

EXPLANATORY MEMORANDUM

DAIRY FARMERS MILK CO-OPERATIVE LIMITED

ARBN 108 690 384

In respect of the scheme of arrangement between DFMC and DFMC Members to return capital to DFMC Members by way of a compulsory share cancellation.

THE DFMC BOARD
UNANIMOUSLY RECOMMENDS
THAT YOU VOTE “**YES**”
IN FAVOUR OF THE SCHEME.

LEGAL ADVISER


ADDISONS
— COMMERCIAL LAWYERS —

CORPORATE ADVISER

BARON

THIS DOCUMENT IS IMPORTANT AND REQUIRES YOUR IMMEDIATE ATTENTION.

If you are in any doubt as to how to deal with it please consult with either your financial, legal or other professional adviser immediately.

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Important Notices and Disclaimers

This Explanatory Memorandum is dated 1 June 2009.

PURPOSE OF THIS EXPLANATORY MEMORANDUM

This Explanatory Memorandum has been prepared to provide DFMC Members with information to explain the impact on DFMC of the proposal to return capital to DFMC Members by way of a compulsory share cancellation by scheme of arrangement between DFMC and DFMC Members under Part 13 of the Co-operatives Act. It includes all information that in the opinion of the DFMC Board is material to the making of a decision by a DFMC Member about how to vote in respect of the Scheme.

This Explanatory Memorandum comprises:

- a. the explanatory statement required to be sent to DFMC Members under Part 13 of the Co-operatives Act in connection with the Scheme; and
- b. the disclosure statement to DFMC Members for a special postal ballot pursuant to section 194 of the Co-operatives Act on the special resolution which must be passed in order for the Scheme to proceed.

In accordance with section 189(3) of the Co-operatives Act, this Explanatory Memorandum, as a whole, sets out the reasons for, and effect of, the special resolution which is proposed to implement the Scheme.

This Explanatory Memorandum has been approved by the Co-operatives Registrar under sections 194(3) and 355 of the Co-operatives Act. By approving this Explanatory Memorandum, the Co-operatives Registrar does not signify that it supports, endorses or expresses an opinion on the Scheme, or that the Scheme will be approved by the Court, should the Scheme be agreed to by DFMC Members. The Co-operatives Registrar takes no responsibility for the contents of this Explanatory Memorandum.

Co-operatives Registrar approval was obtained on or before the date of this Explanatory Memorandum and is valid for six months after the date of Co-operatives Registrar approval.

The fact that the Court has appointed a date for a hearing in relation to the proceedings commenced by DFMC for approval of the Scheme is not an endorsement of, or any other expression of opinion on, the Scheme or any other part of this Explanatory Memorandum.

DEFINITIONS

Capitalised terms used in this Explanatory Memorandum are defined in the Glossary in section 13 of this Explanatory Memorandum.

PROFESSIONAL OR INVESTMENT ADVICE

This Explanatory Memorandum is an important document and should be read in its entirety. The proposed Scheme may have important financial and

taxation consequences for individual DFMC Members. The information contained in this Explanatory Memorandum does not constitute financial product advice and has been prepared without reference to your own investment objectives, financial situation, taxation position and particular needs. Before making any investment decision and any decision as to how to vote in respect of the Scheme, or if you are in doubt as to any of the matters raised in this Explanatory Memorandum, you should consult with either your financial, legal or other professional adviser immediately.

RESPONSIBILITY FOR INFORMATION

The information contained in this Explanatory Memorandum has been prepared by DFMC and its Advisers and is the responsibility of DFMC, other than:

- The details on the Australian taxation implications to DFMC and DFMC Members of the Scheme outlined in section 11 of this Explanatory Memorandum, which has been prepared by Ernst & Young and is the responsibility of Ernst & Young (Tax Information).
- The Independent Audit Report within the financial statements contained in Schedule B of this Explanatory Memorandum which has been prepared by PricewaterhouseCoopers and is the responsibility of PricewaterhouseCoopers (Independent Audit Report).

To the maximum extent permitted by law, neither DFMC nor any of its directors, officers or Advisers (except Ernst & Young and PricewaterhouseCoopers) takes any responsibility for the accuracy or completeness of the Tax Information or the Independent Audit Report respectively.

FORWARD LOOKING STATEMENTS

This Explanatory Memorandum includes certain statements that relate to the future. Such forward looking statements are not guarantees of future events or performance and may be impacted by known and unknown risks, uncertainties, assumptions and other important factors, many of which are beyond the control of DFMC, which may cause actual performance, achievements or events to differ materially from those expressed or implied by such statements.

CURRENT INFORMATION

Unless otherwise stated, all data contained in this Explanatory Memorandum, including in charts, graphs and tables, is based on information available as at 1 June 2009. All references to “\$”, “dollar” and “cent” are references to Australian currency, unless stated otherwise.

PRIVACY AND PERSONAL INFORMATION

DFMC may collect certain personal information in connection with the Special Postal Ballot and the return of capital to DFMC Members. Such information may

Important Notices and Disclaimers

include (as applicable) the names, contact details, bank account details and shareholdings of DFMC Members, and the names of persons appointed by those persons to act as attorney or corporate representative in the Special Postal Ballot. The primary purpose of the collection of personal information is to assist DFMC to conduct the Special Postal Ballot and implement the return of capital to DFMC Members. Personal information of the type described may be disclosed, as appropriate, to the Co-operatives Registrar, print and mail service providers and to the Court.

DFMC Members have certain rights to access personal information that has been collected. DFMC Members should contact DFMC's share registry if they wish to access their personal information. DFMC Members who appoint a named person to act as their attorney or corporate representative should ensure that they inform that person of these matters.

QUESTIONS

If you have any questions in relation to the proposed Scheme or the Special Postal Ballot, please contact DFMC's Executive Officer, your local director or the DFMC share registry manager, whose contact details are contained in the DFMC Corporate Directory at the end of this Explanatory Memorandum.

What you are being sent

Together with this Explanatory Memorandum, active DFMC Members are being sent the following documents by DFMC:

- Special Postal Ballot voting paper – coloured blue (in Voting Guide).
- Postal ballot envelope (marked "Inner Envelope").
- Middle envelope (marked "Middle Envelope").
- Reply paid envelope (marked "Outer Envelope").
- Reply paid envelope (grey) (for return by corporate DFMC Members only of a corporate representative form).
- Voting Guide.

Action required

In relation to the Special Postal Ballot please:

- Read this Explanatory Memorandum. If you are in any doubt as to how to deal with it please consult with either your financial, legal or other professional adviser immediately.
- Call DFMC's Executive Officer, your local director or the DFMC share registry manager if you have any questions about the Special Postal Ballot or the Scheme.
- Cast your vote in the Special Postal Ballot and return the Special Postal Ballot paper so that it is received by 12pm (noon) (Sydney time) Tuesday 30 June 2009.

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Key Dates

The key dates in relation to the Scheme from DFMC's perspective are as follows:

EVENT	DATE
Date of this Explanatory Memorandum	Monday 1 June 2009
Special Postal Ballot closes	12pm (noon) (Sydney time) Tuesday 30 June 2009
Declaration of vote in respect of the Scheme	Tuesday 30 June 2009
Second Court Hearing Date (to approve the Scheme)	Friday 3 July 2009 at 10am
Date for cancellation of shares	Tuesday 7 July 2009
Date for dispatch of payments of capital to DFMC Members	Tuesday 7 July 2009

All dates from the Special Postal Ballot closing date are indicative only and, among other things, are subject to all necessary approvals. Any changes to the timetable will be notified through the DFMC website at www.dfmc.org.au.

References to time in this Explanatory Memorandum are references to Sydney time. Where an act is specified to be done by a particular time or date in an Australian time zone it must be done by the corresponding date or time in any other jurisdiction.

Dear DFMC Member

Distribution of the first part of the Net Proceeds from the sale of DFMC's investment in ACF to National Foods was made by payment of a special dividend of \$1.6879 per share to DFMC Members in December 2008. This represented a total of \$56.9 million (approximately).

This Explanatory Memorandum explains the proposed compulsory cancellation of DFMC Members' shares by scheme of arrangement (Scheme) to make the second payment of Net Proceeds to DFMC Members from the sale of DFMC's investment in ACF. The second payment to DFMC Members will total approximately \$22.3 million. As the Scheme involves DFMC cancelling DFMC Members' shares in return for capital, the DFMC Board is obliged by the Co-operatives Act to conduct a Special Postal Ballot to seek agreement from DFMC Members on the Scheme and then to seek approval from the Court.

The extent of each DFMC Member's participation in the Scheme will be subject to that DFMC Member retaining sufficient shares in DFMC after the cancellation to satisfy the Minimum Shareholding Requirement (as set out in section 6.2.3 of this Explanatory Memorandum). The Minimum Shareholding Requirement is essentially the same as the minimum shareholding required under Rule 23 of the DFMC Rules, except that the transitional provision which applied in respect of the 2004 ACF restructure does not apply. Subject to the Minimum Shareholding Requirement, each participating DFMC Member will have 7 out of every 10 shares held by that DFMC Member cancelled and will receive the amount paid up in respect of each cancelled share, which is \$1 per share in the case of DFMC Members (excluding those former members who have been reinstated as DFMC Members pursuant to the claim referred to in section 9 of this Explanatory Memorandum).

Under the Scheme, DFMC's capital will be reduced from approximately \$31.9 million to approximately \$9.7 million. After the return of capital to DFMC Members and on the assumption that the total amount of approximately \$6 million set aside in December 2008 to deal with the former members' claim is distributed to either DFMC Members or former members (see section 9 of this Explanatory Memorandum), DFMC will retain approximately \$21 million, split between retained earnings (approximately \$11.1 million) and share capital (approximately \$9.7 million).

The DFMC Board believes that the retention of approximately \$21 million is important because DFMC must have adequate funding to undertake its obligations under the Milk Supply Agreement and secure the position of DFMC Members. However, the DFMC Board will continually monitor the level of funding DFMC requires in the future and, if at any time it considers DFMC has surplus funds, it will seek to return those surplus funds to DFMC Members (see section 7.3.3 of this Explanatory Memorandum for more information).

THE DFMC BOARD'S RECOMMENDATION

The DFMC Board **unanimously recommends** that you vote "YES" in favour of the Scheme to return capital to DFMC Members by way of a compulsory share cancellation. Each DFMC director who is an active DFMC Member intends to vote "YES" in the Special Postal Ballot, in favour of implementation of the Scheme.

The reasons for this recommendation by the DFMC Board are briefly as follows:

- a. To ensure that DFMC's capital structure following the 7 out of 10 share cancellation does not operate as an incentive to DFMC Members to cease to supply DFMC.
- b. To reduce the inequality in absolute monetary terms between DFMC Members having regard to the services rendered to them.
- c. To reduce the liabilities on DFMC's balance sheet.
- d. To reduce the future financial risk to DFMC associated with DFMC Members becoming inactive.
- e. To provide a stable capital and financial base for DFMC Members.
- f. To return to DFMC Members capital that is not required to fund DFMC's operations.

For a further explanation of these reasons, please see section 3.2 of this Explanatory Memorandum.

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Chairman's Message

Section 11 of this Explanatory Memorandum, prepared by Ernst & Young, contains details of the Australian tax implications of the Scheme to DFMC and DFMC Members. On the assumption that the \$6 million (approximately) set aside in December 2008 to deal with former members' claims is distributed to either DFMC Members or former members, the tax implications in broad terms will be as follows:

- No part of the proceeds from the share cancellation effected by the Scheme will be assessable as a dividend in the hands of DFMC Members.
- To the extent that a DFMC Member has a cost base per share equal to \$1 or more and the capital proceeds for the cancellation of each share is \$1, no capital gains tax will be payable.

Whilst the DFMC Board has unanimously recommended that you vote "YES" in favour of the Scheme, there are reasons why you may consider voting against the Scheme. These are summarised in section 3.3 of this Explanatory Memorandum.

It is important you have your say and cast your vote in the Special Postal Ballot using the blue Special Postal Ballot paper.

Yours sincerely



Ian Zandstra
Chairman

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Directors' Recommendation and Reasons

3.1 DIRECTORS' RECOMMENDATION

The DFMC Board **unanimously recommends** that you vote "YES" in favour of the Scheme to return capital to DFMC Members by way of a compulsory share cancellation.

Each DFMC director who is an active DFMC Member intends to vote "YES" in the Special Postal Ballot, in favour of implementation of the Scheme.

3.2 REASONS FOR THE DFMC BOARD'S RECOMMENDATION TO VOTE "YES"

The reasons for the DFMC Board's recommendation for you to vote "YES" in favour of the Scheme are:

- a. To ensure that DFMC's capital structure following the 7 out of 10 share cancellation does not operate as an incentive to DFMC Members to cease to supply DFMC. DFMC Members who cease to supply DFMC have their share capital returned to them by DFMC approximately 12 months after they cease supplying DFMC. The DFMC Board does not want its competitors to be able to exploit the potential liquidity available to DFMC Members who cease to supply DFMC by encouraging DFMC Members to enter into supply contracts with those competitors.
- b. To reduce the inequality between DFMC Members and the services rendered to them. A pro rata share cancellation will reduce the gap in absolute monetary terms between DFMC Members who have subscribed the minimum share capital contribution and other DFMC Members who have for historical reasons provided a greater share capital contribution in DFMC.
- c. To reduce the liabilities on DFMC's balance sheet. Capital in a co-operative is a liability for accounting purposes. If DFMC does not reduce its capital (whilst simultaneously maintaining the current level of retained earnings) it will be left with nominal net assets and even a small operating loss in a financial year could result in DFMC having negative net assets. A balance sheet with negative net assets is likely to make it difficult to sign up new members and to convince the market place that DFMC is a viable and successful ongoing operation.
- d. To reduce the future financial risk to DFMC associated with DFMC Members becoming inactive. Even if a substantial group of DFMC Members became inactive and their share capital was repaid, DFMC would still be able to fund its operations and continue to be viable. A strong balance sheet is necessary to ensure DFMC remains a strong and viable ongoing operation.
- e. To provide a stable capital and financial base for all DFMC Members. The proposed balance sheet structure split between retained earnings (approximately \$11.1 million) and share capital (approximately \$9.7 million) results in DFMC having net assets of approximately \$11.1 million. A balance sheet which merely consists of cash and share capital would result in nominal net assets. A strong balance sheet is necessary to ensure DFMC is perceived as being a strong and viable ongoing operation.
- f. To return to DFMC Members capital that is not required to fund DFMC's operations.

3.3 WHY YOU MAY CONSIDER VOTING AGAINST THE SCHEME

Whilst the DFMC Board has unanimously recommended that you vote "YES" in favour of the Scheme, there are reasons why you may consider voting against the Scheme. These include the following:

- a. You may take the view that DFMC does not need to retain as much as \$21 million in order for DFMC to carry out its role and that these funds should be distributed to DFMC Members.
- b. You may take the view that retained earnings should be distributed in full to DFMC Members and that all the funds retained by DFMC should be made up of share capital alone.
- c. You may take the view that each DFMC Member's shareholding should be reduced to the Minimum Shareholding Requirement for that DFMC Member in order to eliminate inequality between DFMC Members.
- d. You may take the view that DFMC's operating expenses should not exceed the Aggregation Fee, so that DFMC should not require any other source of funding for its operating expenses.
- e. You may take the view that instead of retaining earnings and share capital to fund DFMC's operations, DFMC should consider alternative sources of funding, such as charging a milk levy to DFMC Members.
- f. You may take the view that you do not wish to lose your statutory rights to still be considered to be the holder of the shares cancelled in the event that DFMC is taken over, becomes a company, is wound up having a surplus or makes a distribution from reserves within 5 years of the implementation of the Scheme.

The DFMC Board believes that the advantages of the Scheme outweigh the reasons to vote against the Scheme.

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How to Vote

Under the Co-operatives Act, the DFMC Board is obliged to hold a Special Postal Ballot of DFMC Members to determine whether to agree to implementation of the Scheme. A blue Special Postal Ballot paper is enclosed in the Voting Guide (sent to active DFMC Members) with this Explanatory Memorandum.

4.1 THE SPECIAL POSTAL BALLOT

Active DFMC Members will be asked to vote in favour of a special resolution to agree to implementation of the Scheme. In order for the Scheme to be agreed to, 75% or more of those active DFMC Members who cast valid votes in the Special Postal Ballot will need to vote "YES".

4.2 WHO IS ENTITLED TO VOTE?

Only active DFMC Members are entitled to vote in the Special Postal Ballot. Each active DFMC Member is entitled to one vote in the Special Postal Ballot. The test day for determining active membership for the purpose of voting in the Special Postal Ballot is 9am on Monday 1 June 2009.

Section 178(1) and Schedule 2 of the Co-operatives Act operate to disregard the votes of certain DFMC Members in the Special Postal Ballot where another person (whether or not a DFMC Member) has a relevant interest in any share held by the DFMC Member or in the right to vote of that DFMC Member. Under section 178(1) and Schedule 2 of the Co-operatives Act the votes of certain corporate DFMC Members may be disregarded in the Special Postal Ballot. The Co-operatives Council (by its delegate) is satisfied in the circumstances of DFMC that loss of the right to vote of certain corporate DFMC Members would be unjust or unreasonable, and accordingly has made an order under section 178(3) of the Co-operatives Act in the following terms:

A corporate DFMC Member may vote where:

1. no shareholder of that corporate DFMC Member is a DFMC Member in his, her or its own right; or
2. one or more shareholders of that corporate DFMC Member are DFMC Members in their own right but non-DFMC Member shareholders of that corporate DFMC Member hold between them 50% or more of the voting shares in that corporate DFMC Member; or
3. the corporate DFMC Member is a trustee for:
 - a. non-DFMC Member beneficiaries only; or
 - b. beneficiaries, of which 50% or more are non-DFMC Members.

Notwithstanding the above order, if a corporate DFMC Member is not entitled to vote because of the operation of section 178(1) of the Co-operatives Act, that corporate DFMC Member may apply to the Co-operatives Council under section 178(2) of the Co-operatives Act for a review of the matter.

4.3 CASTING YOUR VOTE

If you are entitled to vote in the Special Postal Ballot and wish to register your vote, please complete the blue Special Postal Ballot paper enclosed in the Voting Guide sent to active DFMC Members with this Explanatory Memorandum and return it in accordance with the instructions contained in the Voting Guide so as to reach the Returning Officer not later than 12pm (noon) (Sydney time) on Tuesday 30 June 2009.

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Frequently Asked Questions

5.1 WHAT IS THE PURPOSE OF THE SCHEME?

The purpose of the Scheme is to reduce each participating DFMC Member's shareholding in DFMC by way of a cancellation of shares.

Subject to the Minimum Shareholding Requirement, each participating DFMC Member will have 7 out of every 10 shares held by that DFMC Member cancelled and will receive the amount paid up in respect of each cancelled share, which is \$1 per share in the case of DFMC Members (excluding those former members who have been reinstated as DFMC Members pursuant to the claim referred to in section 9 of this Explanatory Memorandum).

Under the Scheme, DFMC's capital will be reduced from approximately \$31.9 million to approximately \$9.7 million. More information in relation to the Scheme is provided in section 6 of this Explanatory Memorandum. The DFMC Board's reasons for the Scheme are set out in section 3.2 of this Explanatory Memorandum.

5.2 WHY RETAIN \$21 MILLION?

The amount held by DFMC needs to be sufficient to generate enough interest income to fund those parts of DFMC's operations which are not already funded by the Aggregation Fee paid by ACF to DFMC under the Milk Supply Agreement. Further, the DFMC Board believes that the Aggregation Fee (agreed with ACF in 2004) may not be sufficient to cover external costs, such as accountancy, consulting or legal fees, which may be incurred by DFMC as a consequence of any negotiations or disputes with ACF or other third parties in the future, nor does it provide for other management expenses DFMC will incur to undertake its role on behalf of DFMC Members given the new ownership of ACF.

More information is available in section 7.3.3 of this Explanatory Memorandum.

5.3 AM I ELIGIBLE TO VOTE IN THE SPECIAL POSTAL BALLOT?

To be eligible to vote in the Special Postal Ballot, you must be an active DFMC Member. More information is available in sections 4.2 and 6.2.1 of this Explanatory Memorandum.

5.4 AM I ELIGIBLE TO PARTICIPATE IN THE SCHEME?

To be eligible to participate in the Scheme, you must have been recorded on the Register as at 9am on Tuesday 25 November 2008 and continue to hold shares and be a DFMC Member when the Scheme is

implemented. A Minimum Shareholding Requirement after cancellation applies for participation in the Scheme by each DFMC Member. More information is available in section 6.2.2 of this Explanatory Memorandum.

5.5 WHAT WILL I RECEIVE AND WHEN?

If the Scheme is agreed to by DFMC Members and approved by the Court, you will receive the amount paid up in respect of each cancelled share held by you, which is \$1 per share in the case of DFMC Members (excluding those former members who have been reinstated as DFMC Members pursuant to the claim referred to in section 9 of this Explanatory Memorandum). Participating DFMC Members should receive their payments before the end of July 2009.

5.6 WILL I HAVE TO PAY TAX ON THE MONEY I RECEIVE?

Please read section 11 (Tax Issues) of this Explanatory Memorandum carefully.

On the assumption that the \$6 million (approximately) set aside in December 2008 to deal with former members' claims is distributed to either DFMC Members or former members, the tax implications in broad terms will be as follows:

- No part of the proceeds from the share cancellation effected by the Scheme will be assessable as a dividend in the hands of DFMC Members.
- To the extent that a DFMC Member has a cost base per share equal to \$1 or more and the capital proceeds for the cancellation of each share is \$1, no capital gains tax will be payable.

5.7 IF THE SCHEME IS AGREED TO BY DFMC MEMBERS AND APPROVED BY THE COURT, MUST I PARTICIPATE?

Yes. If the Scheme is agreed to by DFMC Members and approved by the Court, and if you are eligible to participate in the Scheme, participation is compulsory. If you do not want the Scheme to be implemented, you can vote against its implementation. However, the Scheme will be implemented if it is:

- a. agreed to by a 75% majority of DFMC Members who vote in the Special Postal Ballot; and
- b. approved by the Court.

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Frequently Asked Questions

5.8 WILL I BE ABLE TO PURCHASE MORE SHARES IN DFMC AFTER THE CANCELLATION OF 7 OUT OF 10 OF MY CURRENT SHARES?

DFMC's current policy is to issue new shares only to new DFMC Members and only to the extent necessary to satisfy the Minimum Shareholding Requirement. That policy may change in the future.

5.9 DID THE DFMC BOARD CONSIDER ALTERNATIVES TO THE SCHEME?

Yes. The DFMC Board considered declaring an additional dividend to DFMC Members. However, this would not have addressed the DFMC Board's concerns relating to DFMC's capital structure and balance sheet issues going forward. The DFMC Board also considered having a voluntary repurchase of shares under section 172 of the Co-operatives Act. However, this would not have addressed the DFMC Board's concern about inequality between DFMC Members and the services rendered to them. The DFMC Board also considered introducing a milk levy to DFMC Members. However, the DFMC Board considered that such a levy may operate as an incentive for DFMC Members to cease supplying DFMC and to enter into supply contracts with DFMC's competitors. More information is available in section 3.2 of this Explanatory Memorandum.

5.10 WILL I RETAIN MY STATUTORY RIGHTS IN RESPECT OF SHARES CANCELLED BY THE SCHEME?

No. For more information see section 8 of this Explanatory Memorandum.

5.11 WHAT HAPPENS IF MY SHARES ARE DUE TO BE CANCELLED DUE TO INACTIVITY BEFORE THE IMPLEMENTATION OF THE SCHEME?

You will be paid 100% of your share capital and the Scheme will not apply to your shareholding.

5.12 WHAT HAPPENS IF I AM AN INACTIVE DFMC MEMBER AND MY SHARES ARE DUE FOR CANCELLATION AFTER THE IMPLEMENTATION OF THE SCHEME?

You will participate in the Scheme. Subject to the Minimum Shareholding Requirement, you will have 7 out of every 10 of your DFMC shares cancelled. Unless you become an active DFMC Member, your remaining shareholding will be forfeited 12 months after you became an inactive DFMC Member.

5.13 WHAT HAPPENS IF THE SCHEME IS NOT AGREED TO BY DFMC MEMBERS OR APPROVED BY THE COURT?

If the Scheme is not agreed to by DFMC Members in the Special Postal Ballot or approved by the Court at the Second Court Hearing Date, the DFMC Board will consider alternative arrangements to distribute retained earnings and/or share capital to DFMC Members (including those outlined in section 5.9 of this Explanatory Memorandum) having regard to the tax implications of any such arrangements. The tax consequences of any such arrangements are likely to be different to the tax consequences of the Scheme, which are described in section 11 of this Explanatory Memorandum.

5.14 WHAT ELSE DO I NEED TO DO TO PARTICIPATE IN THE SCHEME?

If the Scheme is implemented, you must ensure that each of your shares which is to be cancelled under the Scheme is free from any mortgage, charge or other security or third party interest.

Please refer to section 6.4 of this Explanatory Memorandum and clause 4.23 of the Scheme.

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Summary and Implementation of the Scheme

6.1 SUMMARY OF THE SCHEME

The purpose of the Scheme is to reduce each participating DFMC Member's shareholding in DFMC by way of a cancellation of shares.

Subject to the Minimum Shareholding Requirement, each participating DFMC Member will have 7 out of every 10 shares held by that DFMC Member cancelled and will receive the amount paid up in respect of each cancelled share, which is \$1 per share in the case of DFMC Members (excluding those former members who have been reinstated as DFMC Members pursuant to the claim referred to in section 9 of this Explanatory Memorandum).

As explained in section 9 of this Explanatory Memorandum, assuming that the Co-operatives Council orders operate to reinstate each former member applicant's shareholding, no amount has been paid up in respect of those shares and therefore those former members will not receive any payment by operation of the Scheme. However, 70% of their shareholdings (to the extent that they have been reinstated) will be treated as cancelled under the Scheme.

Under the Scheme, DFMC's capital will be reduced from approximately \$31.9 million to approximately \$9.7 million.

After the return of capital to DFMC Members and on the assumption that the total amount of approximately \$6 million set aside in December 2008 to deal with the former members' claim is distributed to either DFMC Members or former members (see section 9 of this Explanatory Memorandum), DFMC will retain approximately \$21 million represented by retained earnings (approximately \$11.1 million) and share capital (approximately \$9.7 million).

The extent of each DFMC Member's participation in the Scheme will be subject to that DFMC Member retaining sufficient shares in DFMC after the cancellation to satisfy the Minimum Shareholding Requirement (as set out in section 6.2.3 of this Explanatory Memorandum).

DFMC estimates that the Scheme will be completed during July 2009.

If the Scheme is not agreed to by DFMC Members or approved by the Court, then the DFMC Board will consider alternative arrangements for the distribution of the balance of Net Proceeds to DFMC Members and the reduction of DFMC's share capital.

6.2 ELIGIBILITY TO PARTICIPATE

6.2.1 Special Postal Ballot

To be eligible to vote in the Special Postal Ballot, you must be an active DFMC Member. Each active DFMC Member is entitled to one vote in the Special Postal Ballot.

For more information see section 4.2 of this Explanatory Memorandum.

6.2.2 Scheme

DFMC Members who were recorded on the Register as at 25 November 2008 will (subject to the Minimum Shareholding Requirement) participate in the Scheme in respect of the shares held by them as at 9am on Tuesday 25 November 2008 and which have not been cancelled as at the date of implementation of the Scheme.

6.2.3 Minimum Shareholding Requirement

A Minimum Shareholding Requirement after cancellation applies for participation in the Scheme. The Minimum Shareholding Requirement is 2,000 shares for each DFMC Member provided that:

- Where the number of DFMC Members having the same registration number is more than one, no DFMC Member having that registration number may hold less than 100 shares after cancellation.
- DFMC Members having the same registration number may collectively comply with the 2,000 shareholding requirement but each individual DFMC Member must still hold not less than 100 shares after cancellation.

The Minimum Shareholding Requirement is essentially the same as the minimum shareholding required under Rule 23 of the DFMC Rules, except that the transitional provision contained in Rule 23 (7B) which applied in respect of the 2004 ACF restructure does not apply.

6.3 IMPLEMENTATION OF THE SCHEME

The Scheme will be implemented as follows:

6.3.1 Special Postal Ballot

A Special Postal Ballot of DFMC Members will be held to determine whether the Scheme is agreed to by DFMC Members. The Special Postal Ballot process is outlined in section 4 of this Explanatory Memorandum.

If the Scheme is agreed to by DFMC Members in the Special Postal Ballot, then the Scheme will be put to the Court for approval.

6.3.2 Court approval

If the Scheme is approved by the Court, then DFMC will take steps to cancel the relevant DFMC Members' shares and make payments to those DFMC Members shortly thereafter. Participating DFMC Members should receive their payments before the end of July 2009.

6.3.3 Cancellation of shares

Individual DFMC Members

If, as a result of cancellation of 7 of every 10 of a DFMC Member's shares, that DFMC Member's remaining shareholding would be less than the Minimum Shareholding Requirement, then that DFMC Member's shares will only be cancelled to the extent that that

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Summary and Implementation of the Scheme

DFMC Member's shareholding does not fall below the Minimum Shareholding Requirement after cancellation.

Groups of DFMC Members

If, as a result of cancellation of 7 of every 10 of the shares of a group of DFMC Members having the same registration number, that group's remaining shareholding would be less than the Minimum Shareholding Requirement, then that group's shares will only be cancelled to the extent that that group's shareholding does not fall below the Minimum Shareholding Requirement after cancellation and (subject to the Minimum Shareholding Requirement) the shareholding of each DFMC Member of that group shall be cancelled on a pro rata basis to the number of group shares to be cancelled.

Rounding

Subject to the Minimum Shareholding Requirement, where a cancellation of shares under the Scheme results in the shareholding of a DFMC Member or group of DFMC Members being reduced by a part of a share, the number of shares by which that DFMC Member's or group's shareholding will be reduced will be rounded to the nearest whole share.

6.4 DEEMED WARRANTY BY SCHEME PARTICIPANTS

The attention of DFMC Members is drawn to the warranties that Scheme participants will be deemed to have given, if the Scheme is implemented, in clause 4.23 of the Scheme. The Scheme is set out in full in Schedule A of this Explanatory Memorandum.

In summary, clause 4.23 of the Scheme provides that, if the Scheme is implemented, each Scheme participant is deemed to have warranted to DFMC that:

- a. as at the implementation date of the Scheme, all of their DFMC shares (including any rights and entitlements attaching to those shares) will be free from all mortgages, charges, liens, encumbrances, pledges, security interests and interests of third parties of any kind, whether legal or otherwise, and from any restrictions on transfer of any kind; and
- b. that they have full power and capacity to allow the cancellation of those shares (including any rights and entitlements attaching to those shares) under the Scheme.

Accordingly, if the Scheme is implemented, Scheme participants must take action to discharge any mortgages, charges, liens, encumbrances, pledges, security interests and interests of third parties of any kind over their DFMC shares. If you are unclear as to your situation, you should consult your legal or other professional adviser.

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DFMC Structure and Operations

7.1 STRUCTURE AND ROLE OF DFMC

DFMC's structure will not change as a result of the Scheme. DFMC will remain as a co-operative which is owned by DFMC Members who will supply DFMC with milk. DFMC will continue to supply the milk it receives to ACF under the Milk Supply Agreement. DFMC will maintain its role of milk supply aggregation and price negotiation with ACF pursuant to the Milk Supply Agreement. The DFMC Board believes this role is very important, as it allows DFMC Members to focus on their own businesses, knowing their interests are being appropriately represented to National Foods as owner of ACF.

In October 2008, DFMC and ACF obtained an ACCC Authorisation in respect of certain aspects of the milk arrangements between DFMC and ACF. The ACCC Authorisation continues for a period of 5 years and expires in 2013. In broad terms, the ACCC Authorisation permits DFMC and ACF to implement "back to back" pricing between ACF, DFMC and DFMC Members.

7.2 SOME MEMBERSHIP STATISTICS

Current Membership

As at 28 February 2009 DFMC had 1703 active members and 117 inactive members (excluding those former members who have been reinstated as DFMC Members pursuant to the claim referred to in section 9 of this Explanatory Memorandum). As at 28 February 2009, DFMC's share capital was \$32,939,752.

Historical Data

The share capital of a DFMC Member is repaid to that DFMC Member 12 months after that DFMC Member becomes inactive. In the financial years ending 30 June 2006, 2007 and 2008, DFMC repaid to inactive DFMC Members \$2.354 million, \$3.752 million and \$5.275 million respectively.

As at 28 February 2009, DFMC had returned \$5.608 million (approximately) in share capital to inactive DFMC Members during the current financial year ending 30 June 2009 (of which approximately \$2.884 million was returned in respect of DFMC Members whose shares were forfeited between July 2008 and 28 February 2009) and DFMC estimates that \$1.005 million (approximately) in share capital will be paid to inactive DFMC Members between 28 February 2009 and the end of the current financial year ending 30 June 2009.

Future Capital Repayments to DFMC Members

The amount of capital to be repaid to DFMC Members in respect of financial years after 30 June 2009 is difficult to predict because it is dependent upon the numbers of DFMC Members who cease to supply DFMC.

As at the date of this Explanatory Memorandum, the DFMC Board expects capital repayments to inactive DFMC Members (after the 7 for 10 cancellation) for the period 1 July 2009 to 30 November 2009 to be approximately \$306,000 and for the period from 1 December 2009 to 28 February 2010, the DFMC Board expects capital repayments to inactive DFMC Members (after the 7 for 10 cancellation) to be approximately \$105,000.

The DFMC Board expects capital returns to inactive DFMC Members during the financial years ending 30 June 2010 and 30 June 2011 to be less than in recent financial years given that the vast majority of DFMC Members currently have contracts to supply milk to DFMC to the end of either June 2010 or June 2011.

7.3 OPERATIONS

7.3.1 Current operations of DFMC

DFMC currently operates from National Foods' premises (the former ACF premises) at Sydney Olympic Park. Its main operations are conducted pursuant to the Milk Supply Agreement with ACF under which DFMC supplies all the milk produced by DFMC Members to ACF. Pursuant to the Milk Supply Agreement DFMC negotiates with ACF to determine the milk price which is paid.

Income and Expenditure

DFMC passes on to DFMC Members the full price it receives from ACF for the sale of milk and thus does not earn any margin from milk supply to cover its expenses. DFMC's only sources of income in a normal year from which it can meet its expenses are the Aggregation Fee (see below) and any interest income which DFMC earns on its cash deposits. The level of interest earned will depend on the interest rate and the amount of cash deposits (see section 7.3.3 of this Explanatory Memorandum).

DFMC's expenditure in a normal year includes the Administrative Services Fee payable to ACF (see below), the salary, benefits and expenses of the Executive Officer, Greg Griffith, who manages the day to day operations of DFMC and reports to the DFMC Board, directors' fees and costs as well as other business and administration costs.

The Aggregation Fee was agreed with ACF in 2004 and has not been increased to reflect increases in the cost of doing business. In addition certain expenses which DFMC now incurs (or is likely to incur) were not contemplated. For example, the expenses of employing an Executive Officer (which the present DFMC Board considers to be essential), the cost of any significant negotiations and disputes with ACF and other third parties and the costs of obtaining or revising any necessary ACCC authorisation were not contemplated.

The DFMC Board expects that, despite a focus on cost minimisation, it is likely, in a normal financial year, that

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DFMC Structure and Operations

DFMC's expenses will exceed the Aggregation Fee and thus without interest income earned on retained cash deposits an operating loss will be incurred by DFMC. For example, in the financial year ending 30 June 2010, the DFMC Board expects that DFMC's operating expenses will exceed the amount of the Aggregation Fee by approximately \$456,000 (see section 7.3.2 of this Explanatory Memorandum).

Therefore, if DFMC does not maintain retained earnings as is proposed, a deficiency on the balance sheet will result in a normal financial year. In a financial year of extraordinary expenditure (for example should DFMC have a significant dispute with ACF or other third party or need to amend or revise the ACCC Authorisation) the deficiency would be greater.

DFMC incurred a number of extraordinary expenses in the 2008/2009 financial year, in particular in relation to the sale of ACF to National Foods, obtaining the ACCC Authorisation, the proposed implementation of the Scheme and the former members' claim referred to in section 9 of this Explanatory Memorandum.

Administrative Services Fee

Under the Milk Supply Agreement, ACF provides DFMC with administrative services (including office accommodation, IT and telecommunications, accounting, taxation, administration and secretarial services). In return DFMC pays to ACF the Administrative Services Fee, which is currently \$100,000 per annum (exclusive of GST). Under the Milk Supply Agreement, the Administrative Services Fee cannot be increased, except by a limited amount based upon percentages of consumer price index changes or if DFMC's membership increases by 10% or more than the number of DFMC Members as at 1 July 2004.

Aggregation Fee

Under the Milk Supply Agreement, ACF provides funding (limited to an Aggregation Fee, which is currently \$1,100,000 per annum (exclusive of GST)) to DFMC for certain essential services of DFMC. The Milk Supply Agreement provides that the Aggregation Fee cannot be reduced or increased, except by a limited amount based upon percentages of consumer price index changes, or in the case of an increase with the agreement of ACF.

Field Advisory Services

In addition to the Aggregation Fee, under the Milk Supply Agreement, ACF currently provides field advisory services directly to DFMC Members. As part of the provision of those field advisory services directly to DFMC Members, ACF currently provides 3 field officers on secondment to DFMC. The field advisory services (including the provision of the 3 field officers on secondment to DFMC) are provided by ACF at no cost to DFMC and are due to be reviewed by ACF and DFMC for the first time no later than August 2011. Provided that, on a review by ACF and DFMC, the field advisory services are

found to have been provided efficiently and effectively in accordance with the criteria or performance measures agreed in the Milk Supply Agreement, then the provision of the field advisory services by ACF will continue for consecutive periods of at least 2 years during the term of the Milk Supply Agreement.

7.3.2 DFMC's operating budget – financial year ending 30 June 2010

DFMC's operating budget for the financial year ending 30 June 2010 shows a net operating profit of approximately \$178,000 after providing for expected legal fees in relation to the claim for reinstatement by former members referred to in section 9 of this Explanatory Memorandum. The budget is summarised below and assumes interest of approximately 3% will be earned on DFMC's net average cash deposits:

	\$'000
Income	
Milk Supply	503,323
Aggregation Fee	1,100
Interest	634
Total Income	505,057
Expenses	
Milk Payments	503,323
Salaries, Wages, On-Costs, SGC Superannuation	209
Directors' Fees	386
Administrative Services Fee	100
Legal and Consultants' Fees	395
Audit Fees	30
Member Communication	126
Insurance	53
Travel and Accommodation	162
Other Administration Expenses	95
Total Expenses	504,879
Net Operating Profit	178

7.3.3 Why retain earnings and capital of \$21 million?

Please refer to section 3 of this Explanatory Memorandum for the reasons for the DFMC Board's recommendation of the Scheme.

The amount held by DFMC needs to be sufficient to provide additional interest income for DFMC to

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DFMC Structure and Operations

supplement the Aggregation Fee and thus be in a position to be able to meet its expected expenses and obligations so it can properly carry out its role under the Milk Supply Agreement on behalf of DFMC Members.

DFMC's current investment strategy is to deposit funds held by it on call with one of Australia's 4 major trading banks (currently ANZ). Those funds earn market rate interest. If the DFMC Board decides to change its investment strategy materially in the future, DFMC Members will be consulted first.

The amount of interest earned will vary over time and will depend on prevailing interest rates at the time. For example, \$21 million invested at 3% per annum will earn approximately \$630,000 in interest per annum. Due to share forfeitures, the amount invested will diminish over time.

In addition, DFMC needs to ensure that, as capital is treated as a liability in a co-operative, an adequate proportion of the retained funds is treated as retained earnings so if any small losses are incurred in the future the balance sheet of DFMC is unlikely to show a deficiency.

It is forecast that the \$21 million will be split between retained earnings (approximately \$11.1 million) and share capital (approximately \$9.7 million).

As in the past, DFMC will need to repay share capital to DFMC Members as and when their membership is cancelled and their shares forfeited (see section 7.2 of this Explanatory Memorandum for more information on the amounts repaid during the last 3 financial years). Accordingly, the amount held by DFMC as share capital is expected to diminish over time.

After the capital return to DFMC Members, the DFMC Board believes that the level of remaining share capital will be at such a level that it will not encourage DFMC Members to seek to unlock their capital with DFMC by commencing supply directly to a processor.

If the proposed 7 for 10 share cancellation is not carried out, the DFMC Board believes a substantial number of DFMC Members will, in the future, seek to discontinue supply to DFMC in order that they can be repaid their capital. A significant reduction in the number of DFMC Members or in DFMC's milk volumes is likely to have a substantial adverse impact on DFMC's ability to achieve the best possible terms of sale for DFMC Members and will substantially threaten DFMC's ongoing ability to achieve its objectives and therefore threaten its ongoing viability. A share cancellation of 70% will significantly reduce the risk of DFMC Members seeking to discontinue supply in order to have their share capital repaid.

Although the amount of interest earned will vary over time and will depend on prevailing interest rates at the time, the DFMC Board considers that retaining \$21 million in share capital and retained earnings will

generate sufficient income from its investment to fund DFMC's operations going forward, without the risk of DFMC having a balance sheet with negative net assets.

Since 2004, one of the factors which, in the opinion of the DFMC Board, has adversely impacted on DFMC's ability to obtain the best possible outcome for DFMC Members has been DFMC's lack of independent funding. The \$21 million will enable DFMC to fund its ongoing operations whilst providing a stable balance sheet structure.

Based upon DFMC's budget for the financial year ending 30 June 2010, the DFMC Board considers that retaining approximately \$21 million represented by retained earnings (approximately \$11.1 million) and share capital (approximately \$9.7 million) is the most appropriate strategy for funding DFMC's operations going forward.

If, in the future, DFMC does not need to retain as much as \$21 million, then the DFMC Board will consider a further distribution to DFMC Members. Any interest earned on the invested cash which is not used to fund the ongoing operations of DFMC is also likely to be distributed by DFMC to DFMC Members by way of dividend or rebate.

7.3.4 Mandatory statement in accordance with the Act

The intentions of the DFMC Board are as follows:

- a. The continuation of the business of DFMC will not be affected in any material manner by the operation of the Scheme.
- b. No major changes will be made to the business of DFMC, including any redeployment of the fixed assets of DFMC, as a result of the operation of the Scheme.
- c. The future employment of the present employees of DFMC will not be affected in any material manner by the operation of the Scheme.

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Members' Statutory Rights

8.1 INTRODUCTION TO RIGHTS OF FORMER MEMBERS

The Co-operatives Act provides for continuing rights of former members of DFMC in certain circumstances, notwithstanding that their shares have been forfeited and their memberships cancelled.

The Co-operatives Act provides that, in certain circumstances, where a co-operative:

- a. is taken over;
- b. becomes registered as a company;
- c. is wound up with a surplus;
- d. makes a distribution from reserves,

(each a trigger event) within 5 years of the forfeiture of a member's shares and cancellation of that member's membership for inactivity, that member is still considered to be a shareholder, and entitled to participate in the takeover, registration, distribution of surplus on a winding-up or of reserves, as appropriate (statutory rights).

8.2 NUMBER OF FORMER SHAREHOLDINGS WITH STATUTORY RIGHTS ON A TRIGGER EVENT

The number of former shareholdings with existing statutory rights on a trigger event was 1,173 at 28 February 2009. The shareholdings of those former members immediately before forfeiture was 17,497,505 (\$17,497,505). Upon the occurrence of a trigger event during the 5 years following the forfeiture of those members' shares, they would be entitled to participate in the trigger event based on their former shareholdings as if they were shareholders at the time.

8.3 THE EFFECT OF THE SCHEME ON FORMER MEMBERS

Former members will not be entitled to participate in the Scheme. However, please refer to section 9 of this Explanatory Memorandum in respect of how the operation of the Scheme will affect those former members who have been reinstated pursuant to the claim referred to in section 9 of this Explanatory Memorandum.

8.4 THE EFFECT OF THE SCHEME ON CURRENT MEMBERS

DFMC Members who have part of their shareholdings cancelled under the Scheme will not be entitled to participate in trigger events within the prescribed time to the extent of their cancelled shareholdings. This is because the cancellation will be effected pursuant to Part 13 of the Co-operatives Act, which does not provide

for statutory rights for former members who have shares cancelled as part of a scheme or arrangement under that part. DFMC Members will however be entitled to participate in trigger events within the prescribed time to the extent of their continued shareholdings in DFMC.

8.5 WHAT HAPPENS IF A TRIGGER EVENT OCCURS AFTER THE SCHEME?

Former members will, if a trigger event occurs within the prescribed time, participate in the trigger event to the extent of their forfeited shareholdings. DFMC Members who have had their shares cancelled under the Scheme would only participate in the trigger event to the extent of their then existing shareholdings.

For example, if in the unlikely event DFMC was wound up immediately after the implementation of the Scheme and the assets of DFMC distributed, DFMC Members would receive approximately 34.28% of any surplus distributed, whilst former members would receive approximately 65.72% of any surplus distributed. This assumes a proforma share cancellation date of 1 July 2009, estimated former members' shareholdings of 18.503 million immediately after the cancellation date and estimated DFMC Member shareholdings of 9.653 million immediately after the cancellation date.

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Former Members' Claim for Reinstatement

In December 2008, 32 former members of DFMC applied to the Co-operatives Council under section 129 of the Co-operatives Act for reinstatement as DFMC Members in order to participate in the special dividend of \$1.6879 per share declared at DFMC's 2008 AGM.

In February 2009 the Co-operatives Council (by majority) ordered that each former member applicant be reinstated as a DFMC Member on the following basis:

- The membership of each former member applicant be reinstated effective from the date of that member's forfeiture of shares.
- The membership of each former member applicant is such that it entitles each former member applicant to participate in the special dividend that was declared by DFMC in December 2008.
- The entitlement of each former member applicant to the special dividend will be on the basis of their shareholding at the date of their change of status to that of inactive member.
- The membership of each former member applicant shall be cancelled 24 hours after payment of the special dividend to that member.

Assuming that the Co-operatives Council orders operate to reinstate each former member applicant's shareholding, no amount has been paid up in respect of those shares and therefore those former members will not receive any payment by operation of the Scheme. However, 70% of their shareholdings (to the extent that they have been reinstated) will be treated as cancelled under the Scheme.

By letter dated 10 February 2009 DFMC notified DFMC Members of the Co-operatives Council's reasons. The DFMC Board believes the decision of the majority of the Co-operatives Council is wrong and it has appealed the decision to the Court.

In the event that DFMC's appeal is unsuccessful and the Co-operatives Council decision stands, the former members who applied for reinstatement will participate in the special dividend on the basis of their forfeited shareholding. If this occurs approximately \$1.7 million will need to be paid to those former members.

In the event that all of the former members (including those members who applied to the Co-operatives Council in December 2008) who had their shares forfeited in the 12 months prior to the sale of ACF shares to National Foods were reinstated and entitled to participate in the special dividend, they would be entitled to receive a total amount of \$6,043,318 or \$1.6879 per share.

DFMC's appeal is due to be heard in early August 2009 and DFMC expects a decision to be handed down shortly thereafter. Whilst the DFMC Board believes its appeal will be successful, it has nevertheless retained \$6,043,318 which would be used to satisfy the former members' claim.

If DFMC's appeal is successful and the decision of the Co-operatives Council is set aside, the DFMC Board currently intends to recommend to DFMC Members that they declare (in general meeting as soon as practicable thereafter) a further dividend to distribute the retained amount to DFMC Members who were on the Register as at 25 November 2008.

10.1 DFMC'S FINANCIAL STATEMENTS

DFMC's audited financial statements as at 28 February 2009 are contained in Schedule B of this Explanatory Memorandum.

A copy of DFMC's balance sheets as at:

- a. 30 June 2008;
- b. 28 February 2009; and
- c. 1 July 2009 (proforma) assuming the capital return to DFMC Members under the Scheme has been paid, are set out on the next page.

The proforma balance sheet is based on the assumptions set out in section 10.2 of this Explanatory Memorandum. These assumptions are based on information available at the date of this Explanatory Memorandum and are subject to change. The proforma balance sheet should be read in conjunction with DFMC's audited financial statements as at 28 February 2009 (contained in Schedule B of this Explanatory Memorandum) including the notes to those financial statements.

Full particulars of material changes to the financial position of DFMC, within the knowledge of the directors, since the date of the last balance sheet at 30 June 2008 laid before DFMC Members in general meeting on 10 December 2008 are also set out in section 10.3 of this Explanatory Memorandum.

10.2 BALANCE SHEETS

Set out on the next page are DFMC's balance sheets as at 30 June 2008 and 28 February 2009 and a proforma balance sheet as at 1 July 2009 assuming the capital return to DFMC Members under the Scheme has been paid.

Assumptions

The proforma balance sheet allows for or assumes:

- The estimated net share forfeiture of inactive DFMC Members' shares of approximately \$1.005 million from 28 February 2009 up to the proforma share cancellation date of 1 July 2009.
- The estimated 7 for 10 share cancellation after allowing for DFMC Members to retain the minimum shareholding pursuant to the Minimum Shareholding Requirement.
- The distribution of funds of approximately \$6 million (to DFMC Members or former members) referred to in section 9 of this Explanatory Memorandum.
- The estimated transaction costs of approximately \$306,000 in respect of implementation of the Scheme.

10.3 MATERIAL FINANCIAL CHANGES SINCE 30 JUNE 2008

The major changes to the DFMC balance sheet from 30 June 2008 to the date of this Explanatory Memorandum are as follows:

- The ACF investment has been sold for total consideration of approximately \$81.9 million and DFMC also received a dividend from ACF of approximately \$9.7 million. Approximately \$56.9 million of the total proceeds was distributed by DFMC in the form of a dividend of \$1.6879 per share in December 2008.
- The ACF Share Forfeit Loan and ACF Subordinated Loan were repaid by ACF to DFMC as a result of the sale of ACF.
- DFMC has repaid share capital to DFMC Members to the value of approximately \$5.608 million (of which approximately \$2.884 million was returned in respect of DFMC Members whose shares were forfeited between July 2008 and 28 February 2009).
- DFMC made loans to farmer members which are being progressively repaid. At 28 February 2009, the amount of these loans outstanding was \$2.110 million, which was reflected as other assets.
- DFMC owed ACF approximately \$2.28 million at 28 February 2009 primarily for the reimbursement of milk already paid for by ACF.

DFMC BALANCE SHEETS

\$'000	AUDITED ANNUAL REPORT 30 JUN 2008	AUDITED FINANCIAL REPORT 28 FEB 2009	DFMC ESTIMATED NET SHARE FORFEITURES TO SHARE CANCELLATION DATE	SHARE CANCELLATION ESTIMATED AT JULY 2009	ESTIMATED SPECIAL DIVIDEND (PARTIALLY FRANKED)	ESTIMATED TRANSACTION COSTS	TOTAL POST CANCELLATION
Current Assets							
Cash and cash equivalents	221	49,680	(984)	(22,281)	(6,004)	(306)	20,106
ACF Share Forfeit Loan	10,388	-	-	-	-	-	-
ACF Subordinated Loan	4,725	-	-	-	-	-	-
Other	166	3,546	-	-	-	-	3,546
	15,500	53,226	(984)	(22,281)	(6,004)	(306)	23,652
Non-Current Assets							
ACF Subordinated Loan	6,392	-	-	-	-	-	-
Investment in ACF	17,016	-	-	-	-	-	-
Property, plant and equipment	10	10	-	-	-	-	10
Deferred tax assets	201	-	-	-	-	-	-
	23,619	10	-	-	-	-	10
Total Assets	39,119	53,236	(984)	(22,281)	(6,004)	(306)	23,662
Current Liabilities							
Payables	574	2,911	21	-	-	-	2,932
Share Forfeit Loan	2,725	-	-	-	-	-	-
Current tax liabilities	-	-	-	-	-	-	-
	3,299	2,911	21	-	-	-	2,932
Non-Current Liabilities							
Deferred tax liabilities	1	-	-	-	-	-	-
Members' share capital	35,803	32,940	(1,005)	(22,281)	-	-	9,654
	35,804	32,940	(1,005)	(22,281)	-	-	9,654
Total Liabilities	39,103	35,851	(984)	(22,281)	-	-	12,586
Net Assets	16	17,385	-	-	(6,004)	(306)	11,075
Equity							
Retained profits	16	16	-	-	-	-	16
Current year profit	-	17,369	-	-	(6,004)	(306)	11,059
Total Equity	16	17,385	-	-	(6,004)	(306)	11,075

11.1 GENERAL

The information contained in this section has been prepared by and is the responsibility of DFMC's tax Adviser, Ernst & Young.

The tax comments contained in this Explanatory Memorandum are based on the taxation legislation enacted as at the date of this Explanatory Memorandum. The tax comments are necessarily general in nature and should not be relied upon as specific advice. DFMC Members should seek their own tax advice applicable to their particular circumstances.

For the purposes of this Explanatory Memorandum, it is assumed that DFMC Members are either individuals (being tax residents of Australia), discretionary trustees (where the beneficiaries are individuals who are tax residents of Australia), complying superannuation funds, or Australian companies that are resident in Australia. Further, it is assumed that DFMC Members hold their shares in DFMC on capital account.

11.2 THE ATO CLASS RULING

The ATO has issued the ATO Class Ruling in respect of the Scheme. DFMC Members are entitled to rely on the ATO Class Ruling provided the Scheme that is implemented by DFMC is materially the same as outlined in the ATO Class Ruling.

The facts upon which the ATO Class Ruling is based assume that, as part of the implementation of the Scheme, the \$6 million (approximately) set aside in December 2008 to deal with former members' claims referred to in section 9 of this Explanatory Memorandum will be distributed to either DFMC Members or former members.

If the \$6 million (approximately) is not distributed to either DFMC Members or former members, then there is a risk that the Commissioner may regard the Scheme as materially different to that as outlined in the ATO Class Ruling. If this is proved to be the case, there is a risk that the Commissioner may consider he is no longer bound by the ATO Class Ruling.

The taxation opinion contained in this section 11 is based upon the assumption that the \$6 million (approximately) will be distributed to either DFMC Members or former members and that the ATO Class Ruling is binding upon the Commissioner. Provided that the Scheme is carried out as outlined at section 6 and Schedule A of this Explanatory Memorandum, it is the opinion of Ernst & Young that the Scheme is materially the same as the scheme described in the ATO Class Ruling.

If the ATO Class Ruling is not binding upon the Commissioner, part of the proceeds received by DFMC Members for the share cancellation attributable to

the profits of DFMC may be deemed to be assessable as a dividend in the hands of DFMC Members.

Please refer to the ATO Class Ruling which can be accessed online at: <http://law.ato.gov.au/atolaw/view.htm?docid=CLR/CR200922/NAT/ATO/00001>.

11.3 INCOME TAX

In broad terms, no part of the proceeds from the share cancellation will be deemed to be a dividend in the hands of DFMC Members.

11.4 CAPITAL GAINS TAX

The share cancellation will, prima facie, give rise to a CGT event for DFMC Members in respect of each share subject to the cancellation.

DFMC Members will derive a capital gain or capital loss equal to the difference between the capital proceeds received in respect of the cancellation and the DFMC Members' tax cost base or reduced cost base of the shares subject to the cancellation.

To the extent that a DFMC Member has a cost base per share equal to \$1 or more and the capital proceeds for the cancellation of each share is \$1, no capital gains tax will be payable.

The cost base of a share is the cost of acquiring the share plus any incidental costs incurred in respect of the acquisition or disposal of the share, and any indexation that may have accumulated during the period of ownership. For DFMC Members that have held any shares subject to the cancellation prior to the restructure of ACF in 2004, the cost base of their shares will be equal to the amount rolled over at that time. The capital proceeds for CGT purposes for the shares cancelled should be the amount that is paid to the DFMC Member in respect of the cancellation (being the amount paid up per share).

11.4.1 Shares acquired on or after the 2004 ACF Restructure

To the extent that a DFMC Member has a cost base per share equal to \$1 or more and the capital proceeds per share are equal to \$1, a DFMC Member should not make a capital gain associated with the cancellation. In this case, a DFMC Member would not have a CGT liability associated with the share cancellation.

11.4.2 Shares acquired prior to 20 September 1985

Shares held by DFMC Members in DFMC that are deemed to have been acquired prior to 20 September 1985 (pursuant to choosing roll-over relief under the 2004 ACF restructure) will be "pre-CGT" shares. Where pre-CGT shares of DFMC Members are cancelled, any capital gain or capital loss arising from the cancellation

will be disregarded, except when the special rules apply as outlined below.

There are special rules in respect of the disposal of pre-CGT shares that, in certain circumstances, can give rise to a taxable capital gain that is not disregarded. Broadly, these rules would apply where the market value of the assets of DFMC that were acquired on or after 20 September 1985 is 75% or more of the net value of DFMC at the time of the share cancellation. This condition is likely to be satisfied as all of the assets of DFMC have been acquired on or after 20 September 1985.

The amount of any capital gain is calculated as being equal to that part of the capital proceeds received by the DFMC Members in connection with the cancellation that is reasonably attributable to the amount by which the market value of the assets of DFMC exceed their total cost base.

At the time of the cancellation, it is expected that the assets of DFMC will primarily consist of cash, cash equivalents, and a minimal amount of property, plant and equipment. Accordingly, the amount by which the market value of these assets exceeds their cost bases at the time of share cancellation is expected to be minimal (if any). On this basis, it is considered unlikely that a material taxable capital gain should arise for DFMC Members in respect of pre-CGT shares in DFMC cancelled under the Scheme (if any). The amount of any capital gain will ultimately depend on the market value of the assets of DFMC and their cost bases at the time of the cancellation. DFMC Members holding pre-CGT shares should obtain their own independent taxation advice in relation to the CGT consequences of disposing of their DFMC shares into the cancellation.

11.4.3 CGT discount

While a CGT gain is not anticipated, DFMC Members who are individuals, trusts or complying superannuation funds and who have held their shares in DFMC for more than 12 months may be entitled to reduce their capital gain (if any). DFMC Members who are individuals or trusts can reduce their gain by 50%, and complying superannuation funds can reduce their gain by 33⅓%. DFMC Members who are companies are not entitled to the CGT discount.

DFMC Members should obtain their own independent taxation advice in relation to the CGT consequences of their DFMC shares and any entitlement to the CGT discount.

11.5 TAX IMPLICATIONS FOR DFMC

DFMC is treated as a “co-operative company” for tax purposes. As such, specific concessional provisions contained within the tax legislation are available to DFMC. Such concessions include the entitlement for DFMC to claim a tax deduction for unfranked dividends paid, representing assessable income of DFMC distributed to DFMC Members.

Broadly, DFMC will continue to maintain this tax status provided that 90% or more of DFMC’s business is conducted with DFMC Members during the income year.

In broad terms, no part of the proceeds from the share cancellation will be deemed to be a dividend. Consequently, payments made by DFMC to DFMC Members in respect of the share cancellation would not be deductible to DFMC. Moreover, there should not be any franking debit to DFMC’s franking account in respect of the share cancellation. A Private Binding Ruling has been issued by the Commissioner on this issue.

12.1 DIRECTORS' SHAREHOLDINGS AND VOTING INTENTIONS

As at the date of this Explanatory Memorandum, the number of DFMC Shares held by or on behalf of a DFMC director and his spouse are set out in the following table.

Securities held by or on behalf of DFMC directors

	HOLDING IN DFMC
Mr Ian Zandstra	129,058
Mr John Bastian	Nil
Mr Alan Mathers	25,906 plus 25,897 (spouse)
Mr John Macarthur-Stanham	60,688
Mr Trevor Middlebrook	121,878
Mr Peter Ness	22,985 plus 22,985 (spouse)
Mr Duncan McInnes	51,977 plus 13,807 (spouse)
Mr Michael Roache	35,753
Mr Edward Wallwork	89,554
Mr Jeff Ballon	45,005

Each of the directors above (except for Mr John Bastian who is not an active DFMC Member and is not entitled to vote in the Special Postal Ballot) intends to vote "YES" in the Special Postal Ballot in favour of the Scheme and the DFMC Board unanimously recommends that you vote "YES" in favour of the Scheme. The reasons for this recommendation are set out in section 3.2 of this Explanatory Memorandum.

12.2 PAYMENTS OR BENEFITS TO ANY DIRECTOR, SECRETARY OR EXECUTIVE OFFICER AS COMPENSATION FOR LOSS OF OFFICE OR IN CONNECTION WITH RETIREMENT FROM OFFICE AND OTHER ARRANGEMENTS

There is no payment or other benefit that is proposed to be made or given to any director, secretary or executive officer of DFMC as compensation for the loss of, or as consideration for or in connection with his or her retirement from, office in DFMC.

There is no other agreement or arrangement made between a director of DFMC and another person in connection with or conditional upon the outcome of the Scheme.

DFMC does not have any related bodies corporate.

12.3 FORMAL DISCLOSURE AND CONSENTS

(a) Consents

This Explanatory Memorandum contains statements made by or statements said to be based on statements made by:

- Ernst & Young.

Ernst & Young has consented to the inclusion of each statement it has made in the form and content in which the statement appears and has not withdrawn that consent as at the date of this Explanatory Memorandum.

PricewaterhouseCoopers has consented to be named as DFMC's auditor in this Explanatory Memorandum and to the inclusion of the Independent Audit Report within the financial statements contained in Schedule B of this Explanatory Memorandum in the form and context in which the Independent Audit Report appears and has not withdrawn that consent as at the date of this Explanatory Memorandum.

The following parties have given and have not withdrawn their consent to be named in the form and context in which they are named:

- Addisons as legal Adviser to DFMC.
- Baron Partners Limited as corporate Adviser to DFMC.
- Ernst & Young as tax Adviser to DFMC.
- PriceWaterhouseCoopers as auditor to DFMC.

(b) Disclosures and Responsibility

Each person named in section 12.3(a) above:

- Has not authorised or caused the issue of this Explanatory Memorandum.
- Does not make, or purport to make, any statement in this Explanatory Memorandum or any statement on which a statement in this Explanatory Memorandum is based, other than:
 - Ernst & Young in respect of the information in section 11.
 - PricewaterhouseCoopers in respect of the Independent Audit Report within the financial statements contained in Schedule B of this Explanatory Memorandum.
- To the maximum extent permitted by law, expressly disclaims all liability in respect of, makes no representation regarding, and takes no responsibility for, any part of this Explanatory Memorandum other than a reference to its name and the statement (if any) included in this Explanatory Memorandum with the consent of that party as specified in this section 12.3(b).

12.4 OTHER MATERIAL INFORMATION

Except as set out in this Explanatory Memorandum, there is no other information that is material to the making of a decision by a DFMC Member in respect of the Scheme, being information that is within the knowledge of the DFMC directors which has not been previously disclosed to DFMC Members.

There are no material interests of the directors of DFMC, whether as directors, as DFMC Members or creditors of DFMC or otherwise in respect of the proposed Scheme which are different from the effect on the like interests of other persons.

If, between the date of this Explanatory Memorandum and the Second Court Hearing Date, DFMC becomes aware that:

- a material statement in this Explanatory Memorandum is false or misleading;
- there is a material omission from this Explanatory Memorandum;
- a significant change affecting a matter included in this Explanatory Memorandum has occurred; or
- a significant new matter has arisen which would have been required to be included in this Explanatory Memorandum,

DFMC will prepare a supplementary document to this Explanatory Memorandum. The form which the supplementary document may take, and whether a copy will be sent to each DFMC Member, will depend on the nature and timing of the new or changed circumstance(s).

12.5 STAMP DUTY

No duty should be chargeable on share cancellations effected as part of the Scheme.

12.6 DFMC SHARE REGISTER

DFMC's share register has been suspended from 4 November 2008 until 31 July 2009. Inactive DFMC Members have however since that date had their memberships cancelled and shares forfeited.

12.7 APPROVAL AND SIGNING

The Co-operatives Registrar has directed that all information contained in this Explanatory Memorandum be furnished to all DFMC Members.

This statement is signed in accordance with a resolution of the DFMC Board dated 26 May 2009.



Mr Ian Zandstra
Director



Mr Alan Mathers
Director



Mr John Bastian
Director



Mr John Macarthur-Stanham
Director



Mr Trevor Middlebrook
Director

Mr Peter Ness
Director




Mr Duncan McInnes
Director

Mr Jeff Ballon
Director



Mr Michael Roache
Director



Mr Edward Wallwork
Director

The meanings of the terms used in this Explanatory Memorandum are set out below.

TERM	MEANING
ACF	Dairy Farmers Limited (formerly Australian Co-operative Foods Limited) (ACN 010 308 068)
ACCC	Australian Competition and Consumer Commission
ACCC Authorisation	the ACCC authorisation dated 22 October 2008
Adviser	in relation to an entity, a financier, financial adviser, corporate adviser, legal adviser, or technical or other expert adviser or consultant who provides advisory services in a professional capacity to the market in general and who has been engaged by that entity to provide advice to it in connection with the Scheme
Administrative Services Fee	the Administrative Services Fee payable by DFMC to ACF under the Milk Supply Agreement
Aggregation Fee	the Aggregation Fee payable by ACF to DFMC under the Milk Supply Agreement
ATO	Australian Taxation Office
ATO Class Ruling	the ATO Class Ruling number CR 2009/22 issued by the Commissioner on 22 April 2009
Commissioner	the Australian Commissioner of Taxation
Co-operatives Act	the Co-operatives Act 1992 (NSW) (as amended)
Co-operatives Council	the Co-operatives Council as established under section 414(1) of the Co-operatives Act
Co-operatives Registrar	the Registrar as defined in the Co-operatives Act or any person delegated the functions of such person
Court	the Supreme Court of New South Wales
DFMC	Dairy Farmers Milk Co-operative Limited (ARBN 108 690 384)
DFMC Board	the board of directors of DFMC
DFMC Member	a member of DFMC
DFMC Rules	the rules of DFMC, registered on 7 May 2004 (as amended)
Explanatory Memorandum	this memorandum sent to DFMC Members in relation to the Special Postal Ballot and the Scheme
Milk Supply Agreement	the milk supply agreement between DFMC and ACF dated on or about 1 July 2004 (as amended)
Minimum Shareholding Requirement	has the meaning given in section 6.2.3 of this Explanatory Memorandum
National Foods	National Foods Limited (ACN 004 486 631)
Net Proceeds	the amount received (including any dividend) by DFMC from the sale of its investment in ACF to National Foods less any tax payable by DFMC and any other costs and expenses incurred or payable by DFMC in connection with the distribution of the amount received by DFMC from the sale of its investment in ACF to National Foods
Register	DFMC's register of shareholders
Returning Officer	the returning officer appointed as such for the Special Postal Ballot
Scheme	the scheme of arrangement to return capital to DFMC Members by a way of compulsory share cancellation from DFMC Members, a copy of which is contained in Schedule A of this Explanatory Memorandum

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Glossary

TERM	MEANING
Second Court Hearing Date	the first day on which the application made by DFMC to the Court for orders pursuant to section 344(1) of the Co-operatives Act approving the Scheme is heard, or if the application is adjourned for any reason, the first day on which the adjourned application is heard
Special Postal Ballot	the special postal ballot of active DFMC Members which is required pursuant to the Co-operatives Act in relation to the resolution to implement the Scheme
Voting Guide	the Voting Guide sent to active DFMC Members with this Explanatory Memorandum

A

Schedule A: Scheme of Arrangement

You should refer to the Glossary in section 13 as you read this Schedule.

SCHEME OF ARRANGEMENT

Pursuant to Part 13 of the Co-operatives Act 1992 (NSW)
between

Dairy Farmers Milk Co-operative Limited
(ARBN 108 690 384)

and

its Existing Members

PART 1: SCOPE AND CONTENTS OF THIS DOCUMENT

- 1.1 This document consists of Parts 1, 2, 3 and 4 and contains the terms of a scheme of arrangement between DFMC and its Existing Members.
- 1.2 Part 2 comprises Definitions and Interpretations.
- 1.3 Part 3 sets out the context and purpose of the Scheme.
- 1.4 Part 4 comprises the provisions of the Scheme.

PART 2: DEFINITIONS AND INTERPRETATION

- 2.1 In this Part 2 and in each of Parts 3 and 4 unless the context otherwise requires:

Act means the Co-operatives Act 1992 (NSW).

Active means, in relation to a Member at a particular time, a Member who satisfies the active membership provisions of the rules of DFMC at that time.

Business Day means a day on which banks are open for general banking business in Sydney.

Conditions Precedent means each of the following events, namely:

- a. the passing of the Members' Scheme Resolution; and
- b. the approval of the Scheme by the Court under Part 13 of the Act; and
- c. the giving of the Required Approval,

the satisfaction of each of which is a condition precedent to the operation of the provisions contained in Part 4.

Court means the Supreme Court of New South Wales.

DFMC means Dairy Farmers Milk Co-operative Limited (ARBN 108 690 384).

Explanatory Memorandum means the DFMC explanatory memorandum in respect of the Scheme signed by the directors of DFMC and dated 1 June 2009.

Existing Members means the Members registered in the Register of Shareholders at the Record Date subject to the registration by DFMC after the Record Date of all transfers and transmissions lodged with DFMC prior to the Record Date in accordance with clause 4.14 and who continue to be Shareholders and Members on the Implementation Date.

Group means more than one Member having the same registration number with DFMC.

Group Balance means the extent to which a Group's Shareholding exceeds 2,000 Shares immediately prior to cancellation of Shares under the Scheme.

Group Member means a Member who is part of a Group.

Implementation Date means the date on which the Scheme becomes effective in accordance with clause 4.2.

Member means a member of DFMC.

Members' Scheme Resolution means a special resolution passed by means of the Special Postal Ballot.

Minimum Shareholding Requirement means in respect of:

- a. a Member (other than a Group Member), 2,000 Shares;
- b. a Group, 2,000 Shares; and
- c. a Group Member, 100 Shares.

Percentage Amount means in respect of a Group Member the amount, expressed as a percentage (to two decimal places), of that Group Member's Shareholding in proportion to the Shareholding of the Group prior to the cancellation of Shares under the Scheme.

Record Date means 25 November 2008.

Registrar means the New South Wales Registrar of Co-operatives, or any person delegated the Registrar's functions.

Register of Shareholders means the register maintained by DFMC of Shareholders.

Required Approval means the approval given by the Registrar of the Explanatory Memorandum in accordance with section 355 of the Act.

scheme of arrangement means an arrangement for the purposes of Part 13 of the Act.

Scheme means a scheme of arrangement between DFMC and its Existing Members in the terms set out in Parts 2, 3 and 4 of this document, subject to any alterations or conditions made or required by

A

Schedule A: Scheme of Arrangement

the Court including without limitation pursuant to section 344(3) of the Act.

Scheme Share means a Share on issue immediately prior to the Implementation Date and which is cancelled by operation of the Scheme.

Shareholder means a holder of Shares.

Shareholding means a holding of Shares.

Shares means ordinary shares having a nominal value of \$1.00 each issued in the capital of the DFMC.

Special Postal Ballot means the special postal ballot of Active Members entitled to vote in or to the effect of the resolution set out in Schedule A to Part 4 closing at 12pm (noon) (Sydney time) on Tuesday 30 June 2009.

- 2.2** In this Part 2 and in each of Parts 3 and 4 unless the context otherwise requires:
- 2.2.1** words and phrases have the same meaning given to them in the Act;
 - 2.2.2** words importing the singular include the plural and vice versa;
 - 2.2.3** words importing a gender include any gender;
 - 2.2.4** the word person includes a firm, a body corporate, an unincorporated association or an authority;
 - 2.2.5** a reference to a holder includes joint holders;
 - 2.2.6** a reference to a paragraph or clause is a reference to a paragraph or clause of this Scheme.
- 2.3** Headings are for convenience only and do not affect the interpretation of this Part 2 or each of Parts 3 or 4.

PART 3: CONTEXT AND PURPOSE OF THE SCHEME

- 3.1** DFMC is a co-operative registered in New South Wales under the Act.
- 3.2** The Scheme constitutes arrangements whereby, in accordance with Part 4:
- a. Share capital of approximately \$22.3 million will be returned to Existing Members; and
 - b. each Existing Member will have 7 out of every 10 Shares held by that Existing Member cancelled in return for payment of the amount paid up in respect of each Scheme Share (up to a maximum amount of \$1.00 per Scheme Share).

PART 4: PROVISIONS OF THE SCHEME

Implementation Date

- 4.1** DFMC will lodge with the Registrar an office copy of the Court order made for the purposes of section 344(4) of the Act approving the Scheme and in any event by 5.00pm on the first Business Day after the day on which the Court approves the Scheme.
- 4.2** The Scheme becomes effective on the Implementation Date which is either of the following dates:
- 4.2.1** the date on which an office copy of the Court order approving the Scheme is lodged with the Registrar by DFMC; or
 - 4.2.2** such other date as the Court specifies in the Court order.

Cancellation of Shares

- 4.3** On the Implementation Date and in the following order:
- a. subject to clauses 4.4, 4.5 and 4.6, DFMC shall cancel 7 out of every 10 Shares held by each Existing Member;
 - b. by virtue of the cancellation of Shares in paragraph (a), the amount paid up in respect of each Scheme Share (up to a maximum amount of \$1.00 per Scheme Share) held by each Existing Member will be payable by DFMC to the Existing Member; and
 - c. each Existing Member directs that the capital payable by DFMC to the Existing Member pursuant to paragraph (b) be forwarded to that Existing Member within 21 days of the Implementation Date.
- 4.4** If, after the proposed cancellation of the Shares of a Member (other than a Group Member) the remaining Shareholding of the Member would be less than 2,000 Shares, the Shares of that Member will only be cancelled down to 2,000 Shares;
- 4.5** If, after the proposed cancellation of a Group's Shares the remaining Shareholding of the Group or a Group Member would be less than the Minimum Shareholding Requirement for a Group or a Group Member (as the case may be):
- a. the Shareholding of that Group will only be cancelled down to 2,000 Shares; and
 - b. the Shareholding of a Group Member will only be cancelled down to 100 Shares; and
 - c. subject to paragraph (b), each Group Member's Shareholding shall be cancelled by the Percentage Amount of the Group Balance.

A

Schedule A: Scheme of Arrangement

- 4.6** If, after the proposed cancellation under the Scheme, the Shareholding of a Member or Group would be reduced by a part of a Share, the number of Shares by which that Member's or Group's Shareholding will be reduced will be rounded to the nearest whole share.
- 4.7** The capital referred to in clause 4.3(c) may be paid by DFMC doing any of the following at its election:
- dispatching or procuring the despatch to each Existing Member by prepaid post to their address recorded in the Register of Shareholders at the Record Date, of a cheque in Australian currency drawn on of the account of DFMC; or
 - depositing or procuring the deposit into an account with any ADI (as defined in the Banking Act 1959 (Cth)) in Australia notified by the Existing Member to DFMC and recorded in or for the purposes of the Register of Shareholders at the Record Date.

Registration of Holdings

- 4.8** DFMC shall promptly register each transaction effected pursuant to clause 4.3 and within 21 Business Days of the Implementation Date, DFMC shall forward Share statements by prepaid post to the address shown in the Register of Shareholders for each Existing Member.

Conditions Precedent

- 4.9** The satisfaction of each of the Conditions Precedent is a condition precedent to the operation of the provisions contained in this Part 4.
- 4.10** The Scheme will lapse and be of no further force or effect if the Implementation Date has not occurred before the later of:
- 31 August 2009; or
 - such later date as DFMC may nominate, which date is approved by the Registrar.
- 4.11** DFMC will provide to the Court a certificate confirming (in respect of matters within its knowledge) whether or not Conditions Precedent (a) and (c) have been satisfied.

Appointment of Attorney

- 4.12** On and from the Implementation Date and without the need for any further act, each Existing Member irrevocably appoints DFMC and each of its directors and officers for the time being jointly and severally as its attorneys and agents for the purpose of executing any document or doing any act or thing necessary or desirable to give effect to the Scheme and the transactions contemplated by it.

Certificates

- 4.13** All certificates or holding statements for cancelled Scheme Shares will cease to have any effect on the

Implementation Date other than for the purpose of registering dealings in the Shares which took place prior to the Record Date and other than as evidence of the entitlement of the Existing Member to a return of capital in accordance with the Scheme.

Entitlements

- 4.14** For the purpose of determining who are the Existing Members and their respective entitlements under the Scheme:

- 4.14.1** dealings in Shares approved by the Board of DFMC before the Record Date will be recognised for the purpose of establishing who are Existing Members; and
- 4.14.2** transfer or transmission applications in respect of Shares not approved by the Board of DFMC before the Record Date or received after the Record Date will not be recognised for any purpose whatsoever including for the purpose of establishing who are Existing Members.

Further Assurances

- 4.15** DFMC will execute all such deeds and other documents and do all such acts and things as may be necessary or expedient in order to carry out the Scheme.

Authority

- 4.16** DFMC is vested with the authority of each of the Existing Members to join and concur in such acts and transactions on the part of the Existing Members as are necessary to procure the due happening of the events specified in the Scheme.

Alterations and Conditions

- 4.17** Should the Court propose to approve the Scheme subject to any alterations or conditions, DFMC may by its counsel consent to those alterations or conditions on behalf of all persons concerned.

Communications

- 4.18** Where a notice, transfer, transmission application, direction or other communication referred to in the Scheme is sent by post to DFMC, it will not be deemed to be received in the ordinary course of post or on a date other than the date (if any) on which it is actually received at the DFMC registered office.

Costs and Stamp Duty

- 4.19** DFMC shall bear its legal costs associated with the preparation and approval of the Scheme and any stamp duty imposed thereon or imposed on any transaction necessarily incidental thereto.

Proper Law

- 4.20** The proper law of the Scheme is the law of New South Wales.

A

Schedule A: Scheme of Arrangement

General Scheme Provisions

- 4.21** The Scheme overrides DFMC's constituent document to the extent of any inconsistency and binds DFMC and all Existing Members, including those who do not vote in the Special Postal Ballot and those who vote against the Scheme in that ballot.
- 4.22** The Existing Members agree to the cancellation of the rights attached to their Scheme Shares constituted by or resulting from the Scheme (if any).
- 4.23** Each Existing Member is deemed to have warranted to DFMC that all their Scheme Shares (including any rights and entitlements attaching to those shares) will, as at the time of the cancellation of them, be free from all mortgages, charges, liens, encumbrances, pledges, security interests and interests of third parties of any kind, whether legal or otherwise, and from any restrictions on transfer of any kind, and that they have full power and capacity to allow the cancellation of those Scheme Shares (including any rights and entitlements attaching to those Scheme Shares) under the Scheme.

SCHEDULE A TO PART 4

Agreement to the Scheme of Arrangement

THAT:

1. the scheme of arrangement proposed between Dairy Farmers Milk Co-operative Limited and its members, as contained in Schedule A to the Explanatory Memorandum accompanying the Notice of Special Postal Ballot, be agreed to pursuant to Section 344 of the Co-operatives Act (and that the Board of Directors of Dairy Farmers Milk Co-operative Limited be authorised to:
 - 1.1 agree to such alterations to or conditions of the scheme of arrangement as are thought fit by the Court; and
 - 1.2 subject to approval of the scheme of arrangement by the Court, implement the scheme of arrangement with any such alterations or conditions).

B

Schedule B: Financial Statements



DAIRY FARMERS MILK CO-OPERATIVE FINANCIAL REPORT

AS AT 28 FEBRUARY 2009

**EIGHT MONTHS
ENDED 28 FEBRUARY 2009**

ABN 74 669 522 867

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REGISTERED OFFICE AND PRINCIPAL PLACE OF BUSINESS

Quad 1
8 Parkview Drive
SYDNEY OLYMPIC PARK NSW 2127
Telephone: 02 8732 5111
Facsimile: 02 8732 5181
Internet: www.dfmc.org.au
Dairy Farmers Milk Co-operative Limited (DFMC) is a co-operative incorporated and domiciled in Australia.

CHAIRMAN

Ian Zandstra

DIRECTORS

Jeff Ballon
John Bastian
John Macarthur-Stanham
Alan Mathers (Deputy Chairman)
Duncan McInnes
Trevor Middlebrook
Peter Ness
Eddie Wallwork
Michael Roache

BANKERS

Australia and New Zealand Banking Group

AUDITORS

PricewaterhouseCoopers

SOLICITORS

Addisons Lawyers

SECRETARY

Brett Wright

B

Schedule B: Financial Statements



PricewaterhouseCoopers
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AUDITORS' INDEPENDENCE DECLARATION

As lead auditor for the audit of Dairy Farmers Milk Co-operative Limited for the eight months ended 28 February 2009, I declare that, to the best of my knowledge and belief, there have been:

- (a) no contraventions of the auditor independence requirements of the Corporations Act 2001 in relation to the audit; and
- (b) no contraventions of any applicable code of professional conduct in relation to the audit.

This declaration is in respect of Dairy Farmers Milk Co-operative Limited.

A handwritten signature in black ink, appearing to read 'S J Bourke'.

S J Bourke

Partner

PricewaterhouseCoopers

Sydney, 8 May 2009

B

Schedule B: Financial Statements

INCOME STATEMENT

	NOTES	8 MONTHS ENDED 28 FEB 2009 S'000	12 MONTHS ENDED 30 JUN 2008 S'000
Sales revenue	2	332,195	466,631
Cost of sales		(332,195)	(466,631)
Gross profit		-	-
Aggregation fee revenue	2	719	1,100
Administration expenses		(1,117)	(1,052)
Restructure and investment advisory costs	3	(1,194)	(1,031)
Net administration result		(1,592)	(983)
Investment revenue			
Dividend revenue – ACF Scheme	2	9,680	-
Interest revenue	2	706	51
Finance costs			
Members' share capital payments* – ordinary	3	(56,934)	-
Other income			
Profit on sale of available for sale financial assets	2	65,709	-
Net investment and financing result		19,161	51
Profit/(Loss) from continuing operations before income tax		17,569	(932)
Income tax (expense)/benefit	4	(200)	105
Profit/(Loss) attributable to members of the Co-operative	15	17,369	(827)

* Note that in accordance with AIFRS, dividends payable to members on their ordinary shares are included as finance costs within the income statement. Accordingly, the profit attributable to members of the Co-operative (as noted above) is presented after deducting such finance costs. Refer to notes 1(j), 3, 5 and 14.

The above income statement should be read in conjunction with the accompanying notes.

B

Schedule B: Financial Statements

BALANCE SHEET

	NOTES	28 FEB 2009 S'000	30 JUN 2008 S'000
Current assets			
Cash and cash equivalents	6	49,680	221
Receivables	7	3,546	15,279
Total current assets		53,226	15,500
Non-current assets			
Receivables	7	–	6,392
Available for sale financial assets	8	–	17,016
Property, plant and equipment	9	10	10
Deferred tax assets	10	–	201
Total non-current assets		10	23,619
Total assets		53,236	39,119
Current liabilities			
Payables	11	2,911	574
Borrowings	12	–	2,725
Total current liabilities		2,911	3,299
Non-current liabilities			
Deferred tax liabilities	13	–	1
Members' share capital*	14	32,940	35,803
Total non-current liabilities		32,940	35,804
Total liabilities		35,851	39,103
Net assets		17,385	16
Equity			
Retained profits	15	17,385	16
Total equity		17,385	16

* Note that in accordance with AIFRS, members' share capital ('ordinary shares') is treated as a liability. Accordingly, net assets is presented after deducting members' share capital and total equity is presented excluding members' share capital. Refer also to notes 1(j), 3, 5 and 14.

The above balance sheet should be read in conjunction with the accompanying notes.

B

Schedule B: Financial Statements

STATEMENT OF CHANGES IN EQUITY

	8 MONTHS ENDED 28 FEB 2009 \$'000	12 MONTHS ENDED 30 JUN 2008 \$'000
Total equity at the beginning of the year*	16	843
Profit/(Loss) for the period/year	17,369	(827)
Total equity at the end of the period/year*	17,385	16

* Note that in accordance with AIFRS, members' share capital ('ordinary shares') is treated as a liability. Accordingly, total equity is presented excluding members' share capital. Changes in members' share capital are disclosed in note 14. Refer also to notes 1(j), 3, 5 and 14.

The above statement of changes in equity should be read in conjunction with the accompanying notes.

B

Schedule B: Financial Statements

CASH FLOW STATEMENT

	NOTES	8 MONTHS ENDED 28 FEB 2009 \$'000	12 MONTHS ENDED 30 JUN 2008 \$'000
Cash flows from operating activities			
Receipts from customers		366,061	514,047
Payments to suppliers and directors		(366,581)	(514,269)
Dividends received – ACF Scheme		9,680	-
Interest received		706	51
Income tax received		-	5
Net operating cash flows	24	9,866	(166)
Cash flows from investing activities			
Payments for property, plant and equipment		(5)	-
Proceeds from sale of investment in DFL		81,910	-
Subordinated loan advanced		-	(1,356)
Share forfeit loan repayments from DFL		11,204	-
Subordinated loan repayments from DFL		11,117	5,273
Loans advanced to farmers		(4,420)	-
Loans repaid from farmers		2,310	-
Net investing cash flows		102,116	3,917
Cash flows from financing activities			
Proceeds from issue of ordinary shares		20	1,756
Payment for ordinary shares repurchased		-	(112)
Repayment of share forfeit loans		(5,609)	(5,275)
Dividends paid – ordinary shares		(56,934)	-
Net financing cash flows		(62,523)	(3,631)
Net increase in cash		49,459	120
Cash at the beginning of the financial year		221	101
Cash at the end of the period/year	6	49,680	221

The above cash flow statement should be read in conjunction with the accompanying notes.

B

Schedule B: Financial Statements

NOTES TO THE FINANCIAL STATEMENTS

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies adopted in the preparation of the financial report are set out below. These policies have been consistently applied to all the periods and years presented, unless otherwise stated. The financial report includes separate financial statements for Dairy Farmers Milk Co-operative Limited ('DFMC' or the 'Co-operative').

(a) Basis of preparation

This general purpose financial report has been prepared in accordance with Australian Accounting Standards, other authoritative pronouncements of the Australian Accounting Standards Board, Urgent Issues Group Interpretations, the Co-operatives Act 1992 (as amended) and the applicable sections of the Corporations Act 2001.

(i) Compliance with IFRS

Australian Accounting Standards include Australian equivalents to International Financial Reporting Standards (AIFRS). Compliance with AIFRS ensures that the Co-operative's financial statements and notes comply with International Financial Reporting Standards (IFRS).

(ii) Historical cost convention

These financial statements have been prepared under the historical cost convention.

(b) Cash and cash equivalents (note 6)

For cash flow statement presentation purposes, cash and cash equivalents includes cash on hand and deposits held at call with financial institutions which are subject to an insignificant risk of change in value, and bank overdrafts.

(c) Receivables (note 7)

(i) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. Trade receivables are generally due for settlement within 30 days.

(ii) Other receivables

Other receivables are recognised initially at fair value, which is typically the invoice value, and are subsequently measured at amortised cost less provision for impairment. Other receivables are generally due for settlement within 30 days.

(iii) Farmer loans

Farmer loans are recognised at fair value, which is the principal amount in the loan agreement, and are subsequently measured at amortised cost less provision for impairment.

(iv) Share forfeit loan to DFL

Share forfeit loans are initially recognised at fair value, which corresponds to the amount lent and are subsequently measured at amortised cost less provision for impairment.

(v) Subordinated loan to DFL

Subordinated loans are initially recognised at fair value, which corresponds to the amount lent and are subsequently measured at amortised cost less provision for impairment.

(vi) Collectibility

The collectibility of trade receivables, other receivables, subordinated loans and farmer loans are reviewed on an ongoing basis and a provision for impairment is established when there is objective evidence that the Co-operative will not be able to collect all amounts due according to the original terms of the receivables.

(d) Available for sale financial assets (note 8)

In the previous financial year, the investment in DFL has been recognised at cost which was \$1.00 per share, because the investment was an equity instrument that did not have a quoted market price in an active market and where fair value could not be reliably determined. See also note 1(t).

(e) Property, plant and equipment (note 9)

Property, plant and equipment is stated at historical cost less depreciation. Historical cost includes expenditure that is directly attributable to the acquisition of the items. Subsequent costs are included in the asset's carrying amount or recognised as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Co-operative and the cost of the item can be measured reliably. Repairs and maintenance are charged to the income statement when incurred.

Depreciation is calculated using the straight line method to allocate their cost, net of their residual values, over their estimated useful lives of 3-4 years.

The assets' residual values and useful lives are reviewed, and adjusted if appropriate, at each reporting date.

An asset's carrying amount is written down immediately to its recoverable amount if the asset's carrying amount is greater than its estimated recoverable amount (Note 1(f)).

Gains and losses on disposals are determined by comparing proceeds with carrying amount. These are included in the income statement.

B

Schedule B: Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(f) Impairment

Assets are reviewed for impairment whenever events or change in circumstances indicate that the carrying amount may not be recoverable. An impairment loss is recognised for the amount by which the asset's carrying amount exceeds its recoverable amount. The recoverable amount is the higher of an asset's value in use and its fair value less costs to sell. For the purpose of assessing impairment, assets are grouped at the lowest levels for which there are separately identifiable cash inflows which are largely independent of the cash inflows from other assets or groups of assets (cash-generating units). Non-financial assets that suffered an impairment are reviewed for possible reversal of the impairment at each reporting date.

(g) Payables (note 11)

Trade creditors and accruals typically represent liabilities for goods and services provided to the Co-operative prior to the end of the financial year and which are unpaid. The amounts are unsecured and are usually paid within 30 days of recognition.

(h) Borrowings (note 12)

Share forfeit loans are initially recognised at fair value and are subsequently measured at amortised cost. As a result, the liability is measured at \$1.00 per share forfeited.

Borrowings are classified as current liabilities unless the Co-operative has an unconditional right to defer settlement of the liability for at least 12 months after the balance sheet date.

(i) Employee benefits

(i) Wages, salaries and annual leave

Liabilities for wages, salaries and annual leave expected to be settled within 12 months of the reporting date are recognised in other payables in respect of employees' services up to the reporting date and are measured at the amounts expected to be paid when the liabilities are settled.

(ii) Long service leave

The liability for long service leave is recognised in the provision for employee benefits and measured as the present value of expected future payments to be made in respect of services provided by employees up to the reporting date using the projected unit credit method. Consideration is given to expected future wage and salary levels, experience of employee departures and periods of service. Expected future payments are discounted using market yields at the reporting date on national government bonds with terms to maturity and currency that match, as closely as possible, the estimated future cash outflows.

(iii) Retirement benefit obligations

All employees of the Co-operative are entitled to benefits from the Co-operative's defined contribution superannuation plan on retirement, disability or death. Obligations for contributions to defined contribution super funds are recognised as an expense in profit and loss when they are due. The Co-operative's legal or constructive obligation is limited to these contributions.

(iv) Termination benefits

Termination benefits are payable when employment is terminated before the normal retirement date, or when an employee accepts voluntary redundancy in exchange for these benefits. The Co-operative recognises termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal or providing termination benefits as a result of an offer made to encourage voluntary redundancy. Benefits falling due more than 12 months after reporting date are discounted to present value.

(j) Members' share capital (note 14)

Ordinary shares are initially recorded at fair value and are subsequently measured at amortised cost. As a result, the liability is measured at \$1.00 per share. When ordinary shares are repurchased, the consideration of \$1.00 per share is deducted from members' share capital.

(k) Revenue recognition (note 2)

Revenue is measured at the fair value of the consideration received or receivable. Amounts disclosed as revenue are net of returns, trade allowances, rebates and amounts collected on behalf of third parties.

Revenue is recognised when the amount of revenue can be reliably measured, it is probable that future economic benefits will flow to the entity and specific criteria have been met for each of the Co-operative's activities as described below. The amount of revenue is not considered to be reliably measurable until all contingencies relating to the sale have been resolved.

Revenue is recognised for the major business activities as follows:

(i) Sale of goods

A sale is recorded when the goods have been delivered to and accepted by the customer or its agent and collectibility of the related receivable is probable.

(ii) Aggregation fee revenue

Fee income is recognised in accordance with agreed terms as revenue on a straight line basis over the year.

B

Schedule B: Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

(iii) Dividends and interest

Dividends and interest on loans are recognised as revenue when the right to receive payment is established.

(iv) Other interest revenue

Interest income is recognised on a time proportion basis using the effective interest method.

(l) Finance costs (notes 3 and 5)

(i) Dividend rate

A provision is made for interest payable on members' share capital, which is calculated at the rate of dividend payable on ordinary shares, when the dividend has been appropriately authorised on or before the end of the financial year but not paid and is no longer at the discretion of the Co-operative.

(ii) Other finance costs

Interest expense is recognised on a time proportion basis using the effective interest method.

(m) Income tax (notes 4, 10 and 13)

The income tax expense or revenue for the year is the tax payable on the current year's taxable income adjusted by changes in deferred tax assets and liabilities attributable to temporary differences between the tax bases of assets and liabilities and their carrying amounts in the financial statements, and to unused tax losses.

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. However, the deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the reporting date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled.

Deferred tax assets are recognised for deductible temporary differences and unused tax losses only if it is probable that future taxable amounts will be available to utilise those temporary differences and losses.

Deferred tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets and liabilities and when the deferred tax balances relate to the same taxation authority. Current tax assets and tax liabilities are offset where the entity has a legally enforceable right to offset and intends either to settle on a net basis, or to realise the asset and settle the liability simultaneously.

Current and deferred tax balances attributable to amounts recognised directly in equity are also recognised directly in equity.

(n) Reporting period

The financial report has been prepared for the eight months ended 28 February 2009.

The comparative period has been prepared for the financial year (twelve months) ended 30 June 2008.

(o) Segment Reporting

A business segment is identified for a group of assets and operations engaged in providing products or services that are subject to risks and returns that are different to those of other business segments. A geographical segment is identified when the products or services provided within a particular economic environment are subject to risks and returns that are different from those of segments operating in other economic environments.

(p) Foreign currency translation

The financial statements are presented in Australian dollars, which is the Co-operative's functional and presentation currency.

(q) Goods and services tax (GST)

Revenues, expenses and assets are recognised net of the amount of associated GST, unless the GST incurred is not recoverable from the taxation authority. In this case it is recognised as part of the cost of acquisition of the asset or as part of the expense.

Receivables and payables are stated inclusive of the amount of GST receivable or payable. The net amount of GST recoverable from or payable to the taxation authority is included with other receivables or trade creditors and accruals in the balance sheet.

Cash flows are presented on a gross basis. The GST components of cash flows arising from investing or financing activities which are recoverable from or payable to the taxation authority are presented in operating cash flows.

(r) Rounding of amounts

The Co-operative is of a kind referred to in the class order 'Rounding in Financial Reports and Directors' Reports', issued by the Registrar of Co-operatives relating to the 'rounding off' of amounts in the financial report. Amounts in the financial report have been rounded off in accordance with that class order to the nearest thousand dollars, or in certain cases, to the nearest dollar.

(s) New accounting standards

Certain new accounting standards and Urgent Issues Group Interpretations have been published that are not yet mandatory for the current financial statements.

B

Schedule B: Financial Statements

NOTE 1: SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

The Co-operative's assessment of the impact of these new standards and interpretations is set out below.

(i) AASB 8 Operating Segments and AASB 2007-3 Amendments to Australian Accounting Standards arising from AASB 8

AASB 8 and AASB 2007-3 are effective for annual reporting periods commencing on or after 1 January 2009. The Co-operative has not yet decided when to adopt AASB 8. Application of AASB 8 may result in different segments, segment results and different types of information being reported in the segment note of the financial report. However, at this stage, it is not expected to affect any of the amounts recognised in the financial statements.

(ii) Revised AASB 123 Borrowing Costs and AASB 2007-6 Amendments to Australian Accounting Standards arising from AASB 123 [AASB 1, AASB 101, AASB 107, AASB 111, AASB 116 & AASB 138 and Interpretations 1 & 12]

The revised AASB 123 is applicable to annual reporting periods commencing on or after 1 January 2009. It has removed the option to expense all borrowing costs and – when adopted – will require the capitalisation of all borrowing costs directly attributable to the acquisition, construction or production of a qualifying asset. There will be no impact on the financial report of the Co-operative.

(iii) Revised AASB 101 Presentation of Financial Statements and AASB 2007-8 Amendments to Australian Accounting Standards arising from AASB 101

The revised AASB 101 was issued in September 2007 and is applicable to annual reporting periods beginning on or after 1 January 2009. It requires the presentation of a statement of comprehensive income and makes changes to the statement of changes in equity, but will not affect any of the amounts recognised in the financial statements. If an entity has made prior period adjustments or has reclassified items in the financial statements, it will need to disclose a third balance sheet (statement of financial position), this one being as at the beginning of the comparative period. The Co-operative will apply the amended standard from 1 July 2009.

(iv) AASB 2008-8 Amendments to IAS 39 Financial Instruments: Recognition and Measurement (effective 1 July 2009)

AASB 2008-8 amends AASB 139 Financial Instruments: Recognition and Measurement and must be applied retrospectively in accordance with AASB 108 Accounting Policies, Changes in Accounting Estimates and Errors. The amendment makes two significant changes. It prohibits designating inflation as a hedgeable component of a fixed rate debt. It also prohibits including time value in

the one-sided hedged risk when designating options as hedges. The Co-operative will apply the amended standard from 1 July 2009. It is not expected to have a material impact on the Co-operative's financial statements.

(v) AASB Interpretation 17 Distribution of Non-cash Assets to Owners and AASB 2008-13 Amendments to Australian Accounting Standards arising from AASB Interpretation 17

AASB-I 17 applies to situations where an entity pays dividends by distributing non-cash assets to its shareholders. These distributions will need to be measured at fair value and the entity will need to recognise the difference between the fair value and the carrying amount of the distributed assets in the income statement on distribution. The interpretation further clarifies when a liability for the dividend must be recognised and that it is also measured at fair value. Historically the Co-operative has not issued dividends by distributing non-cash assets. Therefore it is not expected to have a material impact on the Co-operative's financial statements. The Co-operative will apply the interpretation prospectively from 1 July 2009 if such circumstances are to arise in paying any future dividends.

(vi) AASB 2008-2 Amendments to Australian Accounting Standards – Puttable Financial Instruments and Obligations Arising on Liquidation [AASB 7, AASB 101, AASB 132, AASB 139 and Interpretation 2]

The amendments made by AASB 2008-2 in March 2008 relate to puttable financial instruments and instruments that require the entity to pay the holder a pro-rata share of the entity's net assets on liquidation. The directors consider that AASB 2008-2 will not impact the current classification of members' share capital as liabilities on the balance sheet.

(t) Significant judgements in applying accounting policies

In the prior financial year and up until the ACF scheme implementation, the Co-operative recorded its investment in DFL at cost which is \$1.00 per share, because the investment was an equity investment that did not have a quoted price in an active market and where fair value could not be reliably determined as disclosed in note 26(g).

B

Schedule B: Financial Statements

NOTE 2: REVENUE AND OTHER INCOME

	8 MONTHS ENDED 28 FEB 2009 \$'000	12 MONTHS ENDED 30 JUN 2008 \$'000
Revenue from continuing operations		
<i>Sales revenue</i>		
Sales revenue – sale of goods to DFL (a)	326,358	466,631
Sales revenue – sale of goods to other external parties	5,837	–
	332,195	466,631
<i>Other administration and investment revenue</i>		
Aggregation fee revenue (b)	719	1,100
Dividend revenue – ACF Scheme (c)	9,680	–
Interest revenue – financial institutions and other	706	51
	11,105	1,151
Total revenue from continuing operations	343,300	467,782
Other income		
Profit on sale of available for sale financial assets (d)	65,709	–

(a) Sale of goods to DFL

DFMC and DFL have entered into a ten year rolling Milk Supply Agreement, which presently expires in June 2017, so that DFMC can secure a long term dependable outlet for milk at a commercial price.

(b) Aggregation fee revenue

Under the Milk Supply Agreement between DFMC and DFL, while DFMC derives at least 90% of its revenues from DFL, DFL must pay the Aggregation Fee to DFMC to cover the expenses incurred by DFMC in connection with the consolidation or aggregation of the milk supply for on sale to DFL. The Aggregation Fee for the year ended 30 June 2009 was agreed at \$1.100 million. \$0.719 million of the Aggregation Fee has been earned by DFMC during the eight month period ended 28 February 2009.

(c) Dividend revenue

During the eight month period ended 28 February 2009 DFMC received special dividends totalling \$9.68 million arising from DFMC's investment in DFL.

(d) Profit on sale of investments

On 26 November 2008 DFMC's investment in DFL was disposed (see note 8). Proceeds received totalled \$81.91 million.

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Schedule B: Financial Statements

NOTE 3: EXPENSES

	8 MONTHS ENDED 28 FEB 2009 \$'000	12 MONTHS ENDED 30 JUN 2008 \$'000
Profit before income tax includes the following specific expenses		
Finance costs		
Members' share capital payments (note 5)		
Special dividends	56,934	-
Restructure and investment advisory costs*	1,194	1,031
Depreciation – plant and equipment	4	8
Employee and director benefits expense	253	371
Defined contribution superannuation expense	23	32

- * The restructure and investment advisory costs relate to legal, corporate advisory and tax advice obtained in respect of both the 20% limit to the Co-operative's investment in DFL (see note 8) and in connection with the implementation of the ACF Scheme.

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Schedule B: Financial Statements

NOTE 4: INCOME TAX

(a) Income tax expense reconciliation

	8 MONTHS ENDED 28 FEB 2009 S'000	12 MONTHS ENDED 30 JUN 2008 S'000
Profit/(Loss) before income tax	17,569	(932)
Income tax expense calculated at 30% (2008: 30%)	5,271	(280)
Tax effect of amounts not deductible or (taxable)		
Non deductible advisory fees	339	175
Franked amount of members' share capital payments	2,877	-
Franked dividend revenue	(2,904)	-
Capital loss – forfeiture of DFL shares (note 8)	(267)	(2,668)
Capital profit – sale of available for sale financial assets (note 8)	(5,256)	-
	60	(2,773)
Recognition of prior period capital losses not recognised in prior years	(3,571)	-
Current period tax losses and temporary differences not recognised	3,512	2,668
Prior period tax losses and temporary differences derecognised	51	-
Under provided in prior years	148	-
Income tax expense/(benefit)	200	(105)

(b) Income tax expense analysis

Deferred tax		
Changes in deferred tax assets (note 10)	201	(120)
Changes in deferred tax liabilities (note 13)	(1)	-
	200	(120)
Current tax	-	15
Income tax expense/(benefit)	200	(105)

(c) Unrecognised tax losses

Unused tax losses for which no deferred tax asset has been recognised	11,652	-
Unused capital tax losses for which no deferred tax asset has been recognised	-	8,893
Potential tax benefit at 30%	3,496	2,668

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Schedule B: Financial Statements

NOTE 5: DIVIDENDS ON MEMBERS' SHARE CAPITAL

In accordance with AIFRS, members' share capital ('ordinary shares') is treated as a liability and dividends payable to members on their ordinary shares are included as finance costs within the income statement. The amount of these 'dividends' on ordinary shares are disclosed in note 3 and as follows:

(a) Dividends

(i) Special dividends – recognised and paid during the period/year

	28 FEB 2009 \$'000	30 JUN 2008 \$'000
Payment date	17 Dec 2008	-
Dividend per share	1.69 cents	-
Per cent franked	17%	-
Paid in cash	56,934	-
Total ordinary dividends paid during the period/year	56,934	-

(b) Franking credits

Franking credits available for subsequent financial years	495	456
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The above franking account balance has been adjusted for:

- franking credits/(debits) that will arise from the payment/(refund) of income tax payable/(receivable) as at the end of the financial year
- franking credits that will arise from the receipt of dividends recognised as receivables at the reporting date

(c) Interest payable at dividend rate

In addition to the above, and prior to implementation of the ACF Scheme, interest was payable on share forfeit loans at the rate of ordinary dividend payable on ordinary shares, as disclosed in note 1f(i) and 12. No interest has been paid on share forfeit loans during the eight months ended 28 February 2009 or the previous financial year.

NOTE 6: CASH AND CASH EQUIVALENTS

Cash and cash equivalents (per Balance Sheet and Cash Flow Statement)	49,680	221
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Cash and cash equivalents represent cash on deposit at call with a financial institution which derived interest at a floating rate of between 3.5% and 7.4% (2008: 6.7% and 7.0%).

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Schedule B: Financial Statements

NOTE 7: RECEIVABLES

	28 FEB 2009 \$'000	30 JUN 2008 \$'000
Current		
Share forfeit loan to DFL (a)	-	10,388
Subordinated loan to DFL (b)	-	4,725
Farmer loans (c)	2,110	-
Other receivables	1,407	94
Income tax receivable	22	22
Prepayments	7	50
	3,546	15,279
Non-current		
Subordinated loan to DFL (b)	-	6,392

(a) Share forfeit loan to DFL

On 26 November 2008 the ACF Scheme was implemented and the share forfeit loan was repaid by DFL. In the prior financial year the Share Forefeit Loan receivable from DFL arose as a result of the forfeiture of shares held by DFMC in excess of 20% as indicated in note 8(a).

(b) Subordinated loan to DFL

Amounts collected from milk payment deductions by DFMC under its Share Acquisition Program (currently suspended), which DFMC considered to be surplus to its needs, were lent to DFL under the terms of a loan agreement. In the prior financial year DFMC called for repayment of the loan to fund the payment of forfeited shares. Interest was receivable within 14 days of each declaration of an ordinary dividend by DFL at the rate of the dividend as if the outstanding balance were ordinary shares.

On 25 August 2008, the subordinated loan agreement between DFMC and DFL was terminated and the loan was repaid in full by DFL in cash.

(c) Farmer loans

Farmer loans are repaid on a monthly basis via deductions from monthly milk payments. The loans will be settled in July 2009. DFMC does not hold collateral or any other security over the balance of farmer loans.

NOTE 8: AVAILABLE FOR SALE FINANCIAL ASSETS

Unlisted equity securities at cost – Investment in DFL (a)	-	17,016
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(a) Investment in DFL (ACF)

The investment in DFL was disposed of on 26 November 2008 after implementation of the ACF Scheme. Prior to the implementation date, the investment comprised a 20% (2008: 20%) ownership interest in DFL. The principal activities of DFL include the processing, manufacturing, packaging, distribution and marketing of milk and dairy products. The Supreme Court of New South Wales ruled in accordance with the Co-operatives Act 1992 (as amended) that DFMC was prohibited from holding more than 20% of the shares in DFL. During the eight months ended 28 February 2009, and prior to the implementation date, 0.815 million shares were forfeited by DFL in accordance with these requirements. The amount receivable by DFMC at the end of the prior financial year that arose as a result of this forfeiture is disclosed in note 7(b).

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Schedule B: Financial Statements

NOTE 9: PROPERTY, PLANT AND EQUIPMENT

	28 FEB 2009 S'000	30 JUN 2008 S'000
Plant and equipment		
At cost	23	25
Accumulated depreciation	(13)	(15)
	10	10

(a) Movement reconciliation

Carrying amount at the beginning of the period	10	21
Additions	5	-
Disposals	(1)	(3)
Depreciation	(4)	(8)
Carrying amount at the end of the period	10	10

NOTE 10: DEFERRED TAX ASSETS

Amounts recognised in profit or loss		
Accruals	-	7
Consulting and advisory costs	-	119
Tax losses	-	75
Total deferred tax assets	-	201

(a) Movements

Balance at the beginning of the year	201	96
(Charged)/credited to the income statement	(201)	120
Tax losses utilised during the current period/year	-	(15)
Balance at the end of the period/year	-	201

(b) Timing of recovery

To be recovered		
Within 12 months	-	75
After 12 months	-	126
	-	201

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Schedule B: Financial Statements

NOTE 11: PAYABLES

	28 FEB 2009 \$'000	30 JUN 2008 \$'000
Trade creditors and accruals	2,911	574

NOTE 12: BORROWINGS

Share forfeit loans (a)	-	2,725
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(a) Share forfeit loans

Under the Co-operatives Act 1992 (as amended) and the Rules of the Co-operative, the membership of an inactive member is cancelled and the member's shares are forfeited contemporaneously after one year of continuous inactivity (i.e. non supply of raw milk). Upon forfeiture, the amount paid up in respect of the forfeited share is transferred into the share forfeit loan account. Previously the Co-operative repaid share forfeit loans within 12 months of forfeiture. In November 2008 members were notified that the Co-operative would repay share forfeit loans as soon as possible after each member's membership has been cancelled and shares forfeited. No interest has been paid on share forfeit loans during the eight months ended 28 February 2009 or the previous financial year.

Upon forfeiture, former members are attributed certain statutory rights under Division 5 Part 6 of the Co-operatives Act 1992 (as amended). In broad terms, these statutory rights allow the former member to participate in various trigger events, including conversion to a company, for a period of five years after forfeiture. In order to participate, the former member must re-subscribe for ordinary shares at \$1.00 each either by applying share forfeit loan funds or by paying cash.

NOTE 13: DEFERRED TAX LIABILITIES

The balance comprises temporary differences attributable to:

Property, plant and equipment	-	1
Total deferred tax liabilities	-	1

(a) Movements

Balance at the beginning of the period	1	1
(Credited)/charged to the income statement	(1)	-
Balance at the end of the period	-	1

(b) Timing of settlement

To be settled		
Within 12 months	-	-
After 12 months	-	1
	-	1

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Schedule B: Financial Statements

NOTE 14: MEMBERS' SHARE CAPITAL

	NUMBER OF SHARES		NOMINAL VALUE	
	28 FEB 2009 #	30 JUN 2008 #	28 FEB 2009 S'000	30 JUN 2008 S'000
Opening balance – shares of \$1 each (fully paid)	35,797,194	36,827,321	35,797	36,827
Shares issued				
Cash	26,255	21,169	26	21
Milk payment deductions (a)	–	1,734,427	–	1,734
Shares repurchased – cash (b)	–	(112,011)	–	(112)
Shares forfeited (c)	(2,883,697)	(2,673,712)	(2,883)	(2,673)
Closing balance – shares of \$1 each (fully paid)	32,939,752	35,797,194	32,940	35,797
Unallocated members' contribution (d)			–	6
			32,940	35,803

Ordinary shares

Note that in accordance with AIFRS, members' share capital ('ordinary shares') is treated as a liability. Classification in this manner occurs because the Co-operative must forfeit and ultimately repay share capital that is forfeited under the inactive membership rules contained in the Co-operatives Act 1992 (as amended) and the Rules of the Co-operative.

Ordinary shares entitle the holder to participate in dividends of the Co-operative in proportion to the number of shares held. On a show of hands every holder of ordinary shares present at a meeting in person or by proxy is entitled to one vote and upon a poll each shareholder is entitled to one vote.

(a) Milk payment deductions

Under the terms of its Share Acquisition Program (currently suspended by the Board), the Co-operative makes deductions from payments to members for milk supplies. Periodically, these monies are applied by the Co-operative to issue shares to members.

(b) Shares repurchased

Under the Co-operatives Act 1992 (as amended) and the Rules of the Co-operative, the Co-operative may, at the request of a member and subject to the legislative restrictions contained in the Act, purchase any shares from a member. The board has adopted policies that limit the extent to which purchases of members' shares will occur.

(c) Shares forfeited

Under the Co-operatives Act 1992 (as amended) and the Rules of the Co-operative, the membership of an inactive member is cancelled and the members' shares are forfeited contemporaneously after one year of continuous inactivity (i.e. non supply of raw milk). The amount payable at the end of the period/year is disclosed in note 12.

(d) Unallocated members' contributions

Unallocated members' contributions represent milk payment deductions and other cash received from members which had not been allocated as shares.

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Schedule B: Financial Statements

NOTE 15: RETAINED PROFITS

	8 MONTHS ENDED 28 FEB 2009 S'000	12 MONTHS ENDED 30 JUN 2008 S'000
Balance at the beginning of the financial period	16	843
Profit/(Loss) attributable to members	17,369	(827)
Balance at the end of the period	17,385	16

NOTE 16: COMMITMENTS FOR EXPENDITURE

The Co-operative had \$nil commitments at the end of the financial period.

NOTE 17: CONTINGENT LIABILITIES

Subsequent to the implementation of the ACF Scheme, certain former members claimed to be entitled to participate in the Special Dividend declared at the 2008 AGM and stated that they would apply to the Co-operatives Council for reinstatement as members. The former members allege an entitlement to interest equal to any dividend declared having regard to correspondence they received from DFMC and claimed that they were misled in respect of their statutory entitlements as a result of the 2004 ACF restructure. In response to the threatened legal action by former members, the board decided to reduce the Special Dividend paid to members on 17 December 2008 to \$1.6879 per share from the original proposal of \$1.8671 per share pending resolution of the matter.

In February 2009 the Co-operatives Council (by majority) ordered that each former member applicant be reinstated as a DFMC member effective from the date that the member's previous shareholding was forfeited, that each former member applicant be eligible to participate in the Special Dividend declared by DFMC in December 2008 on the basis of that member's shareholding at the date of their change of status to that of inactive member and the membership of each former member applicant be cancelled 24 hours after payment of the Special Dividend to that member.

The DFMC board believes the decision of the majority of the Co-operatives Council is wrong and has appealed the decision to the Court. The matter is listed for hearing with the NSW Supreme Court on 5 August 2009.

In the event that all of the former members who had their shares forfeited in the twelve months prior to the implementation of the ACF Scheme (including the former member applicants referred to above) were reinstated and entitled to participate in the Special Dividend, they would be entitled to receive a total amount of approximately \$6,043,000 or \$1.6879 per share.

In the event that the former member applicants are not successful in the legal action, the directors intend that the members who received the Special Dividend at \$1.6879 per share will receive a further Special Dividend at \$0.1792 per share. This represents the amount the Special Dividend paid on 17 December 2008 was reduced by when notification of legal action was received.

NOTE 18: SUBSEQUENT EVENTS

There have been no subsequent events which may affect the Co-operative's operations or results of those operations or the Co-operative's state of affairs.

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Schedule B: Financial Statements

NOTE 19: AUDITORS' REMUNERATION

	8 MONTHS ENDED 28 FEB 2009 \$	12 MONTHS ENDED 30 JUN 2008 \$
Amounts received, or due and receivable by PricewaterhouseCoopers for the audit of the financial report	24,000	20,000

NOTE 20: KEY MANAGEMENT PERSONNEL DISCLOSURES

(a) Directors

The directors of the Co-operative during the eight months ended 28 February 2009 were:

J E Ballon, J J Bastian, J G Macarthur-Stanham, A M Mathers (Deputy Chairman), D A McInnes, T J Middlebrook, P C Ness, E W Wallwork, M P Roache and I H Zandstra (Chairman). There have been no changes to directors from 28 February 2009 to the date of approving the financial statements.

(b) Executive Officer

DFMC appointed an Executive Officer during the eight months ended 28 February 2009. The compensation of the Executive Officer is included within the key management personnel compensation disclosed in note 20(d).

(c) Principles used to determine the nature and amount of remuneration

Base directors' fees were established at the first annual general meeting on 17 November 2004 based on advice from external advisors, which included reference to fee levels for comparable companies. Base fee levels per director have not changed since the first annual general meeting. At the 2007 annual general meeting the members approved the payment of \$7,000 per annum to the chairperson of each board sub-committee. The total fees paid are within the limit approved by members.

The board commits to fair and responsible remuneration policies by ensuring that the level and composition of remuneration packages recognises market levels and is sufficient to attract and retain motivated directors. The focus of the board is on the long term strategic direction and overall performance of the Co-operative. As a consequence, director remuneration is not directly related to short-term results.

The remuneration of the Executive Officer was established considering reasonable market remuneration for the role and responsibilities.

(d) Key management personnel compensation

Short-term employment benefits	253,348	370,510
Post-employment benefits (superannuation)	22,629	32,494
Total key management personnel compensation	275,977	403,004

The compensation noted above comprises the following per annum fixed directors' fees (inclusive of superannuation), which applied throughout all of the current and previous financial periods with the exception of the sub-committee chairperson's fees as described in note 20(c). The compensation noted above also includes the Executive Officer.

DIRECTOR	NUMBER OF DIRECTORS	PER ANNUM FEE \$
Chairman	1	110,000
Directors also nominated on DFL board	2	40,000
Other directors	7	33,000

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NOTE 20: KEY MANAGEMENT PERSONNEL DISCLOSURES (continued)

(e) Other transactions with key management personnel

(i) Farmer directors

The Co-operative has undertaken the following transactions with farmer directors and their related entities. All transactions have been conducted within normal commercial terms and conditions as is applicable to all of the Co-operative's farmers and shareholders:

- The acquisition of milk from the farmer directors by the Co-operative
- The issue of ordinary shares to farmer directors and their related entities in relation to the Share Acquisition Program and dividend re-investment plan (both currently suspended)
- The holding of ordinary shares by farmer directors and their related entities, and if applicable, the forfeiture of such shares in accordance with the inactive membership provisions

(ii) Directors generally

Other than as noted in (i) in relation to farmer directors, there were no other transactions with any director or their director related entities during the eight month period ended 28 February 2009 or the previous financial year other than re-imburement of out-of-pocket business expenses and various minor business related fringe benefits.

NOTE 21: RELATED PARTY TRANSACTIONS AND ECONOMIC DEPENDENCY

DFL is not considered to be a related party as defined in the relevant Accounting Standards because, even prior to the implementation of the ACF Scheme, DFMC has not had control or significant influence over DFL. Nevertheless, DFMC is economically dependent on DFL for a significant amount of its revenue and financial support and accordingly disclosure has been made of the significant transactions between DFMC and DFL in the relevant sections of the financial report as follows:

- Sale of milk to DFL (note 2)
- Dividend and Aggregation Fee revenue derived from DFL (note 2)
- Subordinated loan and share forfeit loan to DFL (note 7)
- Investment in DFL (note 8)

In addition, under the terms of the Milk Supply Agreement, DFMC paid an Administrative Services Fee of \$65,385 (2008: \$100,000) to DFL for the eight month period ended 28 February 2009 to cover the cost of providing administrative facilities and services including offices, communication services, computer hardware and systems, and accounting and secretarial services.

In the previous financial year and up until completion of the ACF Scheme, DFMC may have nominated two farmer directors onto the DFL board subject to DFL member approval. During the currency of the Milk Supply Agreement and up until completion of the ACF Scheme, DFMC may have at any time removed a majority of the directors of the DFL board causing casual vacancies. At a meeting of the members of DFL, DFMC was entitled to one vote.

NOTE 22: SEGMENT INFORMATION

The Co-operative operates in one primary reporting business segment, being the supply of dairy products and in one secondary reporting geographical segment, being the domestic Australian market.

NOTE 23: FINANCE FACILITIES

The Co-operative currently operates without the need for bank finance facilities. A fixed amount of annual funding is made available to DFMC to cover its administrative costs through the Aggregation Fee revenue from DFL as indicated in note 2(b). During the eight months ended 28 February 2009 DFMC received \$9.68 million of dividend income from DFL and \$81.91 million proceeds on sale of DFMC's investment in DFL. In addition, in the prior financial year the Co-operative called for repayment of the subordinated loan to fund the payment of forfeited shares as indicated in note 7(b). Further liquidity information is provided in note 26(d).

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NOTE 24: CASH FLOW RECONCILIATION

	8 MONTHS ENDED 28 FEB 2009 \$'000	12 MONTHS ENDED 30 JUN 2008 \$'000
Profit/(Loss) attributable to members	17,369	(827)
Depreciation expense	4	8
Loss on disposal of property, plant and equipment	1	3
Finance costs – members' share capital payments	56,934	–
Profit on sale of available for sale financial assets	(65,709)	–
<i>Changes in operating assets and liabilities</i>		
(Increase)/Decrease in net working capital	1,067	750
Decrease/(increase) in net tax balances	200	(100)
Net cash inflow/(outflow) from operating activities	9,866	(166)

NOTE 25: NON-CASH FINANCING AND INVESTING ACTIVITIES

Shares forfeited during the eight months ended 28 February 2009 totalling \$2.883 million (12 months ended 30 June 2008: \$2.673 million) were transferred from members' share capital to borrowings.

NOTE 26: FINANCIAL INSTRUMENT AND RISK DISCLOSURES

(a) Risk management

The Co-operative's activities expose it to a variety of financial risks including: market risk, credit risk, liquidity risk and interest rate risk. The Co-operative's overall risk management program seeks to minimise potential adverse effects on the financial performance or position of the Co-operative.

Financial risk management is carried out by the audit, finance and governance committee under policies approved by the board of directors. External advice may be sought on strategic issues as deemed appropriate by either the audit, finance and governance committee or board of directors.

(b) Market risk

The Co-operative is exposed to market risk that arises when the fair value of future cash flows of a financial instrument fluctuates because of changes in market prices that are in turn affected by market interest rates or other factors specific to the financial instrument, its issuer or similar instruments. The Co-operative was exposed to market risk in relation to the following material financial assets prior to their sale during the period:

Subordinated loan to DFL (note 7)	–	11,117
Share forfeit loan to DFL (note 7)	–	10,388
Investment in DFL (note 8)	–	17,016
Carrying value at the end of the year	–	38,521

i) Financial returns

The Co-operative derives interest revenue on cash and cash equivalent balances (see note 6 and note 26 (e)). In the prior financial year the Co-operative derived interest revenue on the subordinated loan and dividend revenue on its investment in DFL at the rate of any ordinary dividend on DFL shares. In the prior financial year changes in DFL dividend levels could have had a material impact on DFMC's income statement.

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NOTE 26: FINANCIAL INSTRUMENT AND RISK DISCLOSURES (continued)

(b) Market risk (continued)

(ii) Other market risks

On 26 November 2008 DFMC disposed of its investment in DFL (see note 8) and is no longer exposed to changes in the fair value of its investment in DFL which was dependent on the financial performance and position of DFL, as well as other factors.

(c) Credit risk

The Co-operative is exposed to credit risk that occurs when a counterparty to a financial instrument causes a financial loss for the Co-operative by failing to discharge an obligation. The maximum exposure to credit risk at balance date, which corresponds to the carrying value of each financial instrument, was as follows:

	8 MONTHS ENDED 28 FEB 2009 \$'000	12 MONTHS ENDED 30 JUN 2008 \$'000
Cash and cash equivalents (note 6)	49,680	221
Subordinated loan to DFL (note 7)	–	11,117
Share forfeit loan to DFL (note 7)	–	10,388
Farmer loans (note 7)	2,110	–
Other receivables (note 7)	1,407	94
Maximum credit risk exposure	53,197	21,820

The Co-operative does not hold collateral or any other security over the above financial assets.

(d) Liquidity risk

The Co-operative is exposed to liquidity risk that occurs when it encounters difficulty in meeting obligations associated with financial liabilities. The expected maturity profile of financial liabilities at the end of the financial year was as follows:

Payable within 12 months		
Trade creditors and accruals (note 11)	2,911	574
Share forfeit loans (note 12)	–	2,725
	2,911	3,299
Payable after 12 months		
Members' share capital (note 14)	32,940	35,803
	35,851	39,102

Trade creditors, accruals and associated administration expenses are typically funded through the Aggregation Fee from DFL, which is received quarterly in advance. Share forfeit loans were funded through the subordinated loan to DFL, whereby, under the terms of the loan agreement, DFMC called for repayment to fund payment of share forfeit loans.

Members' share capital is typically only repaid in the event of share forfeiture, in which case payment has been funded as noted above, or in the event that the shares are repurchased. The board has adopted policies that limit the extent to which repurchases will occur, through the application of the 'age 65' and 'hardship' rules.

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NOTE 26: FINANCIAL INSTRUMENT AND RISK DISCLOSURES (continued)

(d) Liquidity risk (continued)

DFMC has communicated with its members on a proposed compulsory share cancellation. The share cancellation will involve each participating DFMC member having 7 out of 10 shares held by that DFMC member cancelled and only to the extent necessary to satisfy the Minimum Shareholding Requirement. The Minimum Shareholding Requirement is essentially the same as the minimum shareholding required under Rule 23 of the DFMC Rules, except that the transitional provision which applied in respect of the 2004 ACF Restructure does not apply. The proposed compulsory share cancellation, if agreed to by DFMC Members and approved by the Court, is expected to be completed in July 2009.

The Co-operative has access to other funding through the Share Acquisition Program (currently suspended).

The Co-operative also maintains a bank deposit account which is at call and which can be used for day to day cash management purposes. The repayment of the subordinated loan on 25 August 2008 in full, the dividend revenue from DFL and DFMC's disposal of its investment in DFL on 26 November 2008 has generated cash which is available to fund operating and capital requirements.

As a result of the above, the board does not currently foresee the need for, and has not established, a bank overdraft or drawdown facility.

(e) Interest rate risk

The Co-operative is exposed to variable interest rate risks on cash and cash equivalents. As at 28 February 2008 the Co-operative earns interest at the following rates on the cash and cash equivalents:

- \$0-\$25 million earns the current cash rate plus 0.15%
- \$25-\$50 million earns the current cash rate plus 0.25%
- \$50 million and more earns the current cash rate plus 0.29%

In the eight months to 28 February 2009, if interest rates had changed by 25 basis points from the average rates with all other variables held constant, post tax profit for the period would have been approximately \$39,000 lower/higher mainly as a result of the higher/lower interest income from cash and cash equivalents.

(f) Capital risk management

The Co-operative's objective when managing capital is to safeguard its ability to continue as a going concern, so that it can continue to provide returns for members and for other stakeholders and to maintain an optimal capital structure to reduce the cost of capital.

In order to maintain or adjust the capital structure, the Co-operative may reduce its share capital, adjust the amount of dividends paid to shareholders including through the dividend re-investment plan (currently suspended) or may generate capital through deductions from payments to members for milk supplies under the terms of its Share Acquisition Program (currently suspended).

The board of directors and the audit, finance and governance committee monitor the capital needs of the Co-operative.

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Schedule B: Financial Statements

NOTE 26: FINANCIAL INSTRUMENT AND RISK DISCLOSURES (continued)

(g) Fair value disclosures

The carrying amounts and fair values of significant financial assets and liabilities are as follows:

	8 MONTHS ENDED 28 FEBRUARY 2009		12 MONTHS ENDED 30 JUNE 2008	
	CARRYING AMOUNT \$'000	FAIR VALUE \$'000	CARRYING AMOUNT \$'000	FAIR VALUE \$'000
Subordinated loan to DFL (note 7)	-	-	11,117	11,117
Share forfeit loans to DFL (note 7)	-	-	10,388	10,388
Farmer loans	2,110	2,110	-	-
Share forfeit loans (note 12)	-	-	(2,725)	(2,725)
Members' share capital (note 14)	(32,964)	(32,964)	(35,803)	(35,803)

The fair value of the above financial instruments has been determined by discounting the expected future cash flows by the interest rate of instruments with similar risk profiles. These fair value disclosures have been determined using a valuation technique that has been based on assumptions not supported by prices from observable current market transactions in the same instrument and are not based on observable market data.

(i) Investment in DFL (note 8)

In the prior financial year, the fair value of the investment in DFL was not disclosed because it could not be measured reliably whilst DFL remained a co-operative. Whilst DFL remained a co-operative, DFMC was restricted from disposing or transferring its shareholding in DFL in certain ways. Under these circumstances, DFMC would have ultimately realised \$1.00 per share in the event that the DFL shares were cancelled.

Following implementation of the ACF Scheme DFMC's investment in DFL was disposed of on 26 November 2008 (see note 8). DFMC received proceeds on disposal of its investment totalling \$81.91 million and received a dividend of \$9.68 million (see note 2).

(ii) Other assets and liabilities

The fair value of all other assets and liabilities approximates their carrying value.

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DIRECTORS' DECLARATION

In the directors' opinion:

- a. the financial statements and notes set out on pages 31 to 53 are in accordance with the Co-operatives Act 1992 (as amended) and the Corporations Act 2001, including:
 - i. complying with Accounting Standards, the Co-operatives Act 1992 (as amended) the Corporations Regulations 2001 and other mandatory professional reporting requirements; and
 - ii. giving a true and fair view of the Co-operative's financial position as at 28 February 2009 and of its performance for the eight month financial period ended on that date; and
- b. there are reasonable grounds to believe that the Co-operative will be able to pay its debts as and when they become due and payable.

This declaration is made in accordance with a resolution of the directors.



Mr Ian Zandstra
Chairman



Mr John Bastian
Director

Sydney, 6 May 2009

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Independent Audit Report to the members of Dairy Farmers Milk Co-operative Limited

Report on the financial report

We have audited the accompanying financial report of Dairy Farmers Milk Co-operative Limited (the Co-operative), which comprises the balance sheet as at 28 February 2009 and the income statement, statement of changes in equity and cash flow statement for the eight months ended on that date, a summary of significant accounting policies, other explanatory notes and the directors' declaration.

Directors' responsibility for the financial report

The directors of the Co-operative are responsible for the preparation and fair presentation of the financial report in accordance with Australian Accounting Standards (including the Australian Accounting Interpretations), the Co-operatives Act 1992 (as amended) and the *Corporations Act 2001*. This responsibility includes establishing and maintaining internal controls relevant to the preparation and fair presentation of the financial report that is free from material misstatement, whether due to fraud or error; selecting and applying appropriate accounting policies; and making accounting estimates that are reasonable in the circumstances. In Note 1(a), the directors also state, in accordance with Accounting Standard AASB 101 *Presentation of Financial Statements*, that compliance with the Australian equivalents to International Financial Reporting Standards ensures that the financial report, comprising the financial statements and notes, complies with International Financial Reporting Standards.

Auditor's responsibility

Our responsibility is to express an opinion on the financial report based on our audit. We conducted our audit in accordance with Australian Auditing Standards. These Auditing Standards require that we comply with relevant ethical requirements relating to audit engagements and plan and perform the audit to obtain reasonable assurance whether the financial report is free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial report. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the financial report, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial report in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by the directors, as well as evaluating the overall presentation of the financial report.

Our procedures include reading the other information in the Annual Report to determine whether it contains any material inconsistencies with the financial report. For further explanation of an audit, visit our website

<http://www.pwc.com/au/financialstatements/audit>.

Our audit did not involve an analysis of the prudence of business decisions made by directors or management. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinions.

Independence

In conducting our audit, we have complied with the independence requirements of the *Corporations Act 2001*.

Auditor's opinion

In our opinion:

- (a) the financial report of Dairy Farmers Milk Co-operative Limited is in accordance with the Co-operatives Act 1992 (as

amended) and the *Corporations Act 2001*, including:

- (i) giving a true and fair view of the Co-operative's financial position as at 28 February 2009 and of its performance for the eight months ended on that date; and
- (ii) complying with Australian Accounting Standards (including the Australian Accounting Interpretations) and the *Corporations Regulations 2001*; and
- (b) the financial report and notes also comply with International Financial Reporting Standards as disclosed in Note 1(a).

S J Bourke
Partner

PricewaterhouseCoopers
Sydney, 8 May 2009

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DFMC Corporate Directory

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Edward Wallwork

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Greg Griffith (Executive Officer & Secretary)

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Chris Clark (Share Registry Manager)

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Taxation Adviser

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