods and services</b>			
Domestic market		460,093	537,319
Foreign market		622,201	446,612
Services rendered		<u>2,616</u>	<u>5,969</u>
		1,084,910	989,900
<b>Deductions</b>			
Sales taxes		(77,564)	(97,316)
Returns and discounts		<u>(3,411)</u>	<u>(3,101)</u>
<b>Net revenues</b>		<u>1,003,935</u>	<u>889,483</u>
<b>Cost of goods and services sold</b>		<u>(846,491)</u>	<u>(710,733)</u>
<b>Gross profit</b>		157,444	178,750
<b>Operating (expenses) income</b>			
Selling expenses		(93,849)	(85,206)
Administrative and general expenses		(61,442)	(52,321)
Net financial	21	(632,873)	2,764
Equity in net income of subsidiaries and group companies	11	(561)	(1,591)
Other operating income (expense)	22	<u>32,786</u>	<u>(187)</u>
		<u>(755,939)</u>	<u>(136,541)</u>
<b>Net (loss) income before income and social contribution taxes</b>		<u>(598,495)</u>	<u>42,209</u>
<b>Income and social contribution taxes</b>	19	<u>139,223</u>	<u>(14,738)</u>
<b>Net (loss) income for the year</b>		<u>(459,272)</u>	<u>27,471</u>
<b>Net (loss) income per lot of thousand shares - R\$</b>		<u>(32.14)</u>	<u>1.92</u>
<b>Number of shares at year-end</b>		<u>14,291</u>	<u>14,291</u>

(\*) Reclassified balances to allow a better presentation of the financial statements

See accompanying notes to the financial statements

Usina Caeté S/A

Statements of changes in shareholders' equity

Years ended December 31, 2008 and 2007

(In thousand of Reais)

	Capital	Capital reserves	Revaluation reserves	Revenue reserves	Retained earnings (accumulated losses)	Total
<b>Balances at January 1, 2006</b>	530,000	19,503	327,312	5,458	(130,016)	752,257
Capital reduction	(3,694)					(3,694)
Capital increase	11,756	(11,756)				-
Reversal of part of 2005 revaluation reserve unduly recognized			(16,537)			(16,537)
Realization of revaluation reserve			(1,422)		1,422	-
Adjustment of 2003 capital reserve arising from income tax exemption incentive		(7,747)			7,747	-
Prior year adjustments					(651)	(651)
Capital reserve arising from income tax exemption incentive		12,484				12,484
Net income for the year					152,270	152,270
Distributions:						
Legal reserve				7,613	(7,613)	-
Proposed dividends					(10,000)	(10,000)
<b>Balances at December 31, 2006</b>	538,062	12,484	309,353	13,071	13,159	886,129
Realization of revaluation reserve			(1,422)		1,422	-
Prior year adjustments					1,017	1,017
Net income for the year					27,471	27,471
Distributions:						
Legal reserve				1,374	(1,374)	-
Proposed dividends					(7,500)	(7,500)
<b>Balances at December 31, 2007</b>	538,062	12,484	307,931	14,445	34,195	907,117
Adjustments to the initial adoption of Law 11638/07 and provisional measure 449/08 (note 3.1)					4,963	4,963
Capital increase	21,938	(12,484)	-	(5,458)	(3,996)	-
Prior years adjustments					(2,785)	(2,785)
Realization of revaluation reserve			(1,422)		1,422	-
Net loss fo the year					(459,272)	(459,272)
<b>Balances at December 31, 2008</b>	<u>560,000</u>	<u>-</u>	<u>306,509</u>	<u>8,987</u>	<u>(425,473)</u>	<u>450,023</u>

See accompanying notes to the financial statements.

# Usina Caeté S/A

## Statements of cash flows - Indirect Method

Years ended December 31, 2008 and 2007

(In thousand of reais)

	<b>2008</b>	<b>2007</b>
<b>Operational activities</b>		
Net (loss) income for the year	(459,272)	27,471
<b>Adjustments to reconcile net income (loss) to available generated by operating activities:</b>		
Depreciation and amortization	170,283	182,156
Residual value of written-off property, plant and equipment	4,569	835
Deferred income and social contribution taxes	(136,666)	(733)
Interest and exchange variation	409,113	2,633
Derivative financial instruments	167,118	-
Reversal of taxes and contributions sub judice	(20,011)	(4,098)
Equity in net income of subsidiaries and group companies	561	1,591
<b>Changes in assets and liabilities</b>		
(Increase) in inventories	(38,339)	(38,006)
(Increase) decrease in advances to sugar cane suppliers	5,446	(25,492)
(Increase) decrease in accounts receivable	(9,807)	20,106
(Increase) in recoverable taxes	(30,379)	(6,224)
(Increase) in judicial deposits and others	(998)	(641)
Increase (decrease) in accounts payable to suppliers	68,925	(24,929)
Increase in salaries and changes	157	2,488
Increase (decrease) in advances from customers	35,567	(13,216)
Increase in taxes and contributions	12,920	743
(Decrease) in income and social contributions taxes	-	(6,137)
Increase in other accounts payable	5,953	32
(Decrease) in taxes and contributions sub judice	(15,499)	-
Adjustment to the initial adoption of Law 11638/07 and provisional measure 449/08	4,963	-
<b>Cash and cash equivalents provided by operating activities</b>	<u>142,472</u>	<u>125,365</u>
<b>Investment activities</b>		
Acquisition of investment	(25)	-
Acquisition of property plant and equipment	(352,472)	(352,541)
Acquisition of intangible	(1,237)	(15)
Acquisition of deferred charges	(7,664)	(1,721)
Loans to related parties	(11,275)	(13,339)
Receipt from loans to related parties	11,928	769
<b>Cash and cash equivalents invested in investment activities</b>	<u>(360,745)</u>	<u>(366,847)</u>
<b>Financing activities</b>		
Prior year adjustments	(2,785)	1,017
Dividends paid	-	(7,500)
Payment of loans and financing/interest paid	(50,921)	(220,406)
Loans and financing borrowed	248,415	493,025
Loans from related parties	5,527	9,950
Payment of loans from related parties	(9,832)	(8,742)
<b>Cash and cash equivalent provided by financing activities</b>	<u>190,404</u>	<u>267,344</u>
<b>Increase (decrease) in cash and cash equivalents</b>	<u>(27,869)</u>	<u>25,862</u>
<b>Statement of increase (decrease) of cash and cash equivalents</b>		
Cash and cash equivalents in the beginning of the year	80,845	54,983
Cash and cash equivalents in the ending of the year	<u>52,976</u>	<u>80,845</u>
<b>Increase (decrease) in cash an cash equivalents</b>	<u>(27,869)</u>	<u>25,862</u>

See the accompanying notes to the financial statements

# Usina Caeté S/A

## Notes to the financial statements

### Years ended December 31, 2008 and 2007

*(In thousand of reais)*

#### 1 Operations

The Company's business purpose is the processing of sugarcane and its industrial by-products, the production and trade of electric energy, the trade of its products in the domestic and foreign markets and interest in other companies. The main processing activity is the production of demerara sugar, crystal sugar, anhydride alcohol and hydrated alcohol. Most of the raw material consumed (sugarcane) is of company production.

Nowadays the Company's productive process is concentrated at 5 plants, with three located in the State of Alagoas and two in the State of Minas Gerais.

According to the Group's strategic planning, in 2007 the Company started a project for the construction of a new industrial unit located in the municipal district of Paulicéia, State of São Paulo, called Usina Caeté S/A - Filial Paulicéia, whereas by December 31, 2008 the company had already made investments in the amount of R\$ 273 million in acquisition of industrial machinery, agricultural implements, generation of energy and expansion of sugarcane plantations and other pre-operating investments. Project go-live is scheduled to occur in the harvest of 2010/2011 with initial milling of 2.0 million tons of sugarcane. In the 2008/2009 harvest the Unit processed 63,000 tons of sugarcane through third parties and sold 1,200,000 tons at other companies from the region. The forecast for the next harvest, of 2009/2010, is for sales of approximately 1,500,000 tons of sugarcane.

#### ***Loss for the year 2008***

Usina Caeté S. A. recorded net loss of R\$ 459,272 in the year 2008 against net income of R\$ 27,471 in 2007. The Company's net loss was influenced mainly by the:

- non-cash impact of approximately R\$ 203,000 of the devaluation of the Brazilian Real in relation to the US Dollar, on foreign currency debts, which represent approximately 62.67% of the total debt.
- non-cash impact of the recognition of derivatives net of R\$ 167,118.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### **2 Presentation of the financial statements**

The Company financial statements were prepared in accordance with accounting practices adopted in Brazil, which are derived from the Brazilian Corporation Law, pronouncements, guidelines and interpretation of the Accounting Pronouncements Committee (CPC), and Federal Accounting Council (CRC).

For the first time when preparing the financial statements for 2008, the Company adopted the amendments to the Corporate Law introduced by Law 11638, which was approved on December 28, 2007 with the respective changes introduced by Provisional Measure 449 on December 3, 2008.

Law 11638/07 and Provisional Measure 449/08 amended Law 6404/76 with respect to the preparation and disclosure of the financial statements.

The adjustments with respect to the initial adoption of Law 11638/07 and Provisional Measure 449/08 are described in detail in Note 3.

### **3 Description of significant accounting policies**

#### ***3.1 Initial adoption of Law 11638/07***

The company elected to prepare a transitional balance sheet on January 1, 2008 which will determine the beginning balances for the accounting in accordance with the Corporate Law amended by Law 11638/07 and Provisional Measure 449/08. The amendments introduced by the aforementioned legislation are defined as changes in accounting practices, however, as permitted by CPC Technical Pronouncement 13 - Initial Adoption of Law 11638/07 and Provisional Measure 449/08, approved by CRC Resolution n° 1.152 of January 23, 2009, all the adjustments that would impact net income/loss of previous years can to be recorded against accumulated profits on the date of transition in the terms of article 186 of Law 6404/76, without retroactive application on the financial statements.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

As a result of the amendments to Law 6404/76, some of the balances for 2007 were reclassified to enable a comparison with the financial statements for 2008. The reclassifications that were made have no impact on net income/loss or shareholders' equity for 2007.

The reclassifications are described below:

- Reclassification of some intangible assets in the amount of R\$ 1,430 from property, plant and equipment to specified account of intangible assets.
- Reclassification of the balance of non-operating income in the amount of 1,539 (revenue) to other operating income/expenses.

The equity adjustments arising from the initial adoption of Law 11638/07 and Provisional Measure 449/08, the summary of the accounting practices changed by the aforementioned legislation and the summary of the effects on net losses for 2008 and on shareholders' equity as of December 31, 2008, resulting from the adoption of the aforementioned legislation, are presented below.

### ***3.1.1 Adjustments to the Balance Sheet on the Transition Date, January 1, 2008, due to the initial adoption of Law 11638/07 and Provisional Measure 449/08***

	12/31/07 - Balances	Date of transition - 01/01/2008	
		Adjustments	Balances
Shareholders' equity	<u>907,117</u>	<u>4,963</u>	<u>912,080</u>
Capital	538,062	-	538,062
Capital reserves	12,484	-	12,484
Revaluation reserve	307,931	-	307,931
Profit reserves	14,445	-	14,445
Retained earnings	34,195	4,963	{ a } 39,158

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### Summary of the adjustments

{a} Adjustments in retained earnings	4,963
{a1} Financial instruments stated at fair values through profit as loss	7,520
{a2} Temporary differences for income and social contribution taxes	(2,557)

### *Summary of the accounting practices changed by the initial adoption of Law 11638/07 and Provisional Measure 449/08.*

#### *Financial instruments*

The Company held financial instruments whose balances on the transition date were reclassified as financial assets or liabilities measured at fair value through the profit or loss.

As a result of the reclassification the adjustments of the initial adoption of Law 11.638/07 and Provision Measure 449/08 approved by resolution n° 1.152 of Federal Accounting Council dated on January 23, 2009 refers to the fair value of financial instruments, as well as the effects in the income and social contribution taxes as follows:

	Carrying value (A)	Fair value (B)	Difference (B) - (A)
<b>Financial instruments</b>		<u>7,520</u>	<u>7,520</u>
Target Forward Operations	-	3,316	3,316
Non-Deliverable Forwards	-	4,204	4,204

The difference between the carrying value and the fair value of the financial instruments available for sale was allocated to the balance of retained earnings on the date of transition.

The operations with derivative financial instruments in 2007 were stated in the balance sheet at their accrual basis on the balance sheet date.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### *Adjustments to present value*

The CPC Technical Pronouncement 12 establish the requirements to be observed when adjustment to present value to measure noncurrent assets and liabilities in consequence of transactions of long term and relevant transactions of short term. No long term or significant short terms were identified to recognize adjustments to present value.

### *Disclosure of related parties*

The Company increased the disclosure of transactions and balances with related parties, in notes to the financial statements, as determined by CPC technical pronouncement 05.

### *Deferred charges*

The balance of deferred charges as of December 31, 2008 will be maintained until they are fully realized through amortization or write-off against income.

### *Intangible assets*

Certain intangible assets which were already recognized prior to the initial adoption of Law 11638/07 and Provisional Measure 449/08 and which meet the specific requirements of CPC Technical Pronouncement 04 - Intangible Assets, approved by CRC Resolution 1.139, were reclassified from property, plant and equipment to intangible assets.

### *Revaluation reserve*

The balance of the Company's revaluation reserve will be maintained until its realization through depreciation expense, sale or write-off to loss.

The possibility of voluntarily revaluation of assets was eliminated beginning in 2008 with the amendments introduced in Brazilian Corporate Law.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### *Non-operating income and expenses*

Non-operating income and expenses were eliminated as of the year 2009, due to the amendment of Law 6404/76 by Provisional Measure 449/08. Nevertheless, the balances existing on March 31, 2009 and 2008 originating from the sale and write-off of assets of s permanent nature were reclassified to other operating income and expenses.

### *Effects of the initial adoption of Law 11638/07 and Provisional Measure 449/08*

The reconciliation of net income/loss for 2008 and shareholders' equity as of December 31, 2008 that reflect the effects of the initial adoption of Law 11638/07, with the results that would be obtained if the changes in accounting practices with respect to the aforementioned legislation had not been adopted, is as follows.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### Statement of the effects in income/loss and Shareholders' Equity as of and for the year ending December 31, 2008 arising from the Initial Adoption of Law 11638/07 and Provisional Measure 449/08

	<b>2008</b>
	(459,272 )
Loss for the year ended December 31	
Adjustments of the effects arising from the initial adoption of Law 11638/07 and Provisional Measure 449/08	
Financial instruments stated at fair value through profit or loss	174,639
Temporary and differences for income tax and social contribution on net income (34%)	( 59,377)
	<u>(344,010)</u>
Net (loss) without the effects of Law 11638/07 (Net adjusted result)	
	<u>(115,262)</u>
Total net adjustments arising from the adoption of Law 11638/07 and Provisional Measure 449/08	
	<b>2008</b>
Shareholders' equity at December 31	450,023
Adjustments on the date of transition recognized in	
Retained earnings and accumulated losses	(4,963)
Difference between net income/loss for 2008 and the adjusted net income/loss	<u>115,262</u>
Shareholders' equity at December 31, 2008 without the effects of Law 11638/07 and Provisional Measure 449/08	560,322

The tax effects of the adjustments arising from the initial adoption of Law 11638/07 and Provisional Measure 449/08, when applicable, were recorded in Shareholders' equity against deferred tax assets or liabilities.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### **3.2 Description of significant accounting policies**

#### *Income Statement*

Income and expenses are recognized on the accrual basis.

Revenue from the sale of goods is recognized in the income statement when the significant risks and rewards of ownership have been transferred to the buyer. Revenue from services rendered is recognized in the income statement in proportion to the stage of completion of the service. Revenue is not recognized if there are significant uncertainties as to its realization.

#### *Accounting estimates*

The accounting estimates were established on objective and subjective factors, based on management's opinion of the appropriate amount to be recorded in the financial statements. Significant items subject to these estimates and assumptions include the residual value of property, plant and equipment, allowance for doubtful accounts, inventories, deferred income tax assets, provision for contingencies, valuation of derivative instruments, and assets and liabilities related to employees' benefits. The settlement of transactions involving these estimates may result in significantly different amounts due to the lack of precision inherent to the process of their determination. The Company reviews the estimates and assumptions at least once a year.

#### *Financial instruments*

Non-derivative financial instruments include cash and cash equivalents, accounts receivable and other receivables, loans and financing, and accounts payable and other debts.

Non-derivative financial instruments are initially recognized at fair value plus, for instruments that are not stated at fair value through profit or loss, any directly attributable transaction costs.

After their initial recognition, non derivative financial instruments are recognized as follows.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### *Instruments held to maturity*

If the Companies have the positive intention and capacity to hold its debt instruments to maturity, these are classified as held to maturity. Investments held to maturity are measured by the amortized cost using the effective interest rate method, deducting any reductions in their recoverable value.

### *Financial instruments at fair value through profit or loss*

An instrument is classified by fair value through profit or loss if it is held for trading, that is, stated as such when initially recognized. Financial instruments are stated at fair value through profit or loss if the Companies manage these investments and make decisions on investment and redemption based on fair value according the strategy of investment and risk management documented by the Companies. After the initial recognition, the attributable transaction costs are recognized in income (loss) when incurred. Financial instruments at fair value through profit or loss are measured at fair value, and their fluctuations are recognized in profit or loss.

### *Other*

Other non-derivative financial instruments measured at amortized cost using the effective interest rate method, reduced by any reductions in the recoverable amount.

### *Derivative financial instruments*

Derivatives are initially recognized at fair value; Attributable transaction costs are recognized in profit or loss when incurred. After the initial recognition, derivatives are measured at fair value and changes are accounted for in profit or loss, except for operations of hedge as described bellow.

### *Foreign currency*

Management of the Company defined that its functional currency is the Real, according the standards described in the Technical Pronouncement CPC 02 - Effects of Changes in Exchange Rates and Conversion of Financial Statements, approved by CFC Resolution 1120.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

Transactions in foreign currency, that is, all of those that are not carried out in functional currency, are converted by the exchange rate of the dates of each transaction. Monetary assets and liabilities denominated in foreign currency were translated into currency functional at the foreign exchange rate prevailing at the balance sheet date. Gains and losses and exchange rate variations on monetary assets and liabilities are recognized in the statement of income (loss).

### *Current and non-current assets*

#### *Trade accounts receivable*

Accounts receivable from customers are recorded by the billed amount including the related sales taxes. The provision for doubtful accounts was calculated at an amount considered adequate by management to cover any losses arising on collection of accounts receivable.

#### *Inventories*

Inventories are stated at the lower of average acquisition or production cost, less a provision for losses or market value.

The cost of inventories includes expenditure incurred in acquiring the inventories and bringing them to their existing location and condition. In the case of finished goods, cost includes an appropriate share of overheads based on normal operating capacity.

The cultivation tracts for sugarcane plantations refer to maintenance costs, to be appropriated to the cost of the next crop.

#### *Investments*

Investments in subsidiaries and associated companies where there is an interest in the voting capital of more than 20% were valued using the equity method.

Other investments were valued at cost, less a provision for devaluation, when applicable.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### *Property, plant and equipment*

Property, plant and equipment are recorded at the cost of acquisition, formation or construction including interest and other financial charges capitalized and increased due to revaluation. Depreciation of assets is calculated by the straight-line method based on the rates mentioned in Note 12 and takes into consideration the estimated useful lives of the assets with the respective residual values.

The Company carries out the main activities of scheduled maintenance on assets from property, plant and equipment on annual bases, with the objective of inspecting and replacing components. The main annual maintenance costs include costs of labor, materials, outsourced services and overhead allocated during the off-season period.

The Company records annual maintenance costs according to “Technical Instruction 01/2006”, issued by the Institute of Independent Auditors of Brazil - IBRACON. These costs are recorded as property, plant and equipment components and depreciated in keeping with the expectation of benefit generation, generally in the following harvest. The costs of normal periodic maintenance are accounted for in expenses when incurred as the replaced components do not improve or maintain the production capacity of the asset or introduce refinements in the equipment. The loss of economic substance of long-term assets is recognized when events or changes in circumstances occur.

### *Intangible assets*

Intangible assets acquired from third parties are measured at the total acquisition cost, minus amortization expenses.

Intangible assets with a refined useful life are amortized using straight-line method over a period of 5 years.

### *Deferred charges*

Refers to pre-operating expenses and to the Company's restructuring expenditures.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

Deferred charges are recorded at purchase and formation cost, less amortization, which is calculated by the straight-line method at rates that consider the useful life of the intangible assets. Deferred charges are recognized only when there is an increase in the economic benefit related to those assets.

The Company elected to maintain the deferred charges until they are fully realized through amortization on write-off in the statement of income.

### *Impairment*

Property, plant and equipment and intangible assets have their severable value tested, at least on an annual basis, in case there are impairment indications.

### *Current and non-current liabilities*

Current and non-current liabilities are stated at known or calculable amounts, plus, when applicable, the corresponding charges, monetary and/or exchange variations incurred through the balance sheet date.

### *Provisions*

A provision is recognized in the balance sheet when the Company has a legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are recorded considering the best estimates of the risk specific to the liability.

### *Income and social contribution taxes*

The income and social contribution taxes of the Company, both current and deferred, are calculated based on the rates of 15% plus a surcharge of 10% on taxable income in excess of R\$ 240 for income tax and 9% on taxable income for social contribution on net income, and consider the offsetting of tax loss carryforward and negative basis of social contribution limited to 30% of the annual taxable income.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

The Company enjoys the fiscal incentive of exemption of income tax levied on earnings from exploration at its three units located in the State of Alagoas.

The deferred tax assets resulting from carryforward tax losses, negative basis of social contribution and temporary differences were recorded in accordance with CFC Resolution 998/04, and consider past profitability and expectations of future taxable income, based on a technical viability study approved by Management bodies.

The Company should opt for the Transition Tax Regime (RTT), pursuant to Provisional Measure nº 449/08, an option exercise that should be expressed, irreversibly, in the Corporate Income Tax Return of 2009.

### *Environmental aspects*

The production facilities of the Company are subject to environmental regulations. The Company reduces the risks associated with environmental matters, by operational procedures and controls and investments in pollution control equipment and systems. The Company believes that no allowance for loss relating to environmental matters is required at present, based on the current laws and regulations in force.

## **4 Cash and cash equivalents**

	<b>2009</b>	<b>2008</b>
Cash and bank deposits	29,001	29,663
Short-term investments	<u>23,975</u>	<u>51,182</u>
	<u>52,976</u>	<u>80,845</u>

Interest-earning bank deposits correspond to cash investments in Bank Deposit Certificates - CDB remunerated at rates which vary from 100 to 105% of the Interbank Deposit Certificate (CDI).

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

Interest-earning bank deposits are performed with prime institutions, to minimize the credit risk, a policy that is adopted by the Company in the management of these financial assets.

### 5 Trade accounts receivable

	<b>2008</b>	<b>2007</b>
Domestic customers	46,694	46,749
Foreign customers	<u>62,864</u>	<u>30,784</u>
	109,558	77,533
Provision for doubtful accounts	( <u>528</u> )	( <u>635</u> )
	<u>109,030</u>	<u>76,898</u>

The Company's maximum exposure to credit risk is the fair value of the abovementioned accounts receivable.

The credit risks of accounts receivable is derived from the possibility of the Company not receiving amounts resulting from sale operations. To mitigate this risk, the Company adopts the practice of analyzing in detail its customers' economic and financial condition, defining a credit limit, and following up on its outstanding positions.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### 6 Inventories

	<b>2008</b>	<b>2007</b>
Finished goods	203,512	188,511
Sugarcane plantations	208,655	189,390
Soybean agriculture	6,764	6,607
Maintenance supplies and others	<u>24,887</u>	<u>20,971</u>
	<u>443,818</u>	<u>405,479</u>

### 7 Advanced payments to sugar cane suppliers

	<b>2008</b>	<b>2007</b>
Advances to suppliers	<u>82,732</u>	<u>88,178</u>
Current	<u>(73,816)</u>	<u>(74,467)</u>
Non-current	<u>8,916</u>	<u>13,711</u>

Refers to advances for delivery of sugarcane that will be offset upon the conclusion of the harvest with the balances of supply of sugarcane.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

The estimates of realization of non-current assets are foreseen for the following harvests:

<b>Harvest</b>	<b>2008</b>
2010/2011	2,092
2011/2012	1,529
2012/2013	1,588
2013/2014	1,886
2014/2015	1,089
Others harvest	<u>732</u>
	<u>8,916</u>

### 8 Recoverable taxes

	<b>2008</b>		<b>2007</b>	
	<b>Current assets</b>	<b>Non-current assets</b>	<b>Current assets</b>	<b>Non-current assets</b>
Income and social contribution tax	13,792	-	5,847	-
Value added tax – ICMS	14,734	9,461	7,302	5,518
Excise tax credit – IPI	-	3,405	-	3,098
Employees' Profit Participation Program – PIS	2,953	-	781	-
Social contribution for social security financing - COFINS	13,584	-	5,005	-
Social security contribution – INSS	-	8,814	-	8,814
Other	<u>7</u>	<u>-</u>	<u>6</u>	<u>-</u>
	<u>45,070</u>	<u>21,680</u>	<u>18,941</u>	<u>17,430</u>

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

The excise tax - IPI credit recoverable is being recognized based on court discussions, starting from the fiscal credit taken in the respective tax book.

### **9 Related parties**

The main balances of assets and liabilities as of December 31, 2008 and 2007, as well as the transactions that influenced the income for the years, related to operations with related parties, result from transactions between Usina Caeté S/A and its subsidiaries and associated companies, which were performed under normal market conditions for similar types of operations.

- The associated company SOTAN - Sociedade de Táxi Aéreo do Nordeste Ltda., renders air transport services to the Company. The total expenditure with these services was R\$ 6,122 in the year 2008 (R\$ 3,397 in 2007).
- The balance with Varrela Pecuária Ltda. Refers to a loan without incidence of financial charges, with no date established for its settlement.
- The balances with Empresa Futura Agropecuária Ltda refer to the amount of initial costs related to the development of the project for construction of a new production unit, which with the effective formalization of the corporate documents determining the transfer of controlling interest from Futura - Agropecuária Indústria e Comércio Ltda. to Usina Caeté S/A and to Lagense S/A Administração e Participação, was reclassified to this group.
- Fábrica da Pedra S.A. - refers to a loan without incidence of financial charges, with no date established for its settlement.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

The balances of transactions with companies from the group are kept at historic amounts and shown as follows:

	2008		2007	
	Assets non-current	Liabilities non-current	Assets non-current	Liabilities non-current
Lagense S.A.	-	4,202	-	8,795
Sotan Ltda.	-	318	773	-
Varrela Pecuária Ltda.	6,613	-	4,041	-
Futura Agropecuária Ltda	4,033	-	9,261	-
Fábrica da Pedra S.A.	<u>2,806</u>	<u>-</u>	<u>-</u>	<u>-</u>
	<u>13,452</u>	<u>4,520</u>	<u>14,075</u>	<u>8,795</u>

### 10 Others account receivables

	2008	2007
Road paving and improvements recoverable from the Minas Gerais State Government (I)	19,263	16,855
Advances for suppliers (II)	13,635	5,303
Others	<u>3,398</u>	<u>4,331</u>
	36,296	26,489
Current asset	<u>(35,328)</u>	<u>(8,887)</u>
Non current assets	<u>968</u>	<u>17,602</u>

(I) Balance refers to the construction of roads, where due to the project launched by the government called PPP (Public Private Partnership) the Company is reimbursed for the amounts spent on the construction work according to the revenue generated for the government through ICMS payable.

(II) Consists of an advance payment made to the suppliers of services, materials for maintenance on the industrial, agricultural and commercial facilities, given the peculiarities of said activities.

# Usina Caeté S/A

(In thousand of reais)

## 11 Investments

	2008				2007			
	SOTAN – Sociedade de Táxi Aéreo do Nordeste Ltda.(*)	Varrela Pecuária Ltda.(*)	Futura Agropecuária Ltda.(*)	Total	SOTAN – Sociedade de Táxi Aéreo do Nordeste Ltda.(*)	Varrela Pecuária Ltda.(*)	Futura Agropecuária Ltda.(*)	Total
Capital	24,500	12,400	10		24,500	12,400	10	
Number of shares/quotas	1,852,809	20,000	10		1,852,809	20,000	10	
Investment interest	90.38%	16.13%	99%		90.38%	16.13%	99%	
Shareholders' equity at December 31	14,144	6,196	(15)		14,450	7,952	(30)	
Book value of investment	13,060	1,283	-	14,343	14,363	1,571	-	15,934
Equity in net income (loss) of subsidiaries and group companies	( 277)	( 284)	-	( 561)	( 1,303)	( 288)	-	( 1,591)
Adjusted book value of investments	<u>12,783</u>	<u>999</u>	<u>-</u>	<u>13,782</u>	<u>13,060</u>	<u>1,283</u>	<u>-</u>	<u>14,343</u>
Property and real state				2,342				2,342
Other investments				<u>589</u>				<u>564</u>
				<u>16,713</u>				<u>17,249</u>

(\*) Companies revised by KPMG

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### 12 Property, plant and equipment

#### a. Composition of balances

	Average depreciation rate (p.a.)	2008			2007
		Cost	Depreciation	Net	Net
Buildings and improvements	4	179,491	(35,310)	144,181	141,086
Installations	10	30,210	(14,182)	16,028	18,243
Machinery and equipment	10	459,437	(240,032)	219,405	240,503
Machinery and agricultural implements	25	59,971	(43,586)	16,385	11,621
Fixtures and fittings	10	7,296	(3,171)	4,125	3,705
Vehicles	20	83,030	(53,074)	29,956	17,866
Computers equipment	20	12,890	(7,249)	5,641	3,971
Apparels and tools	10	7,543	(4,774)	2,769	2,405
Equipment and phone apparels	20	2,636	(1,982)	654	662
Sugarcane plantation	20	513,113	(130,390)	382,723	321,352
Others		-	-	-	12
Land		418,694	-	418,694	411,443
Fixed assets in progress		122,638	-	122,638	9,924
Industry off-season maintenance costs		118,965	(97,552)	21,413	30,167
Advances to suppliers		<u>42,243</u>	<u>-</u>	<u>42,243</u>	<u>34,690</u>
		<u>2,058,157</u>	<u>(631,302)</u>	<u>1,426,855</u>	<u>1,247,650</u>

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### *b. Changes in the cost*

	2007	2008			Cost
	Cost	Additions	Write-offs	Others	
Buildings and improvements	169,463	3,142	(2,670)	9,556	179,491
Installations	29,627	260	(7)	330	30,210
Machinery and equipment	437,314	2,137	(144)	20,130	459,437
Machinery and agricultural implements	54,828	12,742	(7,592)	(7)	59,971
Fixtures and fittings	6,397	1,197	(334)	36	7,296
Vehicles	64,182	21,029	(2,190)	9	83,030
Computers equipment	10,090	2,783	(173)	190	12,890
Apparels and tools	6,752	826	(19)	(16)	7,543
Equipment and phone apparels	2,432	232	(28)	-	2,636
Sugarcane plantation	416,249	128,363	-	(31,499)	513,113
Others	51	-	(51)	-	-
Land	411,443	7,853	(602)	-	418,694
Fixed assets in progress	9,924	142,942	-	(30,228)	122,638
Industry off-season maintenance costs	97,552	21,413	-	-	118,965
Advances to suppliers	<u>34,690</u>	<u>7,553</u>	<u>-</u>	<u>-</u>	<u>42,243</u>
	<u>1,750,994</u>	<u>352,472</u>	<u>(13,810)</u>	<u>(31,499)</u>	<u>2,058,157</u>

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### 13 Deferred

	<b>2008</b>	<b>2007</b>
Preoperating expenses	17,937	10,273
Accumulated amortization	<u>(7,771)</u>	<u>(6,665)</u>
	<u>10,166</u>	<u>3,608</u>

Pre-operating expenditures, which include remuneration of employees, training and rental of equipment, refer to the deployment and expansion of Volta Grande Unit up until the time it started operating normally and to the construction project of the new industrial unit called "Filial Paulicéia". The deferred expenses of Volta Grande Unit are amortized over the period of up to ten years.

### 14 Suppliers

	<b>2008</b>	<b>2007</b>
Sugar cane suppliers	51,821	31,779
Others suppliers	<u>84,693</u>	<u>35,810</u>
	<u>136,514</u>	<u>67,589</u>

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### 15 Loans and financing

Type	Financial		2008		2007	
	Index	Average Annual Interest	Short term	Long term	Short term	Long term
Credit	R\$	8.75%	-	-	12,135	-
FAT (BNDES)	URTJLP	7.5% a 10.20%	22,511	91,123	22,714	118,663
	UMBNDDES	7.99% a 8.3955%	445	1,067	-	-
	US\$	6.1955%	1,638	4,487	-	-
Finame	URTJLP	7.5 a 11.5%	15,025	25,002	16,953	25,517
Pró Indústria	IGP-M	50% to the index	2,110	-	3,485	1,843
Resolution 2770	US\$	4.53 a 8.5%	7,325	16,396	27,313	-
Resolution 635/87	UMBNDDES	9.96%	160	794	8,856	-
Advances on Exchange Contracts	Us\$	5.72% a 6.10%	136,863	8,316	12,680	-
Working capital – Export	R\$	CDI 2.5 to 6.75%	4,576	50,889	10,149	-
Industrial credite note	R\$	8.91% to 10.12%	-	-	14,569	-
NCE – Export credit note	R\$	CDI 6.5 to 12.25%	56,743	12,376	20,138	-
NCE – Export credit note	Us\$	6.50%	1,933	55,308	8,932	5,314
Export pre-payment	Us\$	5.98% a 7.0%	40,821	498,883	23,168	315,902
Bank Credit Note	R\$	CDI 2.5 to 12.5%	30,409	108,879	10,049	20,787
Bank Credit Note	Us\$	5.95%	181	27,426	-	-
Credit note- export	CDI CETIP	12.6825%	18,845	11,402	-	-
Secured accounts	CDI CETIP	9.3872%	9	10,244	-	-
Hot Money	-	16.80%	710	-	-	-
Leasing	-	-	4,221	13,520	-	-
Rural promissory note	R\$	6.75%	-	-	4,849	-
			<u>344,525</u>	<u>936,112</u>	<u>195,990</u>	<u>488,026</u>

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

The long-term installments have the following payment schedule:

<b>Maturity:</b>	<b>2008</b>	<b>2007</b>
2009	-	65,838
2010	433,901	133,972
2011	169,922	89,507
2012	175,593	100,081
2013 a 2015	<u>156,696</u>	<u>98,628</u>
	<u>936,112</u>	<u>488,026</u>

Financings and loans are backed by collateralization of the financed assets in the amount of R\$ 470,586 (R\$ 491,562 in 2007), promissory notes and sureties from senior management and from the parent company in the amount of R\$ 223,638 (R\$ 524,637 in 2007) and products in the amount of R\$ 169,441. The other guarantees refer to real estate, mortgages, sugarcane and an energy power contract that amount to R\$ 65,706.

### 16 Advances from customers

	<b>2008</b>	<b>2007</b>
From foreign market	32,596	-
From domestic market	<u>4,309</u>	<u>1,338</u>
	<u>36,905</u>	<u>1,338</u>

Foreign market advances are comprised of amounts advanced by clients in foreign currency for acquisition of sugar and alcohol intended for export, which are converted into the functional currency at the exchange rate of the closing date.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### 17 Taxes and contributions payable

	<b>2008</b>	<b>2007</b>
INSS	3,226	3,884
FGTS	1,962	1,812
IRRF	1,420	968
Cofins	-	1,110
PIS	-	240
IPI	769	629
Asplana Asplamed Assist. Social	846	217
INSS sugar cane supplier	435	316
INSS – Installments	914	911
ICMS regular transactions	116	3,076
INSS – Installments TPDA 32.570.779-0	257	-
Special installments – Proc 104104525852004/11 (i)	18,347	-
Special installments (PAES) Lei 10.684/03	78	90
ICMS – Installments Decr. 2381/04 (ii)	59,095	61,124
Others	<u>793</u>	<u>961</u>
	<u>88,258</u>	<u>75,338</u>
Current	<u>(19,609)</u>	<u>(18,769)</u>
Non current	<u>68,649</u>	<u>56,569</u>

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

(i) - In 2008 the Company reclassified the special installment payment - proceeding 104104525852004/11 made in 2003 from the group of sub judice taxes and contributions in non-current liabilities to the group of taxes and contributions payable, segregating short and long term due to ratification of the debt.

(ii) - In 2005 the Company recognized the liability corresponding to the installment payment of ICMS, pursuant to the agreement signed with a basis on Decree n° 2381 of December 2004, of the Alagoas State Government, including principal and interest. The settlement of the installment payment is occurring normally and its final maturity is in January 2019.

### **18 Sub judice taxes and contributions**

The Company is a party in lawsuits and administrative proceedings before various courts and government agencies, resulting from the normal course of operations, involving tax, labor, civil and other issues.

The sums involved in these lawsuits were provisioned and partially deposited in escrow with the courts. Based on opinions of its legal advisors, the Company does not expect losses upon the conclusion of these proceedings above the amounts provisioned.

a) Based on information from its legal advisors, an analysis of the outstanding legal proceedings, and in respect of labor claims previous experience with regards to amounts claimed, the Company recorded provisions for amounts considered sufficient to cover potential losses from the current actions, as follows:

	<b>2008</b>	<b>2007</b>
INSS on director compensation	147	147
IPI – Delta Industrial Unit	4,383	4,383
Tax credits of IPI (Export Premium Credit, non-taxable and zero rate)	194,348	219,421
Other	<u>671</u>	<u>1,122</u>
	<u>199,549</u>	<u>225,073</u>

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

Based on opinions of legal consultants, the Company recognized in previous years tax credits of Excise Tax - IPI (including export premium credit, non-taxable and zero rate), which are pending court decision. In compliance with the accounting standards relating to the recognition of contingent earnings, in 2005 the Company recognized the sub-judice liabilities corresponding to the tax credits obtained in previous years.

- b) There are other processes that have been assessed by the Company's legal counsel as being a possible or remote risk of loss which cannot be determined with certainty, for which no provision has been recorded in view of the fact that the accounting practices adopted in Brazil do not require that they be recorded.
- c) Unrecorded contingent assets

The Company considers possible the realization of some contingent assets, with an emphasis on the credit in the approximate amount of R\$ 270,000 (same amount in 2007) relating to the Northeast Units, resulting from an action for damages, based on Law 4870/65, which refers to sugar production, the revenue of Instituto do Açúcar e Alcool and its application. Although the lawsuit has become final, with sentence in favor of the Company, the amount involved is still being challenged, hence the contingent earnings will only be recognized when this sentence produces its effects and there is no longer any possibility of appeals filed by the adversary party.

### **19 Income and social contribution taxes**

The deferred income and social contribution taxes are recognized to reflect future tax effects attributable to temporary differences between the tax bases of assets and liabilities and their book values.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

In accordance with CFC Resolution 998, of May 21, 2004, the Company, based on its expectation of generating future taxable income determined by a technical valuation approved by management, recognized tax credits on income tax loss carry-forwards and the negative bases of social contribution tax, with no statutory limitation period and that can be offset against a maximum of 30% of annual taxable income. The book value of deferred fiscal charges is reviewed periodically and projections are reviewed annually. If there are relevant factors that modify the projections, these are reviewed during the year by the Company. On December 31, 2008, the Company had tax loss carryforwards in the sum of R\$ 415,667 and the negative basis of accumulated social contribution of R\$ 416,376. Based on its record of profitability and on the projections of future taxable income, the Company recognizes in the year 2008 deferred income and social contribution taxes on part of these tax credits and on the temporary differences, as follows:

### a) *Deferred taxes*

	2008	2007
<b><i>Current assets:</i></b>		
Derivatives financial statements	58,310	-
Provision for doubtful accounts	<u>1,176</u>	<u>-</u>
	<u>59,486</u>	<u>-</u>
<b><i>Non current assets:</i></b>		
Provision for contingences	488	-
Income tax carryforward	56,948	-
Negative base of social contribution	<u>20,502</u>	<u>-</u>
	<u>77,938</u>	<u>-</u>
<b><i>Current liabilities:</i></b>		
Derivatives financial instruments	<u>1,490</u>	<u>-</u>
<b><i>Non current liabilities:</i></b>		
Revaluation reserve	<u>16,097</u>	<u>16,829</u>

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

Management considers that deferred charges resulting from timing differences will be realized in proportion to the final resolution of contingencies and events.

Based on the technical study of taxable income projections, the Company estimates recovering tax credit arisen out of accumulated losses in the following years:

2010	9,802
2011	10,720
2012	12,605
2013	13,554
2014 to 2016	<u>30,769</u>
	<u>77,450</u>

The expected recoverability of the tax credits is based on the projections of future taxable income taking into consideration various business and financial assumptions at year-end. Accordingly, these estimates may differ from the effective taxable income in the future due to the inherent uncertainties involving these estimates.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

The reconciliation between the tax expense as calculated by the combined statutory rates and the income and social contribution tax expense charged or credited to net income is presented below:

	<b>2008</b>	<b>2007</b>
Income (loss) before income and social contribution taxes	<u>(598,495)</u>	<u>42,209</u>
Combined statutory rates	34%	34%
Income and social contribution taxes Calculated at combined statutory rate	(203,488)	14,351
Permanent additions: Nondeductible expenses	<u>324</u>	<u>387</u>
Part of the tax loss and negative basis without formation of deferred income tax and social contribution	63,941	-
Income tax and social contribution in income for the year Effective rate	<u>(139,223)</u> -	<u>14,738</u> 34%

## 20 Shareholders' equity

### a. Capital

The subscribed and paid-in, at December 31, 2008, is of R\$ 560,000 (R\$ 538,062 in 2007), divided in 14,291 (identical in 2007) nominative ordinary shares with no par value.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### **b. Reserves**

#### *Legal reserve*

In compliance with article 193 of Law 6404/76, the reserve was recorded at the rate of 5% of the net profit for the year, up to the limit of 20% of the capital.

#### *Revaluation reserve*

The reserve was recognized as a result of the revaluations of land and buildings improvements, recorded by the Company, based on an appraisal report prepared by independent appraisers. The deferred income and social contribution tax effects over depreciable items are classified under noncurrent liabilities.

The revaluation reserve is realized in proportion to the depreciation, disposal or sale of the revalued assets, net of the related taxes.

### **c. Dividends**

The Company's bylaw determines the following destination of profits for each year, after approval by the General Ordinary Shareholders' meeting:

- amount (optional) to be approved by the shareholders' meeting as a fund for installation replacement;
- up to 10% for management bonus;
- a minimum of 25%, adjusted as determined by the Brazilian Corporate Law, for distribution of dividends to the shareholders.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

In 2007 the Company advanced a distribution of dividends on the net profit for the year as follows:

	<b>2007</b>
Net income for the year	27,471
Appropriation for legal reserve	<u>( 1,374)</u>
Base for calculation of the dividends	26,097
Statutory dividends (25%)	<u>6,524</u>
Proposed dividends	<u>7,500</u>

### 21 Net Financial

	<b>2008</b>	<b>2007</b>
<b>Financial expenses</b>		
Interest on loans, financing and taxes	(88,604)	(55,539)
Derivatives financial instruments	(414,264)	(20,877)
Monetary variation and expenses exchange variation	(204,604)	(19,323)
Other	<u>( 3,296)</u>	<u>( 3,235)</u>
	<u>(710,768)</u>	<u>(98,974)</u>
<b>Financial income</b>		
Interest on short term investment	6,937	6,512
Income exchange variation	41,579	58,352
Derivatives financial instruments	24,062	34,114
Other	<u>5,317</u>	<u>2,760</u>
	<u>77,895</u>	<u>101,738</u>
	<u>(632,873)</u>	<u>2,764</u>

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### 22 Other operating income (expense) net

	<b>2008</b>	<b>2007</b>
Other operating expenses		
Excise Tax – IPI – Credits on supply purchases	16,926	-
Credit of Pis Law 10.637/02 and COFINS Law 10.833/03	4,694	4,046
Income of fixed assets sold	10,940	1,539
Recoverable of expenses	5,901	3,049
Other income	<u>6,348</u>	<u>2,950</u>
	<u>44,809</u>	<u>11,584</u>
Other operating expenses		
Contribution of association	1,962	1,292
Fines and taxes	2,903	1,073
CPMF	73	5,794
ICMS – rate difference	1,481	2,131
IOF	2,683	8
Other income	<u>2,921</u>	<u>1,481</u>
	<u>12,023</u>	<u>11,771</u>
	<u>32,786</u>	<u>( 187)</u>

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### 23 Financial instruments

The Company carries out operations with financial instruments. The management of these instruments is done through operating strategies and internal controls, aimed at assuring liquidity, profitability and security. The contracting of financial instruments with the objective of offering protection is performed by means of a periodic analysis of the risk exposure that management intends to cover (exchange rate, interest rate, etc.), which is approved by the Board of Directors to operationalize the strategy presented. The control policy consists of permanent follow-up of the conditions engaged versus those in force in the market.

The objective of the financial policy is to determine parameters of use of financial instruments, including derivatives, which aim at the protection of operating assets and liabilities, exposed to exchange rate variation, interest and commodities, and to establish credit limits at the financial institutions.

Every transaction involving financial instruments is fully acknowledged in the accounting books and refer to instruments described below:

Description	Loans and receivable	Measured at fair value	Available for sale	Book balance/fair value
<b>Assets</b>				
Cash and cash equivalent			29,001	29,001
Short term investments			23,975	23,975
Trade accounts receivable	109,030			109,030
Other accounts receivable and advances to supplies	119,028			119,028
Related parties	13,452			13,452
Other accounts receivable	52,323			52,323
Derivatives financial instruments		4,382		4,382
<b>Liabilities</b>				
Accounts payable to supplies and others	(143,284)			(143,284)
Derivatives financial instruments		(171,500)		(171,500)
Loans and financing	(1,280,637)			(1,280,637)
Related parties	(4,520)			(4,520)

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

The following methods and assumptions were adopted in the determination of the fair value:

- Cash and cash equivalents - defined as assets intended for business transactions. The accounting values found in the balance sheet are close to the fair values due to the short-term maturity of these instruments.
- Interest earning bank deposits – The bookkeeping values of these instruments are close to their fair value by virtue of earning rates (CDBs are all indexed to the CDI variation) or short maturity.
- Accounts receivable, advances to suppliers, other accounts receivable, suppliers and other accounts payable – Balances resulting directly from Company's operations are stated at their amortized cost, less allowance for losses when applicable. The accounting values found in the balance sheet are close to the market value on the calculation date.
- Loans and Financing - stated as other financial liabilities and shown at their amortized cost. For disclosure purposes, the bookkeeping balances are equal to market values as this funding has exclusive features, originating from specific funding sources, at pre-fixed rates: TJLP - Long-term Interest Rate and CDI - Bank Deposit Certificates.
- Derivative financial instruments - the criteria for calculating the fair value of derivative financial instruments are based chiefly on their prices in active markets, or in their absence in pricing models broadly accepted by the Market and that take into account market data outside of the Company on the base date.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

The Company's transactions are subject to the risk factors listed below:

### ***Credit risk***

It results from the possibility of the Company incurring losses arising out of default of their counterparties or financial institutions depository of resources or financial investments. In order to mitigate such risks, the Company adopts as practice an analysis of the financial and equity situation of their counterparties, as well as the definition of credit limits and permanent follow-up of open positions. As regards financial institutions, the Company only conducts operations with low risk financial institutions assessed by rating agencies.

### ***Price risk of goods sold or produced or of input acquired***

It results from the possibility of market oscillation of the price of products marketed or produced by the Company and of other input used in the production process. This price oscillation may cause material alterations in Company's revenues and costs. In order to mitigate such risks, the Company permanently monitors local and international markets, trying to be ahead of price movements.

### ***Interest rate and exchange risk***

Results from the possibility of the Company suffering gains or losses arising from oscillations of interest rates levied on their financial assets and liabilities. Aiming to mitigate this type of risk, the Company seeks to diversify borrowings in terms of prefixed or post-fixed rates, and under certain circumstances contract derivative financial instrument operations, such as swaps and forward currency, as hedge, to lock the financial cost of the operations.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

### *Derivative financial instruments*

As defined in internal policy, the Company's income (loss) should come from its business cash generation and not from financial market transactions. Hence, the use of derivatives should serve the sole purpose of hedging any occasional exposure it have as a result of the risks to which it is exposed, without speculative purposes. Contracting derivatives should have an exposed asset or liability as a counterpart, whether recognized or not, with a possible effect on income of the Company, but never to leverage a position. The criteria adopted to define a reference value for derivative financial instruments are related to the value of the liability and/or the assets. The Company does not invest in financial derivatives referred to as exotic.

The purpose of derivative transactions is always related to eliminating market risks, related to our policies and guidelines, and also to managing volatile financial flows. All gains and losses arising from derivative financial instruments are stated at their market value.

The Company's management permanently monitors its derivative financial instruments through its internal controls.

The following derivative instruments are employed by the Company:

- Non-Deliverable Forwards: Over-the-counter dollar sale and/or purchase operations with future maturity, without initial cash disbursement, based on an amount in dollars (*notional*) and the future long or short rate (*strike*). Upon the maturity of the operation the result will be the difference between the contracted rate and the Ptax upon maturity, multiplied by the base value (*notional*).
- Target forward: Over-the-counter dollar sale and/or purchase operations with future maturity, without initial cash disbursement, with the following conditions: If the Ptax on the fixing *date* is below the contracted dollar (*strike*), the Company will receive the difference between the contracted dollar and Ptax, multiplied by the original base amount. There can be a limiter of earnings for the Company, when the difference between Ptax and the *strike*, over the course of the maturities, attains R\$ 0.40 on average, canceling the subsequent maturities (*Knock out*). If the dollar is above the *strike*, the Company will pay the difference between the contracted dollar and Ptax, multiplied by double the base amount.

# Usina Caeté S/A

## Notes to the financial statements

(In thousand of reais)

- **CDI rate x Dollar swap contracts:** Structured over-the-counter operation with prime financial institutions for exchange of indexes, on a base amount (notional), where the Company receives CDI at the asset leg, paying dollar variation at the liability leg.
- **Commodity options:** These are over-the-counter operations, in which the vendor (Usina Caeté) sells a given asset (sugar and alcohol) at a prefixed price. The put option grants the right to sell the asset on the date of maturity or before it, at a predetermined price (strike price), whereas the option is exercised, if the strike price is higher than the price of the target asset.

The chart below presents all the derivative financial instruments contracted, as well as the respective fair values calculated by the management of the Company on December 31, 2008.

<b>Equity protection contracts</b>	<b>Maturities</b>	<b>Reference value</b>	<b>Fair value</b>	<b>Amounts receivable</b>	<b>Amounts payable</b>
Commodity options	Jan to Dec, 2009	58,500	23,252	-	23,252
Non-Deliverable Forwards	Jan to Dec 2009	67,010	33,276	-	33,276
Target - Profit	Jan to Oct 2009	138,429	53,672	-	53,672
Dollar vs CDI swap contracts:	Jan to Dec 2009	1,674,930	56,918	4,382	61,300
				<u>-</u>	<u>-</u>
				<u>4,382</u>	<u>171,500</u>

The operations with derivatives shown above were fully settled up to the date of the independent auditors' report.

# Usina Caeté S/A

## Notes to the financial statements

*(In thousand of reais)*

### **24 Purchase commitments**

The Company has several sugarcane purchase commitments with third parties to ensure a portion of their production for the next harvesting periods. The quantity of sugarcane to be purchased is calculated based on a sugarcane harvest estimate by geographical area. The amount to be paid by the Company will be determined for each harvesting period at the end of such period.

### **25 Insurance coverage**

The Company adopts the policy of contracting insurance coverage for assets subject to risks for amounts considered to be sufficient to cover eventual casualties, considering the nature of its activity. The assumptions adopted, given their nature, are not part of the scope of an audit of financial statements and, accordingly, they were not examined by our independent auditors.

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