

ALLIANCE ONE INTERNATIONAL, INC.  
Form 10-Q  
February 08, 2010

**UNITED STATES**

**SECURITIES AND EXCHANGE COMMISSION**

Washington, D.C. 20549

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**FORM 10-Q**

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- QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED December 31, 2009**
- TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE TRANSITION PERIOD FROM \_\_\_\_\_ TO \_\_\_\_\_.**

**Alliance One International, Inc.**  
(Exact name of registrant as specified in its charter)

|   |                                   |   |
|---|-----------------------------------|---|
| <b>Virginia</b>   | <b>001-13684</b>                  | <b>54-1746567</b>                             |
| _____<br>(State or other jurisdiction of Incorporation) | _____<br>(Commission File Number) | _____<br>(I.R.S. Employer Identification No.) |

8001 Aerial Center Parkway  
Morrisville, NC 27560-8417  
(Address of principal executive offices)

(919) 379-4300  
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act:

| <u>Title of Each Class</u>  | <u>Name of Exchange On Which Registered</u> |
|-----------------------------|---|
| Common Stock (no par value) | New York Stock Exchange                     |

Securities registered pursuant to Section 12(g) of the Act: None

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes [ ] No [ ]

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, or a smaller reporting company. See the definitions of large accelerated filer, accelerated filer and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer [ ] Accelerated  
filer [X]

Non-accelerated filer [ ] Smaller reporting company [ ]  
(Do not check if a smaller reporting company)

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

As of February 4, 2010, the registrant had 89,088,383 shares outstanding of Common Stock (no par value) excluding 7,853,121 shares owned by a wholly owned subsidiary.

Alliance One International, Inc. and Subsidiaries

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**Part I. Financial Information**  
**Item 1. Financial Statements.**

Alliance One International, Inc. and Subsidiaries  
**CONDENSED CONSOLIDATED STATEMENTS OF OPERATIONS**  
 Three and Nine Months Ended December 31, 2009 and 2008  
*(Unaudited)*

| <i>(in thousands, except per share amounts)</i>  | Three Months Ended<br>December 31, |           | Nine Months Ended<br>December 31, |             |
|--|------------------------------------|-----------|-----------------------------------|-------------|
|  | 2009                               | 2008      | 2009                              | 2008        |
| Sales and other operating revenues   | \$658,353                          | \$689,974 | \$1,743,991                       | \$1,746,231 |
| Cost of goods and services sold  | 560,252                            | 570,485   | 1,451,102                         | 1,469,633   |
| Gross profit   | 98,101                             | 119,489   | 292,889                           | 276,598     |
| Selling, administrative and general expenses   | 38,070                             | 35,395    | 116,461                           | 113,644     |
| Other income (expense)   | 112                                | (982)     | 2,817                             | 465         |
| Restructuring and asset impairment charges   | -                                  | 47        | -                                 | 499         |
| Operating income   | 60,143                             | 83,065    | 179,245                           | 162,920     |
| Debt retirement expense  | 62                                 | -         | 40,351                            | 954         |
| Interest expense (includes debt amortization of \$2,518 and \$1,067 for the three months and \$6,803 and \$3,300 for the nine months in 2009 and 2008, respectively) | 29,479                             | 24,033    | 87,224                            | 74,847      |
| Interest income  | 957                                | 883       | 3,062                             | 2,525       |
| Income before income taxes and other items   | 31,559                             | 59,915    | 54,732                            | 89,644      |
| Income tax expense (benefit)   | (14,891)                           | 697       | (5,219)                           | (3,918)     |
| Equity in net income of investee companies   | 1,338                              | 398       | 1,338                             | 1,497       |
| Income from continuing operations  | 47,788                             | 59,616    | 61,289                            | 95,059      |
| Income (loss) from discontinued operations, net of tax   | -                                  | (41)      | -                                 | 423         |
| Net income   | 47,788                             | 59,575    | 61,289                            | 95,482      |
| Less: Net income attributable to noncontrolling interests  | 530                                | 113       | 1,011                             | 358         |
| Net income attributable to Alliance One International, Inc.  | \$ 47,258                          | \$ 59,462 | \$ 60,278                         | \$ 95,124   |

## Amounts attributable to Alliance One International, Inc.

|   |           |           |           |           |
|---|-----------|-----------|-----------|-----------|
| Income from continuing operations                           | \$ 47,258 | \$ 59,503 | \$ 60,278 | \$ 94,701 |
| Income (loss) from discontinued operations                  | -         | (41)      | -         | 423       |
| Net income attributable to Alliance One International, Inc. | \$ 47,258 | \$ 59,462 | \$ 60,278 | \$ 95,124 |

## Basic earnings per share

|  |        |        |        |         |
|--|--------|--------|--------|---------|
| Net income from continuing operations      | \$ .53 | \$ .67 | \$ .68 | \$ 1.08 |
| Income (loss) from discontinued operations | -      | -      | -      | -       |
| Net income                                 | \$ .53 | \$ .67 | \$ .68 | \$ 1.08 |

## Diluted earnings per share

|  |        |        |        |         |
|--|--------|--------|--------|---------|
| Net income from continuing operations      | \$ .43 | \$ .67 | \$ .60 | \$ 1.07 |
| Income (loss) from discontinued operations | -      | -      | -      | -       |
| Net income                                 | \$ .43 | \$ .67 | \$ .60 | \$ 1.07 |

## Average number of shares outstanding

|         |         |        |         |        |
|---------|---------|--------|---------|--------|
| Basic   | 88,689  | 88,460 | 88,589  | 88,324 |
| Diluted | 111,937 | 89,070 | 104,058 | 89,101 |

*See notes to condensed consolidated financial statements*

Alliance One International, Inc. and Subsidiaries  
**CONDENSED CONSOLIDATED BALANCE SHEETS**  
*(Unaudited)*

| <i>(in thousands)</i>                          | December<br>31,<br>2009 | December<br>31,<br>2008 | March 31,<br>2009 |
|--|-------------------------|-------------------------|-------------------|
| <b>ASSETS</b>                                  |                         |                         |                   |
| Current assets                                 |                         |                         |                   |
| Cash and cash equivalents                      | \$ 109,518              | \$ 74,607               | \$ 87,665         |
| Trade and other receivables, net               | 256,310                 | 238,822                 | 175,705           |
| Accounts receivable, related parties           | 33,116                  | 21,855                  | 29,765            |
| Inventories:                                   |                         |                         |                   |
| Tobacco  | 652,359                 | 625,673                 | 627,496           |
| Other  | 46,096                  | 52,619                  | 59,693            |
| Advances on purchases of tobacco, net          | 139,449                 | 160,934                 | 137,824           |
| Recoverable income taxes                       | 14,002                  | 5,420                   | 3,995             |
| Current deferred taxes                         | 30,391                  | 28,833                  | 24,837            |
| Prepaid expenses                               | 57,953                  | 51,110                  | 47,800            |
| Assets held for sale                           | 836                     | 4,149                   | 4,411             |
| Current derivative asset                       | 1,075                   | 43,502                  | 23,469            |
| Other current assets                           | 5,704                   | 6,396                   | 9,603             |
| Total current assets                           | 1,346,809               | 1,313,920               | 1,232,263         |
| Other assets                                   |                         |                         |                   |
| Investments in unconsolidated affiliates       | 22,619                  | 21,694                  | 21,675            |
| Goodwill and other intangible assets           | 46,437                  | 42,906                  | 49,877            |
| Deferred income taxes                          | 145,941                 | 97,135                  | 142,832           |
| Other deferred charges                         | 29,527                  | 9,235                   | 13,278            |
| Other noncurrent assets                        | 101,258                 | 103,172                 | 95,640            |
|  | 345,782                 | 274,142                 | 323,302           |
| Property, plant and equipment, net             | 192,852                 | 206,469                 | 202,954           |
|  | \$1,885,443             | \$1,794,531             | \$1,758,519       |
| <b>LIABILITIES AND STOCKHOLDERS EQUITY</b>     |                         |                         |                   |
| Current liabilities                            |                         |                         |                   |
| Notes payable to banks                         | \$ 286,406              | \$ 488,776              | \$ 261,468        |
| Accounts payable                               | 50,799                  | 76,738                  | 120,214           |
| Due to related parties                         | 11,546                  | 2,392                   | 27,488            |
| Advances from customers                        | 61,846                  | 78,236                  | 44,440            |
| Accrued expenses and other current liabilities | 114,132                 | 92,379                  | 97,644            |
| Current derivative liability                   | 2,716                   | 48,800                  | 25,670            |
| Income taxes                                   | 12,797                  | 9,166                   | 16,659            |
| Long-term debt current                         | 19,335                  | 16,982                  | 17,842            |
| Liabilities of discontinued operations         | -                       | 26                      | -                 |
| Total current liabilities                      | 559,577                 | 813,495                 | 611,425           |
| Long-term debt                                 | 806,238                 | 530,651                 | 652,584           |
| Deferred income taxes                          | 7,750                   | 9,622                   | 8,230             |
| Liability for unrecognized tax benefits        | 23,289                  | 46,743                  | 58,135            |

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|  |             |             |             |             |             |             |
|--|-------------|-------------|-------------|-------------|-------------|-------------|
| Pension, postretirement and other long-term liabilities          |             |             |             | 98,885      | 90,156      | 97,365      |
|  |             |             |             | 936,162     | 677,172     | 816,314     |
| Commitments and contingencies                                    |             |             |             | -           | -           | -           |
| Stockholders equity  | Dec. 31,    | Dec. 31,    | March       |             |             |             |
|  | <u>2009</u> | <u>2008</u> | 31,         |             |             |             |
|  |             |             | <u>2009</u> |             |             |             |
| Common Stock no<br>par value:                                    |             |             |             |             |             |             |
| Authorized shares  | 250,000     | 250,000     | 250,000     |             |             |             |
| Issued shares  | 96,942      | 96,814      | 96,827      | 464,387     | 465,426     | 468,195     |
| Retained deficit   |             |             |             | (68,131)    | (165,844)   | (128,409)   |
| Accumulated other comprehensive income (loss)                    |             |             |             | (11,340)    | 661         | (13,125)    |
| Total stockholders equity of Alliance One International,<br>Inc. |             |             |             | 384,916     | 300,243     | 326,661     |
| Noncontrolling interests   |             |             |             | 4,788       | 3,621       | 4,119       |
| Total equity   |             |             |             | 389,704     | 303,864     | 330,780     |
|  |             |             |             | \$1,885,443 | \$1,794,531 | \$1,758,519 |

See notes to condensed consolidated financial statements

Alliance One International, Inc. and Subsidiaries  
**CONDENSED CONSOLIDATED STATEMENTS OF STOCKHOLDERS EQUITY**  
*(Unaudited)*

| <i>(in thousands,<br/>except per share amounts)</i>                         | Attributable to Alliance One International, Inc. |                     |                                       |  |                             |                                 |
|---|--|---------------------|---------------------------------------|--|-----------------------------|---------------------------------|
|   | Common<br>Stock                                  | Retained<br>Deficit | Currency<br>Translation<br>Adjustment | Accumulated<br>Other Comprehensive<br>Income (Loss)<br>Pensions,<br>Net of Tax | Noncontrolling<br>Interests | Total<br>Stockholders<br>Equity |
| Balance, March 31, 2008   | \$462,798  | \$(258,395)         | \$ 5,154                              | \$ 1,910   | \$ 3,623                    | \$ 215,090                      |
| Net income  | -  | 132,558             | -                                     | -  | 679                         | 133,237                         |
| Restricted stock surrendered  | (284)  | -                   | -                                     | -  | -                           | (284)                           |
| Employee stock option related   | 40   | -                   | -                                     | -  | -                           | 40                              |
| Stock-based compensation  | 5,641  | -                   | -                                     | -  | -                           | 5,641                           |
| Conversion of foreign currency<br>financial statements                      | -  | -                   | (7,024)                               | -  | (183)                       | (7,207)                         |
| Adjustment in pensions  | -  | -                   | -                                     | (13,165)   | -                           | (13,165)                        |
| Adoption of EITF 06-10  | -  | (2,572)             | -                                     | -  | -                           | (2,572)                         |
| Balance, March 31, 2009   | \$468,195  | \$(128,409)         | \$ (1,870)                            | \$(11,255)   | \$ 4,119                    | \$ 330,780                      |
| Net income  | -  | 60,278              | -                                     | -  | 1,011                       | 61,289                          |
| Stock warrants issued   | 16,821   | -                   | -                                     | -  | -                           | 16,821                          |
| Call option related to convertible<br>debentures, net of tax<br>of \$13,796 | (25,622)   | -                   | -                                     | -  | -                           | (25,622)                        |
| Restricted stock surrendered  | (249)  | -                   | -                                     | -  | -                           | (249)                           |
| Stock-based compensation  | 5,242  | -                   | -                                     | -  | -                           | 5,242                           |

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|   |           |             |        |            |          |            |
|---|-----------|-------------|--------|------------|----------|------------|
| Adjustment in pensions                              | -         | -           | -      | (359)      | -        | (359)      |
| Noncontrolling interest dividend paid               | -         | -           | -      | -          | (360)    | (360)      |
| Conversion of foreign currency financial statements | -         | -           | 2,144  | -          | 18       | 2,162      |
| Balance, December 31, 2009                          | \$464,387 | \$ (68,131) | \$ 274 | \$(11,614) | \$ 4,788 | \$ 389,704 |

*See notes to condensed consolidated financial statements.*



Alliance One International, Inc. and Subsidiaries  
**CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS**  
 Nine Months Ended December 31, 2009 and 2008  
*(Unaudited)*

| <i>(in thousands)</i>   | December<br>31,<br>2009 | December<br>31,<br>2008 |
|---|-------------------------|-------------------------|
| Operating activities  |                         |                         |
| Net income  | \$ 61,289               | \$ 95,482               |
| Adjustments to reconcile net income to net cash used by operating activities of continuing operations |                         |                         |
| Net income from discontinued operations, net of tax   | -                       | (423)                   |
| Depreciation and amortization   | 21,904                  | 21,979                  |
| Debt amortization/interest  | 8,604                   | 3,587                   |
| Debt retirement cost  | 40,351                  | 954                     |
| Gain on foreign currency transactions   | (3,782)                 | (488)                   |
| Other, net  | 48                      | (3,716)                 |
| Changes in operating assets and liabilities, net  | (160,634)               | (207,958)               |
| Net cash used by operating activities of continuing operations  | (32,220)                | (90,583)                |
| Net cash provided by operating activities of discontinued operations                                  | -                       | 604                     |
| Net cash used by operating activities   | (32,220)                | (89,979)                |
| Investing activities  |                         |                         |
| Purchases of property and equipment   | (9,299)                 | (9,328)                 |
| Intangibles, including internally developed software costs  | (581)                   | (7,133)                 |
| Proceeds on sale of property and equipment  | 7,673                   | 4,286                   |
| Foreign currency derivatives  | (5,026)                 | (14,397)                |
| Refinancing of Brazilian Farmers  | (10,374)                | (8,448)                 |
| Return of capital on investments in unconsolidated affiliates   | -                       | 5,830                   |
| Proceeds from notes receivable  | 6,558                   | 5,102                   |
| Other, net  | (1,869)                 | (5,144)                 |
| Net cash used by investing activities of continuing operations  | (12,918)                | (29,232)                |
| Net cash provided by investing activities of discontinued operations                                  | -                       | -                       |
| Net cash used by investing activities   | (12,918)                | (29,232)                |
| Financing activities  |                         |                         |
| Repayment of short-term demand notes  | -                       | (64,079)                |
| Proceeds from short-term demand notes   | -                       | 9,014                   |
| Net change in short-term borrowings   | 17,415                  | 185,955                 |
| Proceeds from long-term borrowings  | 1,040,509               | -                       |
| Repayment of long-term borrowings   | (908,654)               | (38,596)                |
| Debt issuance cost  | (36,095)                | (896)                   |
| Debt retirement cost  | (23,456)                | (73)                    |
| Excess tax benefits from share-based payment arrangements   | -                       | 348                     |
| Proceeds from issuance of warrants  | 16,821                  | -                       |
| Purchase of call options  | (39,418)                | -                       |

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|  |            |           |
|--|------------|-----------|
| Dividends paid to noncontrolling interests       | (360)      | -         |
| Net cash provided by financing activities        | 66,762     | 91,673    |
| Effect of exchange rate changes on cash          | 229        | (10,069)  |
| Increase (decrease) in cash and cash equivalents | 21,853     | (37,607)  |
| Cash and cash equivalents at beginning of period | 87,665     | 112,214   |
| Cash and cash equivalents at end of period       | \$ 109,518 | \$ 74,607 |

*See notes to condensed consolidated financial statements*

Alliance One International, Inc. and Subsidiaries  
**NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS**  
*(in thousands)*

1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES

**Basis of Presentation**

Because of the seasonal nature of the Company's business, the results of operations for any fiscal quarter will not necessarily be indicative of results to be expected for other quarters or a full fiscal year. In the opinion of management, all adjustments (consisting of normal recurring adjustments) considered necessary for a fair statement of financial position, results of operation and cash flows at the dates and for the periods presented have been included.

As part of the preparation of the condensed consolidated financial statements, the Company performed an evaluation of subsequent events occurring after the condensed consolidated balance sheet date of December 31, 2009, through February 8, 2010, the date the condensed consolidated financial statements were issued. The unaudited information included in this Form 10-Q should be read in conjunction with the financial statements and notes thereto included in the Company's Annual Report on Form 10-K for the fiscal year ended March 31, 2009.

Certain prior year amounts have been reclassified to conform with the current year's presentation, due to the adoption of a new accounting standard related to accounting for noncontrolling interests discussed below.

**New Accounting Standards**

***Recently Adopted Accounting Pronouncements***

On April 1, 2009, the Company adopted new accounting guidance on the accounting and reporting related to noncontrolling interests in a consolidated subsidiary. It requires noncontrolling interests (or minority interests) to be reported as a component of shareholders' equity, which is a change from its current classification between liabilities and shareholders' equity. It also requires earnings attributable to minority interests to be included in net earnings, although such earnings will continue to be deducted to measure earnings per share. This standard is to be applied prospectively, except for the presentation and disclosure requirements, which are applied retrospectively for all periods presented. The Company adopted this new accounting guidance with no material impact to its financial condition or results of operations.

***Recent Accounting Pronouncements Not Yet Adopted***

In December 2008, the Financial Accounting Standards Board ( FASB ) issued new accounting guidance on employers' disclosures about postretirement benefit plan assets. This accounting guidance relates to employers' disclosures about

plan assets of a defined benefit pension or other postretirement plan. The disclosures about plan assets required by this accounting guidance are required for the Company in its fiscal year ending March 31, 2010. The Company does not expect these new disclosure requirements to have a material impact on its financial condition or results of operations.

In June 2009, the FASB issued new accounting guidance on accounting for transfers of financial assets. The objective of this accounting guidance is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement in transferred financial assets. This accounting guidance will be effective for the Company on April 1, 2010. The Company is evaluating the impact of this new accounting guidance on its financial condition and results of operations.

In June 2009, the FASB issued new accounting guidance on accounting for variable interest entities. The objective of this accounting guidance is to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. This accounting guidance will be effective for the Company on April 1, 2010. The Company is evaluating the impact of this new accounting guidance on its financial condition and results of operations.

In October 2009, the FASB issued new accounting guidance on accounting for multiple-deliverable revenue arrangements. The objective of this accounting guidance is to address the accounting for multiple-deliverable arrangements to enable vendors to account for products or services (deliverables) separately rather than as a combined unit. This accounting guidance will be effective for the Company on April 1, 2011. The Company is evaluating the impact of this new accounting guidance on its financial condition and results of operations.

In January 2010, the FASB issued new accounting guidance on fair value measurements and disclosures. This guidance will require reporting entities to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. It will also require reporting entities to present separately information about purchases, sales, issuances, and settlements in their Level 3 fair value reconciliations. The new disclosures and clarifications of existing disclosures (the Level 1 and Level 2 changes) will be effective for the Company on January 1, 2010. The disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements will be effective for the Company on April 1, 2011. The Company does not expect these new disclosure requirements to have a material impact on its financial condition or results of operations.

Alliance One International, Inc. and Subsidiaries

## 1. BASIS OF PRESENTATION AND SIGNIFICANT ACCOUNTING POLICIES *(Continued)*

### **Supplemental Cash Flow Information**

Non-cash investing and financing activities are excluded from the condensed consolidated statement of cash flows. During fiscal 2009, non-cash investing activities included \$17,184 related to the net settlement of foreign currency derivatives. There were no non-cash investing activities during fiscal 2010.

### **Taxes Collected from Customers**

Certain subsidiaries are subject to value added taxes on local sales. These amounts have been included in sales and were \$6,833 and \$3,458 for the three months ended December 31, 2009 and 2008, respectively and \$25,124 and \$29,394 for the nine months ended December 31, 2009 and 2008, respectively.

## **2. INCOME TAXES**

### **FIN 48**

As of December 31, 2009, the Company's unrecognized tax benefits totaled \$9,060, all of which would impact the Company's effective tax rate if recognized.

The Company recognizes interest and penalties related to unrecognized tax benefits in income tax expense. As of December 31, 2009, accrued interest and penalties totaled \$9,252 and \$4,976, respectively.

The Company expects to continue accruing interest related to the unrecognized tax benefits described above. Additionally, the Company may be subject to fluctuations in the unrecognized tax benefit due to currency exchange rate movements.

During the three months ended December 31, 2009, the Company participated in various governmental tax programs in certain locations in an effort to resolve outstanding tax issues. By participating in these programs, the Company's liability for unrecognized tax benefits, including accrued interest and penalties, was reduced from \$72,636 to \$23,288 as compared to September 30, 2009. The decrease in the liability for unrecognized tax benefits relates to cash payments of approximately \$12,943, settlement of unrecognized tax benefits of approximately \$37,292, and an increase related to current period activity of approximately \$887. As recognized in the income statement the settlement of unrecognized tax benefits is reduced by the write off of related deferred tax assets.

The Company expects to recognize an unrecognized tax benefit, related to foreign taxes, for the amount of \$5,746 due to the expiration of an applicable statute of limitations in the next twelve months. Circumstances can change due to unexpected developments in the law and interpretation of the law which may ultimately affect the unrecognized tax benefit.

The Company and its subsidiaries file a U.S. federal consolidated income tax return as well as returns in several U.S. states and a number of foreign jurisdictions. As of December 31, 2009, the Company's earliest open tax year for U.S. federal income tax purposes was its fiscal year ended March 31, 2007. Open tax years in state and foreign jurisdictions generally range from three to six years.

### **Provision for the Nine Months Ended December 31, 2009**

The effective tax rate used for the nine months ended December 31, 2009 was a benefit of 9.5% compared to 4.4% for the nine months ended December 31, 2008. The effective tax rates for these periods are based on the current estimate of full year results including the effect of taxes related to specific events which are recorded in the interim period in which they occur. The Company expects the tax rate for the year ending March 31, 2010 to be an expense of 4.2% after absorption of discrete items.

For the nine months ended December 31, 2009, the Company recorded a specific event adjustment benefit of \$22,089 bringing the effective tax rate estimated for the nine months from an expense of 30.8% to a benefit of 9.5%. This specific event adjustment benefit relates to a reversal of income tax, interest, penalties and exchange losses related to liabilities for unrecognized tax benefits totaling a benefit of \$4,918, net exchange gains on income tax accounts totaling a benefit of \$18,006, and other miscellaneous tax adjustments totaling an expense of \$835. For the nine months ended December 31, 2008, the Company recorded a specific event adjustment expense of \$1,921 bringing the effective tax rate estimated for the nine months from a benefit of 6.5% to 4.4%. This specific event adjustment relates primarily to additional income tax and interest related to liabilities for unrecognized tax benefits and net exchange losses on income tax accounts. The significant difference in the estimated effective tax rate for the nine months ended December 31, 2009 from the statutory rate is primarily due to expenses related to exchange effects.

Alliance One International, Inc. and Subsidiaries

### 3. RESTRUCTURING AND ASSET IMPAIRMENT CHARGES

The Company records other restructuring and impairment charges as they occur in the normal course of business. The following table summarizes the restructuring and asset impairment charges recorded in the Company's reporting segments during the three months and nine months ended December 31, 2009 and 2008:

|   | Three Months Ended<br>December 31, |      | Nine Months Ended<br>December 31, |      |
|---|------------------------------------|------|-----------------------------------|------|
|   | 2009                               | 2008 | 2009                              | 2008 |
| <b>Restructuring and Asset Impairment Charges</b> |                                    |      |                                   |      |

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Employee separation and other cash charges:

|   |      |        |        |          |
|---|------|--------|--------|----------|
| Beginning balance   | \$ - | \$ 379 | \$ 103 | \$ 2,360 |
| Period charges:   |      |        |        |          |
| Severance charges (recovery)                                    | -    | (3)    | -      | 523      |
| Other cash charges (recovery)                                   | -    | 50     | -      | (24)     |
| Total period charges  | -    | 47     | -      | 499      |
| Payments through December 31                                    | -    | (330)  | (103)  | (2,763)  |
| Ending balance December 31                                      | \$ - | \$ 96  | \$ -   | \$ 96    |
| Total restructuring and asset impairment charges for the period | \$ - | \$ 47  | \$ -   | \$ 499   |

The following table summarizes the employee separation and other cash charges recorded in the Company's South America and Other Regions segments during the three months and nine months ended December 31, 2009 and 2008:

| Employee Separation and Other Cash Charges | Three Months Ended<br>December 31, |          | Nine Months Ended<br>December 31, |            |
|--|------------------------------------|----------|-----------------------------------|------------|
|  | 2009                               | 2008     | 2009                              | 2008       |
| Beginning balance:                         | \$ -                               | \$ 379   | \$ 103                            | \$ 2,360   |
| South America                              | -                                  | -        | -                                 | 134        |
| Other regions                              | -                                  | 379      | 103                               | 2,226      |
| Period charges:                            | \$ -                               | \$ 47    | \$ -                              | \$ 499     |
| South America                              | -                                  | -        | -                                 | 47         |
| Other regions                              | -                                  | 47       | -                                 | 452        |
| Payments through December 31:              | \$ -                               | \$ (330) | \$ (103)                          | \$ (2,763) |
| South America                              | -                                  | -        | -                                 | (181)      |
| Other regions                              | -                                  | (330)    | (103)                             | (2,582)    |
| Ending balance December 31:                | \$ -                               | \$ 96    | \$ -                              | \$ 96      |
| South America                              | -                                  | -        | -                                 | -          |
| Other regions                              | -                                  | 96       | -                                 | 96         |

All restructuring costs are recorded in earnings as restructuring and asset impairment costs only when they are incurred or meet the criteria for recording in accordance with generally accepted accounting principles.

### Assets Held for Sale

As of December 31, 2009, the Company reported assets held for sale of \$836, related primarily to production and administrative facilities in Kyrgyzstan, Malawi and Brazil, that are being actively marketed by the Company.

Alliance One International, Inc. and Subsidiaries

#### 4. DISCONTINUED OPERATIONS

The Company continually evaluates its component operations to assure they are consistent with its business plan. Results of operations and the assets and liabilities of its business reported as discontinued operations were as follows:

##### Summary of Results of Operations

|  | <b>Discontinued Operations, Other Regions Segment</b> |             |              |
|--|---|-------------|--------------|
|  | <b>Mozambique</b>                                     | <b>Wool</b> | <b>Total</b> |
| <b>Three Months Ended December 31, 2008</b>      |   |             |              |
| Loss from discontinued operations, net of tax:   |   |             |              |
| Loss from discontinued operations, before tax    | \$ (8)  | \$ (33)     | \$ (41)      |
| Income tax                                       | -   | -           | -            |
| Loss from discontinued operations, net of tax    | \$ (8)  | \$ (33)     | \$ (41)      |
| <b>Nine Months Ended December 31, 2008</b>       |   |             |              |
| Income from discontinued operations, net of tax: |   |             |              |
| Income from discontinued operations, before tax  | \$ 87   | \$ 336      | \$ 423       |
| Income tax                                       | -   | -           | -            |
| Income from discontinued operations, net of tax  | \$ 87   | \$ 336      | \$ 423       |



**Summary of Assets and Liabilities**

**Discontinued Operations, Other Regions Segment**

**December 31, 2008**

Liabilities of discontinued operations:

Accrued expenses

Total liabilities of discontinued operations

**Mozambique**

**Wool**

**Total**

\$ 26

\$ -

\$ 26

\$ 26

\$ -

\$ 26

\* As of March 31, 2009, the Company had completed the liquidation of its discontinued Mozambique and Wool Operations.

## 5. SEGMENT INFORMATION

The Company purchases, processes, sells and stores leaf tobacco. Tobacco is purchased in more than 45 countries and shipped to more than 90 countries. The sales, logistics and billing functions of the Company are primarily concentrated in service centers outside of the producing areas to facilitate access to its major customers. Within certain quality and grade constraints, tobacco is fungible and, subject to these constraints, customers may choose to fulfill their needs from any of the areas where the Company purchases tobacco.

Selling, logistics, billing, and administrative overhead, including depreciation, which originates primarily from the Company's corporate and sales offices are allocated to the segments based upon segment operating income. The Company reviews performance data from purchase through sale based on the source of the product and all intercompany transactions are allocated to the region that either purchases or processes the tobacco.

5. SEGMENT INFORMATION *(Continued)*

The following table presents the summary segment information for the three months and nine months ended December 31, 2009 and 2008:

|  | Three Months Ended<br>December 31, |            | Nine Months Ended<br>December 31, |              |
|--|------------------------------------|------------|-----------------------------------|--------------|
|  | 2009                               | 2008       | 2009                              | 2008         |
| Sales and other operating revenues:        |                                    |            |                                   |              |
| South America                              | \$ 176,766                         | \$ 189,707 | \$ 743,374                        | \$ 774,076   |
| Other regions                              | 481,587                            | 500,267    | 1,000,617                         | 972,155      |
| Total revenue                              | \$ 658,353                         | \$ 689,974 | \$1,743,991                       | \$ 1,746,231 |
| Operating income:                          |                                    |            |                                   |              |
| South America                              | \$ 6,930                           | \$ 25,018  | \$ 78,736                         | \$ 72,880    |
| Other regions                              | 53,213                             | 58,047     | 100,509                           | 90,040       |
| Total operating income                     | 60,143                             | 83,065     | 179,245                           | 162,920      |
| Debt retirement expense                    | 62                                 | -          | 40,351                            | 954          |
| Interest expense                           | 29,479                             | 24,033     | 87,224                            | 74,847       |
| Interest income                            | 957                                | 883        | 3,062                             | 2,525        |
| Income before income taxes and other items | \$ 31,559                          | \$ 59,915  | \$ 54,732                         | \$ 89,644    |

**Analysis of Segment Assets**

|                 | December 31, 2009 | December 31, 2008 | March 31, 2009 |
|-----------------|-------------------|-------------------|----------------|
| Segment assets: |                   |                   |                |
| South America   | \$ 651,252        | \$ 887,046        | \$ 939,234     |
| Other regions   | 1,234,191         | 907,485           | 819,285        |
| Total assets    | \$1,885,443       | \$1,794,531       | \$1,758,519    |

## 6. EARNINGS PER SHARE

The weighted average number of common shares outstanding is reported as the weighted average of the total shares of common stock outstanding net of shares of common stock held by a wholly owned subsidiary. Shares of common stock owned by the subsidiary were 7,853 at December 31, 2009 and 2008. This subsidiary waives its right to receive dividends and it does not have the right to vote.

Certain potentially dilutive options were not included in the computation of earnings per diluted share because their exercise prices were greater than the average market price of the shares of common stock during the period and their effect would be antidilutive. These shares totaled 1,626 at a weighted average exercise price of \$7.02 per share at December 31, 2009 and 1,818 at a weighted average exercise price of \$6.97 per share at December 31, 2008.

In connection with the offering of the Company's 5 ½% Convertible Senior Subordinated Notes due 2014, issued on July 2, 2009 (the Convertible Notes), the Company entered into privately negotiated convertible note hedge transactions (the convertible note hedge transactions) equal to the number of shares that underlie the Company's Convertible Notes. These convertible note hedge transactions are expected to reduce the potential dilution of the Company's common stock upon conversion of the Convertible Notes in the event that the value per share of common stock exceeds the initial conversion price of \$5.0280 per share. These shares were not included in the computation of earnings per diluted share because their inclusion would be antidilutive. The Company also entered separately into privately negotiated warrant transactions relating to the same number of shares of the Company's common stock as the convertible note hedge transactions. The warrants have a strike price of \$7.3325 per share. The warrants expire in daily installments commencing on October 15, 2014 and ending on April 8, 2015. See Note 10 Debt Arrangements to the Notes to Condensed Consolidated Financial Statements for further information.

The following table summarizes the computation of earnings per share for the three months and nine months ended December 31, 2009 and 2008, respectively.

Alliance One International, Inc. and Subsidiaries

6. EARNINGS PER SHARE *(Continued)*

| <i>(in thousands, except per share data)</i>  | Three Months Ended |          | Nine Months Ended |          |
|---|--------------------|----------|-------------------|----------|
|   | December 31,       |          | December 31,      |          |
|   | 2009               | 2008     | 2009              | 2008     |
| <b>BASIC EARNINGS</b>   |                    |          |                   |          |
| Amounts attributable to Alliance One International, Inc.  |                    |          |                   |          |
| Income from continuing operations, net of tax   | \$ 47,258          | \$59,503 | \$60,278          | \$94,701 |
| Income (loss) from discontinued operations, net of tax  | -                  | (41)     | -                 | 423      |
| Net income attributable to Alliance One International, Inc.   | \$ 47,258          | \$59,462 | \$60,278          | \$95,124 |
| <b>SHARES</b>   |                    |          |                   |          |
| Weighted average number of shares outstanding   | 88,689             | 88,460   | 88,589            | 88,324   |
| <b>BASIC EARNINGS PER SHARE</b>   |                    |          |                   |          |
| Net income from continuing operations   | \$ .53             | \$ .67   | \$ .68            | \$ 1.08  |
| Net income (loss) from discontinued operations  | -                  | -        | -                 | -        |
| Net income  | \$ .53             | \$ .67   | \$ .68            | \$ 1.08  |
| <b>DILUTED EARNINGS</b>   |                    |          |                   |          |
| Income from continuing operations, net of tax   | \$ 47,258          | \$59,503 | \$60,278          | \$94,701 |
| Plus interest expense on 5 1/2% convertible notes, net of tax   | 1,047              | -        | 2,044             | -        |
| Income from continuing operations, net of tax as adjusted   | 48,305             | 59,503   | 62,322            | 94,701   |
| Income (loss) from discontinued operations, net of tax  | -                  | (41)     | -                 | 423      |
| Net income attributable to Alliance One International, Inc. as adjusted   | \$ 48,305          | \$59,462 | \$62,322          | \$95,124 |
| <b>SHARES</b>   |                    |          |                   |          |
| Weighted average number of common shares outstanding  | 88,689             | 88,460   | 88,589            | 88,324   |
| Plus: Restricted shares issued and shares applicable to stock options and restricted stock units, net of shares assumed to be purchased from proceeds at average market price | 376                | 610      | 390               | 777      |
| Assuming conversion of 5 1/2% convertible notes at the  | 22,872             | -        | 15,079            | -        |

|   |         |        |         |         |
|---|---------|--------|---------|---------|
| time of issuance  |         |        |         |         |
| Shares applicable to stock warrants                           | -*      | -      | -*      | -       |
| Adjusted weighted average number of common shares outstanding | 111,937 | 89,070 | 104,058 | 89,101  |
| <b>DILUTED EARNINGS PER SHARE</b>                             |         |        |         |         |
| Net income from continuing operations                         | \$ .43  | \$ .67 | \$ .60  | \$ 1.07 |
| Income (loss) from discontinued operations                    | -       | -      | -       | -       |
| Net income as adjusted  | \$ .43  | \$ .67 | \$ .60  | \$ 1.07 |

\* For the three months and nine months ended December 31, 2009, the warrants were not assumed exercised because the exercise price was more than the average price for the periods presented.

## 7. COMPREHENSIVE INCOME

The components of comprehensive income were as follows:

|  | Three Months Ended<br>December 31, |          | Nine Months Ended<br>December 31, |          |
|--|------------------------------------|----------|-----------------------------------|----------|
|  | 2009                               | 2008     | 2009                              | 2008     |
| Net income   | \$ 47,788                          | \$59,575 | \$61,289                          | \$95,482 |
| Equity currency conversion adjustment                        | (1,264)                            | (3,312)  | 2,162                             | (6,403)  |
| Pension adjustment, net of tax                               | (359)                              | -        | (359)                             | -        |
| Total comprehensive income                                   | 46,165                             | 56,263   | 63,092                            | 89,079   |
| Comprehensive income attributable to noncontrolling interest | 521                                | 113      | 1,029                             | 358      |
| Total comprehensive income attributable to the Company       | \$ 45,644                          | \$56,150 | \$62,063                          | \$88,721 |

Alliance One International, Inc. and Subsidiaries

## 8. STOCK-BASED COMPENSATION

The Company recorded stock-based compensation expense related to stock-based awards granted under its various employee and non-employee stock incentive plans of \$1,823 and \$784 for the three months ended December 31, 2009 and 2008, respectively, and \$5,233 and \$2,656 for the nine months ended December 31, 2009 and 2008, respectively.

The Company's shareholders amended the 2007 Incentive Plan (the 2007 Plan) at its Annual Meeting of Shareholders on August 6, 2009. The 2007 Plan is an omnibus plan that provides the flexibility to grant a variety of equity awards including stock options, stock appreciation rights, stock awards, stock units, performance awards and incentive awards to officers, directors and employees of the Company.

During the nine months ended December 31, 2009 and 2008, respectively, the Company made the following stock-based compensation awards:

|   | Nine Months Ended<br>December 31, |        |
|---|-----------------------------------|--------|
|   | 2009                              | 2008   |
| <b>Restricted Stock</b>                         |                                   |        |
| Number Granted                                  | 192                               | 146    |
| Grant Date Fair Value                           | \$4.25                            | \$4.47 |
| <b>Restricted Stock Units</b>                   |                                   |        |
| Number Granted                                  | 106                               | 99     |
| Grant Date Fair Value                           | \$4.26                            | \$4.47 |
| <b>Performance Shares</b>                       |                                   |        |
| Number Granted                                  | 1,758                             | 1,197  |
| Grant Date Fair Value                           | \$4.19                            | \$4.47 |
| <b>Performance Based Restricted Stock Units</b> |                                   |        |
| Number Granted                                  | -                                 | 150    |
| Grant Date Fair Value                           | -                                 | \$4.47 |

Under the terms of both the Performance Shares and Performance Based Restricted Stock Units, shares ultimately issued will be contingent upon specified business performance goals. If minimum standards are not attained, compensation paid under these awards will be zero. Alternatively, if the maximum performance levels described by the plan are attained, the awards may be 150% of the stated award.

### Stock Options with Stock Appreciation Rights

Stock appreciation rights (SARs) have historically been granted in tandem with certain option grants under which the employee may choose to receive in cash the excess of the market price of the share on the exercise date over the market price on the grant date (the intrinsic value of the share) rather than purchase the shares. The choice to receive cash is limited to five years after grant. The fair value of SARs is determined at each balance sheet date using a Black-Scholes valuation model multiplied by the cumulative vesting of each SAR award.

Assumptions used to determine the fair value of SARs as of December 31 included the following:

2009

2008

|                        |   |        |
|------------------------|---|--------|
| Stock Price            | - | \$2.94 |
| Exercise Price         | - | \$6.45 |
| Expected Life in Years | - | .9     |
| Annualized Volatility  | - | 65%    |
| Annual Dividend Rate   | - | -      |
| Discount Rate          | - | .32%   |

Because the exercise price of these SARs is above the current stock price, the expected life has been determined to be the maximum time period the SARs may be exercised. The discount rate used is the risk free treasury bill rate consistent with the expected life. Volatility is based on historical volatility of the Company's stock price.

All SARs had expired as of December 31, 2009.



Alliance One International, Inc. and Subsidiaries

## 9. CONTINGENCIES

### **Non-Income Tax**

In September 2006, the Company's Serbian operations were assessed for VAT and government pension liability for payments to farmers. The Company has appealed the assessment from the tax authorities based upon favorable discussions with the Ministry of Finance and is awaiting the final decision from the Supreme Court. As of December 31, 2009, the balance of the reserve is \$220.

The government in the Brazilian State of Parana ( Parana ) issued a tax assessment on October 26, 2007 with respect to local intrastate trade tax credits that result primarily from tobacco transferred between states within Brazil. The assessment for intrastate trade tax credits taken is \$7,567 and the total assessment including penalties and interest through December 31, 2009 is \$15,485. The Company believes it has properly complied with Brazilian law and will contest any assessment through the judicial process. Should the Company lose in the judicial process, the loss of the intrastate trade tax credits would have a material impact on the financial statements of the Company.

The assessment of \$7,567 represents intrastate trade tax credit amounts which were offset against intrastate trade tax payables. At December 31, 2009, the Company also has intrastate trade tax credits from Parana of \$12,742. During fiscal 2008, the Company recorded an impairment charge of \$7,143. After the assessment, the Company has treated new expenditures for intrastate trade taxes on tobacco acquisition as a cost of inventory procurement.

The Company also has local intrastate trade tax credits in the Brazil State of Rio Grande do Sul ( Rio Grande ) of \$59,077 and \$44,807 at December 31, 2009 and 2008, respectively. Based on management's expectations about future realization, the Company has recorded a valuation allowance on the Rio Grande intrastate trade tax credits of \$7,419 and \$7,232 at December 31, 2009 and 2008, respectively. The allowance on the Rio Grande intrastate trade tax credits may be adjusted in future periods based on market conditions and the Company's ability to use the tax credits.

In 2001, the Company's subsidiary in Brazil won a claim related to certain excise taxes ( IPI credit bonus ) for the years 1983 through 1990. The Company used this IPI credit bonus to offset federal income and other taxes until January 2005 when it received a Judicial Order to suspend the IPI compensation. The Company appealed and the case is currently before the Supreme Court. In addition, the Company received an assessment in 2006 for federal income taxes in 2005 that were offset by the IPI credit bonus. The assessment is valued at \$27,926 at December 31, 2009. The Company appealed the assessment and believes it has properly utilized the IPI credit bonus. No benefit for the utilization of the IPI credit bonus has been recognized as it has been recorded in pension, postretirement and other long term liabilities. As a result of various legislative and judicial actions, the Company does not expect a ruling by the Supreme Court in the near future, which would directly impact the outcome of the Company's appeal of the tax assessment as well as its utilization of its remaining IPI credit bonus. No benefit for any potential future utilization of IPI credit bonus has been recognized.

### **Other**

In October 2001, the Directorate General for Competition ( DGCOMP ) of the European Commission ( EC ) began an administrative investigation into certain tobacco buying and selling practices alleged to have occurred within the leaf tobacco industry in some countries within the European Union, including Spain, Italy, Greece and potentially other countries. The Company and its subsidiaries in Spain, Italy and Greece have been subject to these investigations. In respect of the investigation into practices in Spain, in 2004, the EC fined the Company and its Spanish subsidiaries €4,415 (US\$5,641). In respect of the investigation into practices in Italy, in October 2005, the EC announced that the Company and its Italian subsidiaries have been assessed a fine in the aggregate amount of €24,000 (US\$28,800). With respect to both the Spanish and Italian investigations, the fines imposed on the Company and its predecessors and subsidiaries were part of fines assessed on several participants in the applicable industry. With respect to the investigation relating to Greece, the EC informed the Company in March 2005 it had closed its investigation in relation to the Greek leaf tobacco industry buying and selling practices. The Company, along with its applicable subsidiaries, has appealed the decisions of the EC with respect to Spain and Italy to the Court of First Instance of the European Commission for the annulment or modification of the decision, but the outcome of the appeals process as to both timing and results is uncertain. The Company has fully recognized the impact of each of the fines set forth above and has paid all of such fines as part of the appeal process.

The Company had previously disclosed that it had received notice from Mindo, S.r.l., the purchaser in June 2004 of the Company's Italian subsidiary Dimon Italia, S.r.l., of its intent to assert against the Company, or its subsidiaries, a claim arising out of that sale transaction. That claim, which may be followed by additional claims, was filed before the Court of Rome on April 12, 2007. The claim, allegedly arising from a guaranty letter issued by a consolidated subsidiary of the Company in connection with the sale transaction, seeks the recovery of €7,377 (US\$10,573) plus interest and costs. The Company believes the claim to be without merit and intends to vigorously defend it. No amounts have been reserved with respect to such claim.

In March 2004, the Company discovered potential irregularities with respect to certain bank accounts in southern Europe and central Asia. The Audit Committee of the Company's Board of Directors engaged an outside law firm to conduct an investigation of activity relating to these accounts. That investigation revealed that, although the amounts involved were not material and had no material impact on the Company's historical financial statements, there were payments from these accounts that may have violated the U.S. Foreign Corrupt Practices Act. In May 2004, the Company voluntarily reported the

Alliance One International, Inc. and Subsidiaries

## 9. CONTINGENCIES *(Continued)*

### **Other** *(Continued)*

matter to the U.S. Department of Justice ( Justice ). Soon thereafter, the Company closed the accounts in question, implemented personnel changes and other measures designed to prevent similar situations in the future, including the addition of new finance and internal audit staff and enhancement of existing training programs, and disclosed these circumstances in its filings with the SEC. In August 2006, the Company learned that the SEC had issued a formal order of investigation of the Company and others to determine if these or other actions, including those in other countries in which the Company does business, may have violated certain provisions of the Securities Exchange Act of 1934 and rules thereunder. In May 2008, the Company learned that Justice is conducting an investigation into possible violations of federal laws stemming from the same actions being investigated by the SEC.

The Company has been advised by Justice and the SEC that such agencies believe that violations of applicable federal laws have occurred. The Company is engaging in discussions with Justice and the SEC to effect a resolution which may involve, among other things, injunctive relief, disgorgement, fines, penalties and modifications to business practices and the appointment of a monitor. Because of existing uncertainty with respect to the scope of any possible violations and with respect to the methodology for determining the amount of potential fines, penalties or disgorgement related to any such violations, an estimate of the amount of loss, or a reliable range of estimated loss, cannot be made. Accordingly, the Company has not accrued any loss, though it believes that a loss is probable. The resolution could materially adversely affect the Company's results of operations. The Company intends to continue to cooperate with the authorities as resolution discussions proceed.

On December 13, 2007, the Public Prosecutors' offices in the States of Santa Catarina and Parana filed claims against the Company's Brazilian subsidiary, Alliance One Brazil Exportadora de Tabacos Ltda. and a number of other tobacco processors, on behalf of all tobacco farmers in those states. The lawsuits primarily assert that there exists an employment relationship between tobacco processors and tobacco farmers. The Company believes these claims to be without merit and intends to vigorously defend them. Ultimate exposure if an unfavorable outcome is received is not determinable.

At the initial hearing in Santa Catarina, on January 29, 2008, the Court granted the Company's motion to have the case removed to the Labor Court in Brasilia. No hearing date has yet been set.

In the state of Parana, the relief sought by the Public Prosecutor was granted by the local Labor Court. The Company appealed that initial ruling and it was overturned in part and affirmed in part. The Company has appealed from that part of the initial ruling which was affirmed and no ruling has yet been rendered on the appeal. The Company has separately asserted, on April 11, 2008, a lack of jurisdiction motion similar to that which it asserted in the case in Santa Catarina which resulted in the transfer of that case to the Labor Court in Brasilia. No hearing date for that motion has been set.

On July 23, 2009, the Company received notice that Sharpmind Enterprises, Ltd., a British Virgin Islands company, had filed in the United States District Court for the Eastern District of North Carolina, a claim against the Company seeking unspecified damages for an alleged breach of a sales representation agreement between the Company and Sharpmind. Sharpmind has indicated that it would seek damages in excess of \$2,000. The Company views the claim as baseless and intends to vigorously defend it.

The Company and certain of its foreign subsidiaries guarantee bank loans to growers to finance their crops. Under longer-term arrangements, the Company may also guarantee financing on growers' construction of curing barns or other tobacco production assets. The Company also guarantees bank loans to certain tobacco cooperatives to assist with the financing of their growers' crops. Guaranteed loans are generally repaid concurrent with the delivery of tobacco to the Company. The Company is obligated to repay any guaranteed loan should the grower or tobacco cooperative default. If default occurs, the Company has recourse against the grower or cooperative. At December 31, 2009, the Company was guarantor of an amount not to exceed \$188,701 with \$173,555 outstanding under these guarantees.

In accordance with generally accepted accounting principles, the Company records all known asset retirement obligations ( ARO ) for which the liability can be reasonably estimated. Currently, it has identified an ARO associated with one of its facilities that requires it to restore the land to its initial condition upon vacating the facility. The Company has not recognized a liability under generally accepted accounting principles for this ARO because the fair value of restoring the land at this site cannot be reasonably estimated since the settlement date is unknown at this time. The settlement date is unknown because the land restoration is not required until title is returned to the government, and the Company has no current or future plans to return the title. The Company will recognize a liability in the period in which sufficient information is available to reasonably estimate its fair value. The Company has no additional material AROs.

On November 6, 2009, the Company's subsidiary in Brazil announced the construction of a new tobacco processing facility in the State of Santa Catarina. The new facility will require an investment of R\$100,000 (approximately US\$57,160) and will have a production capacity of 70 tons. The Company estimates that the facility will be operational for processing the 2011 crop and approximately 1,500 permanent and temporary jobs will be created. Additionally, the Company projects sufficient excess liquidity from both cash and available credit lines to meet construction and development cost while maintaining an appropriate liquidity cushion.

Alliance One International, Inc. and Subsidiaries

## 10. DEBT ARRANGMENTS

The Company completed a number of refinancing transactions, which are described below.

### **Senior Secured Credit Facility**

On July 2, 2009, the Company entered into a Credit Agreement (the *Credit Agreement*), with a syndicate of banks that replaced the Company's \$305,000 Amended and Restated Credit Agreement dated March 30, 2007 and provides for a senior secured credit facility (the *Credit Facility*) that consists of:

.  
a three and one-quarter year \$270,000 revolver (the *Revolver*) which initially accrues interest at a rate of LIBOR plus 2.50%.

The interest rate for the *Revolver* may increase or decrease according to a consolidated interest coverage ratio pricing matrix as defined in the *Credit Agreement*. The *Credit Agreement* permits the Company to add \$55,000 in commitments from existing or additional lenders which would increase the amount of the *Revolver* to \$325,000.

*First Amendment.* On August 24, 2009, the Company closed the First Amendment to the *Credit Agreement* which included the following modifications effective August 24, 2009:

.  
Amended the definition for Senior Notes to allow for the issuance of up to an additional \$100,000 of Senior Notes due 2016 within 90 days of the First Amendment Effective Date;

.  
Amended the definition of Consolidated Total Senior Debt to exclude the Existing Senior Notes 2005;

.  
Amended the definition of Applicable Percentage to clarify the effective date of the change in the Applicable Percentage;

Modifications to several schedules within the Credit Agreement.

*Borrowers and Guarantors.* One of the Company's primary foreign holding companies, Intabex Netherlands B.V. ( Intabex ), is co-borrower under the Revolver, and the Company's portion of the borrowings under the Revolver is limited to \$200,000 outstanding at any one time. One of the Company's primary foreign trading companies, Alliance One International AG ( AOIAG ), is a guarantor of Intabex's obligations under the Credit Agreement. Such obligations are also guaranteed by the Company and must be guaranteed by any of its material direct or indirect domestic subsidiaries.

*Collateral.* The Company's borrowings under the Credit Facility are secured by a first priority pledge of:

100% of the capital stock of any domestic subsidiary held directly by the Company or by any material domestic subsidiary;

100% of the capital stock of any material domestic subsidiary;

100% of the capital stock of any material foreign subsidiary held directly by the Company or any domestic subsidiary; provided that not more than 65% of the voting stock of any material foreign subsidiary is required to be pledged to secure obligations of the Company or any domestic subsidiary;

U.S. accounts receivable and U.S. inventory owned by the Company or its material domestic subsidiaries (other than inventory the title of which has passed to a customer and inventory financed through customer advances and certain other exceptions); and

Intercompany notes evidencing loans or advances the Company makes to subsidiaries.

In addition, Intabex's borrowings under the Credit Facility are secured by a pledge of 100% of the capital stock of Intabex, AOIAG, certain of the Company's and Intabex's material and other foreign subsidiaries and the collateral described above for the Company's borrowings.

*Financial Covenants.* The Credit Facility includes certain financial covenants and required financial ratios, including:

.  
a minimum consolidated interest coverage ratio of not less than 1.90 to 1.00;

.  
a maximum consolidated leverage ratio in an amount not more than a ratio specified for each fiscal quarter, which ratio is 5.75 to 1.00 for the fiscal quarter ended December 31, 2009;

.  
a maximum consolidated total senior debt to working capital amount ratio of not more than 0.80 to 1.00; and

.  
a maximum amount of annual capital expenditures of \$75,000 during fiscal year ending March 31, 2010 and \$40,000 during any fiscal year thereafter, with a one-year carry-forward for capital expenditures in any fiscal year below the maximum amount.

Alliance One International, Inc. and Subsidiaries

10. DEBT ARRANGMENTS *(Continued)*

**Senior Secured Credit Facility** *(Continued)*

Certain of these financial covenants and required financial ratios adjust over time in accordance with schedules in the Credit Agreement.

The Credit Agreement also contains certain customary affirmative and negative covenants, including, without limitation, restrictions on additional indebtedness, guarantees, liens and asset sales.

The Company continuously monitors its compliance with these covenants. If the Company fails to comply with any of these covenants and is unable to obtain the necessary amendments or waivers under the Credit Agreement, the lenders under the Credit Agreement have the right to accelerate the outstanding loans thereunder and demand repayment in full and to terminate their commitment to make any further loans under the Credit Facility. Certain defaults under the Credit Facility would result in a cross default under the indentures governing the Company's senior notes and convertible senior subordinated notes and could impair access to its seasonal operating lines of credit in local jurisdictions. A default under the Credit Agreement would have a material adverse effect on the Company's liquidity and financial condition. The Company records all fees and third-party costs associated with the Credit Agreement, including amendments thereto, in accordance with accounting guidance for changes in line of credit or revolving debt arrangements.

As a result of terminating the \$305,000 Amended and Restated Credit Agreement dated March 30, 2007, the Company accelerated approximately \$5,741 of deferred financing costs.

**Senior Notes**

On July 2, 2009, the Company issued \$570,000 of 10% Senior Notes due 2016 (the "Senior Notes"). The Senior Notes were priced at 95.177% of the face value, for gross proceeds of approximately \$542,509 and representing a yield to maturity of 11.0%. On August 26, 2009, the Company issued an additional \$100,000 tranche of 10% Senior Notes due 2016. The notes were priced at 97.500% of the face value, for gross proceeds of approximately \$97,500 and representing a yield to maturity of 10.512%. These additional notes form part of the same series as the Senior Notes issued on July 2, 2009. The aggregate principal amount of the outstanding Senior Notes is \$670,000. The Senior Notes are required to be guaranteed by any material domestic subsidiaries of the Company as defined in the indenture governing the Senior Notes. Because no subsidiary is, or has been at any relevant time, a material domestic subsidiary, the Senior Notes are not guaranteed by any subsidiaries of the Company, though such a guarantee would be required if any subsidiary subsequently qualifies as a material domestic subsidiary. The indenture governing the Senior Notes contains covenants that, among other things, limit the Company's ability to incur additional indebtedness; issue preferred stock; merge, consolidate or dispose of substantially all of its assets; grant liens on its assets; pay dividends, redeem stock or make other distributions or restricted payments; repurchase or redeem capital stock or prepay subordinated debt; make certain investments; agree to restrictions on the payment of dividends to the Company by its subsidiaries; sell or otherwise dispose of assets, including equity interests of its subsidiaries; enter into



transactions with its affiliates; and enter into certain sale and leaseback transactions. If a change of control (as defined in the indenture governing the Senior Notes) occurs at any time, holders of the Senior Notes will have the right, at their option, to require the Company to repurchase all or a portion of the Senior Notes for cash at a price equal to 101% of the principal amount of Senior Notes being repurchased, plus accrued and unpaid interest.

### **Convertible Senior Subordinated Notes**

On July 2, 2009, the Company issued \$100,000 of 5 ½% Convertible Senior Subordinated Notes due 2014 (the Convertible Notes ). The Company granted the initial purchasers of the Convertible Notes an option to purchase up to an additional \$15,000 of Convertible Notes solely to cover over-allotments. The initial purchasers exercised the option and purchased an additional \$15,000 of the Convertible Notes on July, 15, 2009. Holders may surrender their Convertible Notes, in integral multiples of \$1,000 principal amount, for conversion into shares of the Company's common stock at the then-applicable conversion rate until the close of business on the second scheduled trading day immediately preceding the maturity date. The initial conversion rate for the Convertible Notes is 198.8862 shares of common stock per \$1,000 principal amount of Convertible Notes. The conversion rate is subject to adjustments based on certain events as described in the indenture governing the Convertible Notes. In addition, upon the occurrence of certain fundamental changes (as defined in the indenture governing the Convertible Notes), a holder that converts its notes in connection with such a fundamental change may be entitled to receive a make-whole premium in the form of an increase in the conversion rate. In addition, if such a fundamental change occurs at any time, holders of the Convertible Notes will have the right, at their option, to require the Company to repurchase all or a portion of the Convertible Notes for cash at a price equal to 100% of the principal amount of the Convertible Notes to be repurchased plus accrued and unpaid interest.

Alliance One International, Inc. and Subsidiaries

10. DEBT ARRANGMENTS *(Continued)***Convertible Note Hedge and Warrant Transactions**

In connection with the offering of the Convertible Notes, the Company entered into privately negotiated convertible note hedge transactions (the convertible note hedge transactions) with three counterparties, one initial purchaser of the Convertible Notes and affiliates of two other initial purchasers (the hedge counterparties). The convertible note hedge transactions cover, subject to customary anti-dilution adjustments, the number of shares of the Company's common stock that initially underlie the Convertible Notes. The Company also entered separately into privately negotiated warrant transactions (the warrant transactions) relating to the same number of shares of the Company's common stock with the hedge counterparties. The convertible note hedge transactions are expected to reduce the potential dilution with respect to the common stock of the Company upon conversion of the Convertible Notes in the event that the value per share of common stock, as measured under the convertible note hedge transactions, during the applicable valuation period, is greater than the strike price of the convertible note hedge transactions, which corresponds to the \$5.0280 per share initial conversion price of the Convertible Notes and is similarly subject to customary anti-dilution adjustments. If, however, the price per share of the Company's common stock, as measured under the warrants, exceeds the strike price of the warrant transactions during the applicable valuation period, there would be dilution from the issuance of common stock pursuant to the warrants. The warrants have a strike price of \$7.3325 per share, which is subject to customary anti-dilution adjustments. The warrants expire in daily installments commencing on October 15, 2014 and ending on April 8, 2015.

**Tender of Existing Notes**

On July 2, 2009, the Company applied a portion of the net proceeds from the issuance of the Senior Notes and Convertible Notes to fund the purchase \$467,544 aggregate principal amount of its existing notes pursuant to an early settlement of a cash tender offer (the Tender Offer) for any and all of its 11% Senior Notes due 2012, 8 ½% Senior Notes due 2012, 12 ¾% Senior Subordinated Notes due 2012, 9 % Senior Notes due 2011, 7 ¾% Senior Notes due 2013 and 8% Senior Notes due 2012, Series B (collectively, the "Existing Notes"). On July 9, 2009, the Company applied a portion of the remaining net proceeds to fund the purchase of an additional \$1,127 aggregate principal amount of Existing Notes in connection with the final settlement of the Tender Offer. The following table sets forth the principal amount of the Existing Notes outstanding at the commencement of the Tender Offer and the principal amount of the Existing Notes that the Company purchased:

| Existing Notes                | Issuer (1) | Principal Amount Outstanding | Principal Amount Purchased |
|-------------------------------|------------|------------------------------|----------------------------|
| 11% Senior Notes due 2012 (2) | A          | \$264,381                    | \$258,126                  |
| 8 ½% Senior Notes due 2012    | A          | \$150,000                    | \$120,365                  |
|                               | A          | \$ 89,500                    | \$ 82,105                  |

12 ¾% Senior Subordinated Notes due  
2012 (2)

|  |   |          |          |
|--|---|----------|----------|
| 9 % Senior Notes due 2011 (3)          | D | \$ 3,437 | \$ 3,415 |
| 7 ¾% Senior Notes due 2013 (3)         | D | \$ 435   | \$ 375   |
| 8% Senior Notes due 2012, Series B (3) | S | \$ 6,285 | \$ 4,285 |

(1) The issuer of a series of Existing Notes designated with an A is Alliance One International, Inc. In 2005, Standard Commercial Corporation ( Standard Commercial ) merged with and into DIMON Incorporated ( DIMON ), which changed its name to Alliance One International, Inc. The issuer of a series of Existing Notes designated with a D was originally DIMON and the issuer of a series of Existing Notes designated with an S was originally Standard Commercial.

(2) On July 31, 2009 funds were paid to the Trustee to defease the remaining outstanding principal and interest. The Notes were redeemed in full on August 3, 2009.

(3) On December 4, 2009 funds were paid to redeem in full the remaining outstanding principal and interest as well as the applicable redemption premium.

As a result of the repurchase, defeasance and redemption of the Existing Notes as described in the foregoing table, the Company accelerated approximately \$5,591 of deferred financing costs and \$5,563 of amortization of original issue discount.

#### **Amendment of Certain Existing Notes**

On July 2, 2009, in connection with the early settlement of the Tender Offer with respect to the Company's 11% Senior Notes due 2012, 8 ½% Senior Notes due 2012 and 12 ¾% Senior Subordinated Notes due 2012 (the Alliance One Notes ), certain amendments to the indentures governing the Alliance One Notes became operative and effective. These amendments eliminated substantially all of the restrictive covenants, eliminated requirements for subsidiary guarantees and requirements to conduct repurchase offers following certain events, including a change in control, modified redemption notice periods from 30 days to three business days, eliminated or modified certain events of default and certain conditions to defeasance of the Alliance One Notes, and eliminated or modified related provisions contained in the indentures governing the Alliance One Notes.

## Alliance One International, Inc. and Subsidiaries

## 10. DEBT ARRANGMENTS (Continued)

**Foreign Seasonal Lines of Credit**

The Company has typically financed its non-U.S. operations with uncommitted unsecured short-term seasonal lines of credit at the local level. These operating lines are seasonal in nature, normally extending for a term of 180 to 270 days corresponding to the tobacco crop cycle in that location. These facilities are typically uncommitted in that the lenders have the right to cease making loans and demand repayment of loans at any time. These loans are typically renewed at the outset of each tobacco season. As of December 31, 2009, the Company had approximately \$286,406 drawn and outstanding on foreign seasonal lines with maximum capacity totaling \$649,984 subject to limitations as provided for in the Credit Agreement. Additionally, against these lines there was \$20,186 available in unused letter of credit capacity with \$11,188 issued but unfunded.

**Summary of Debt**

The carrying value and estimated fair value of the Company's long-term debt are \$825,573 and \$912,291, respectively, as of December 31, 2009 and \$670,426 and \$613,336, respectively, as of March 31, 2009.

The following table summarizes the Company's debt financing as of December 31, 2009:

|   | December 31, 2009          |                               | Lines and Letters Available | Interest Rate |
|---|----------------------------|-------------------------------|-----------------------------|---------------|
|   | Outstanding March 31, 2009 | Outstanding December 31, 2009 |                             |               |
| Senior secured credit facility:                     |                            |                               |                             |               |
| Revolver  | \$120,000                  | \$ -                          | \$270,000                   |               |
| Senior notes:                                       |                            |                               |                             |               |
| 10% senior notes due 2016                           | -                          | 641,466                       | -                           | 10.0%         |
| 11% senior notes due 2012                           | 264,381                    | -                             | -                           | 11.0%         |
| 8 ½% senior notes due 2012                          | 149,520                    | 29,561                        | -                           | 8.5%          |
| Other (1)   | 10,157                     | -                             | -                           |               |
|   | 424,058                    | 671,027                       | -                           |               |
| 5 ½% convertible senior subordinated notes due 2014 | -                          | 115,000                       | -                           | 5.5%          |
| 12 ¾% senior subordinated notes due 2012            | 83,999                     | -                             | -                           | 12.8%         |

|                            |           |             |           |      |     |
|----------------------------|-----------|-------------|-----------|------|-----|
| Other long-term debt       | 42,369    | 39,545      | 1,898     | 9.1% | (2) |
| Notes payable to banks (3) | 261,468   | 286,406     | 343,391   | 6.2% | (2) |
| Total debt                 | \$931,894 | \$1,111,978 | 615,289   |      |     |
| Short term                 | \$261,468 | \$ 286,406  |           |      |     |
| Long term:                 |           |             |           |      |     |
| Long term debt current     | \$ 17,842 | \$ 19,335   |           |      |     |
| Long term debt             | 652,584   | 806,238     |           |      |     |
|                            | \$670,426 | \$ 825,573  |           |      |     |
| Letters of credit          | \$ 3,814  | \$ 11,188   | 8,998     |      |     |
| Total credit available     |           |             | \$624,287 |      |     |

(1) Notes redeemed in total as of December 4, 2009

(2) Weighted average rate for the nine months ended December 31, 2009

(3) Primarily foreign seasonal lines of credit

Prior to the debt refinancing, the discount amortization and repayment of the senior notes and the senior subordinated notes by fiscal year was \$(1,609) in 2011, \$1,581 in 2012, \$509,045 in 2013 and \$435 in 2014. After the debt refinancing, the discount amortization and repayment of the senior notes and convertible senior subordinated notes by fiscal year is \$(3,308) in 2011, \$(3,664) in 2012, \$27,559 in 2013, \$(4,480) in 2014 and \$772,786 in later fiscal years.

Alliance One International, Inc. and Subsidiaries

## 11. DERIVATIVE FINANCIAL INSTRUMENTS

**Fair Value of Derivative Financial Instruments**

The Company recognizes all derivative financial instruments, such as interest rate swap contracts and foreign exchange contracts at fair value. Changes in the fair value of derivative financial instruments are either recognized periodically in income or in shareholders' equity as a component of other comprehensive income depending on whether the derivative financial instrument qualifies for hedge accounting, and if so, whether it qualifies as a fair value hedge or a cash flow hedge. Changes in fair values of derivatives accounted for as fair value hedges are recorded in income along with the portions of the changes in the fair values of the hedged items that relate to the hedged risk(s). Changes in fair values of derivatives accounted for as cash flow hedges, to the extent they are effective as hedges, are recorded in other comprehensive income net of deferred taxes. Changes in fair values of derivatives not qualifying as hedges are reported in income. During the three months and nine months ended December 31, 2009 and 2008, there were no qualified cash flow or fair value hedges. Estimates of fair value were determined in accordance with generally accepted accounting principles. See Note 15 "Fair Value Measurements" to the Notes to Condensed Consolidated Financial Statements for further information of fair value methodology. The following table summarizes the fair value of the Company's derivatives by type at December 31, 2009.

|  | Fair Values of Derivative Instruments |            |                              |            |
|--|---------------------------------------|------------|------------------------------|------------|
|  | Assets                                |            | Liabilities                  |            |
| Derivatives Not Designated as Hedging Instruments: | Balance Sheet Account                 | Fair Value | Balance Sheet Account        | Fair Value |
| Foreign currency contracts (a)                     | Current Derivative Asset              | \$1,075    | Current Derivative Liability | \$2,716    |

(a) At December 31, 2009, the cumulative adjustment for non-performance risk was a loss of \$7.

**Earnings Effects of Derivatives*****Foreign Currency Contracts***

The Company periodically enters into forward or option currency contracts to protect against volatility associated with certain non-U.S. dollar denominated forecasted transactions. When these derivatives qualify for hedge accounting treatment, they are accounted for as cash flow hedges and are recorded in other comprehensive income, net of deferred taxes.

The Company has entered into forward currency contracts to hedge cash outflows in foreign currencies around the world for green tobacco purchases and processing costs as well as selling, administrative and general costs as the Company deems necessary. These contracts do not meet the requirements for hedge accounting treatment under generally accepted accounting principles, and as such, all changes in fair value are reported in income.

The following table summarizes the earnings effects of derivatives in the condensed consolidated statements of operations for the three months and nine months ended December 31, 2009 and 2008.

| Derivatives Not Designated as Hedging Instruments | Location of Gain (Loss) Recognized in Income | Gain (Loss) Recognized in Income     |            |                                     |            |
|---|--|--------------------------------------|------------|-------------------------------------|------------|
|   |  | Three Months Ended December 31, 2009 |            | Nine Months Ended December 31, 2008 |            |
| Foreign currency contracts                        | Cost of goods and services sold              | \$ (2,980)                           | \$ (1,330) | \$ 12,889                           | \$ (2,472) |
| Foreign currency contracts                        | Selling, administrative and general expenses | 200                                  | 15         | 3,599                               | (57)       |
| Total   |  | \$ (2,780)                           | \$ (1,315) | \$ 16,488                           | \$ (2,529) |

### Credit Risk

Financial instruments, including derivatives, expose the Company to credit loss in the event of non-performance by counterparties. The Company manages its exposure to counterparty credit risk through specific minimum credit standards, diversification of counterparties, and procedures to monitor concentrations of credit risk. If a counterparty fails to meet the terms of an arrangement, the Company's exposure is limited to the net amount that would have been received, if any, over the arrangement's remaining life. The Company does not anticipate non-performance by the counterparties and no material loss would be expected from non-performance by any one of such counterparties.

## Alliance One International, Inc. and Subsidiaries

## 12. PENSION AND POSTRETIREMENT BENEFITS

The Company has a defined benefit plan that provides retirement benefits for substantially all U.S. salaried personnel based on years of service rendered, age and compensation. The Company also maintains various other Excess Benefit and Supplemental Plans that provide additional benefits to (1) certain individuals whose compensation and the resulting benefits that would have actually been paid are limited by regulations imposed by the Internal Revenue Code and (2) certain individuals in key positions. The Company funds these plans in amounts consistent with the funding requirements of federal law and regulations.

Additional non-U.S. defined benefit plans sponsored by certain subsidiaries cover certain full-time employees located in Germany, Greece, Turkey, Malawi and the United Kingdom.

Components of Net Periodic Benefit Cost

Net periodic pension cost for continuing operations consisted of the following:

|                                    | Three Months Ended |          | Nine Months Ended |          |
|------------------------------------|--------------------|----------|-------------------|----------|
|                                    | December 31,       |          | December 31,      |          |
|                                    | 2009               | 2008     | 2009              | 2008     |
| Service cost                       | \$ 895             | \$ 1,125 | \$ 2,685          | \$ 3,375 |
| Interest expense                   | 2,236              | 2,284    | 6,707             | 6,852    |
| Expected return on plan assets     | (1,114)            | (1,622)  | (3,340)           | (4,866)  |
| Amortization of prior service cost | (44)               | (71)     | (133)             | (214)    |
| Actuarial gain                     | (2)                | (84)     | (6)               | (251)    |
| Net periodic pension cost          | \$ 1,971           | \$ 1,632 | \$ 5,913          | \$ 4,896 |

Employer Contributions

The Company's investment objectives are to generate consistent total investment return to pay anticipated plan benefits, while minimizing long-term costs. Financial objectives underlying this policy include maintaining plan contributions at a reasonable level relative to benefits provided and assuring that unfunded obligations do not grow to a level to adversely affect the Company's financial health. As of December 31, 2009, contributions of \$5,925 were made to pension plans for fiscal 2010. Additional contributions to pension plans of approximately \$1,760 are expected during the remainder of fiscal 2010. However, this amount is subject to change, due primarily to potential plan combinations, asset performance significantly above or below the assumed long-term rate of return on pension assets and significant changes in interest rates.



Postretirement Health and Life Insurance Benefits

The Company also provides certain health and life insurance benefits to retired employees, and their eligible dependents, who meet specified age and service requirements. As of December 31, 2009, contributions of \$911 were made to the plans for fiscal 2010. Additional contributions of \$330 to the plans are expected during the rest of fiscal 2010. The Company retains the right, subject to existing agreements, to modify or eliminate the postretirement medical benefits.

Components of Net Periodic Benefit Cost

Net periodic benefit cost for postretirement health and life insurance benefit plans consisted of the following:

|                                     | Three Months Ended<br>December 31, |         | Nine Months Ended<br>December 31, |          |
|-------------------------------------|------------------------------------|---------|-----------------------------------|----------|
|                                     | 2009                               | 2008    | 2009                              | 2008     |
| Service cost                        | \$ 16                              | \$ 32   | \$ 48                             | \$ 97    |
| Interest expense                    | 189                                | 205     | 564                               | 616      |
| Amortization of prior service cost  | (415)                              | (405)   | (1,245)                           | (1,217)  |
| Actuarial loss                      | 76                                 | 94      | 229                               | 282      |
| Curtailement (gain)/loss recognized | (777)                              | -       | (777)                             | -        |
| Settlement (gain)/loss recognized   | (290)                              | -       | (290)                             | -        |
| Net periodic pension cost (benefit) | \$ (1,201)                         | \$ (74) | \$ (1,471)                        | \$ (222) |

## Alliance One International, Inc. and Subsidiaries

## 13. ADVANCES ON PURCHASES OF TOBACCO

The Company provides seasonal crop advances of, or for, seed, fertilizer, and other supplies. These advances are short term in nature, are repaid with delivery of tobacco to the Company, and are reported in advances on purchases of tobacco in the condensed consolidated balance sheet. Primarily in Brazil and certain African countries, the Company also has made long-term advances to tobacco farmers to finance curing barns and other farm infrastructure. In addition, due to low crop yields and other factors, in some years individual farmers may not deliver sufficient volumes of tobacco to fully repay their seasonal advances, and the Company may extend repayment of those advances into future crop years. Current advances of \$139,449 at December 31, 2009 and \$160,934 at December 31, 2008 are presented as advances on purchases of tobacco, net in the condensed consolidated balance sheet. The long-term portion of advances of \$40,821 at December 31, 2009 and \$49,905 at December 31, 2008 are included in other non-current assets in the condensed consolidated balance sheet. Both the current and the long-term portion of advances on purchases of tobacco are reported net of allowances. Allowances of \$142,304 at December 31, 2009, and \$105,732 at December 31, 2008 were recorded based on the Company's historical loss information and crop projections. The Company records allowances when advances are issued to report them at their net realizable value. The Company continuously monitors events that may impact the farmers' ability to deliver tobacco as noted above and updates its allowances as needed. The allowances were increased by provisions for unrecoverable advances of approximately \$26,018 and \$31,505 for the nine months ended December 31, 2009 and 2008 respectively. Provisions for unrecoverable advances for inventory purchases related to the current crop are capitalized into inventory. Provisions for unrecoverable advances for inventory purchases that relate to prior crops are expensed as incurred. The allowance increased \$24,110 at December 31, 2009 and decreased \$26,339 at December 31, 2008 primarily due to exchange rate changes.

In Brazil, some farmers obtain government subsidized rural credit financing which is guaranteed by the Company. The farmers borrow these funds from local banks. Repayment of both Company advances and rural credit financing by the farmer is concurrent with delivery of tobacco to the Company. The Company remits payments to the local banks on behalf of guaranteed farmers. Terms of rural credit financing are such that repayment is due to local banks based on contractual due dates. As of December 31, 2009 and 2008, respectively, the Company had balances of \$1,420 and \$5,409 that were due to local banks on behalf of farmers. These amounts are included in accounts payable in the condensed consolidated balance sheet. As of December 31, 2009 and 2008, respectively, the Company was guarantor for Brazilian farmer loans of \$138,550 and \$118,003 with outstanding amounts of \$138,404 and \$111,578. The fair value of guarantees for rural credit financing was \$11,126 and \$12,970 as of December 31, 2009 and 2008, respectively.

In Malawi, as of December 31, 2009 and 2008, respectively, the Company was guarantor for crop input advances to farmers of \$2,075 and \$4,639. The fair values of the Malawi guarantees were \$132 and \$278 as of December 31, 2009 and 2008, respectively.

In Argentina, as of December 31, 2009 and 2008, respectively, the Company was guarantor for farmer cooperative loans of \$18,600 and \$27,400. The fair values of the Argentine guarantees were \$725 and \$932 as of December 31, 2009 and 2008, respectively.

The fair value of all guarantees is recorded in accrued expenses and other current liabilities.

#### 14. SALE OF RECEIVABLES

Alliance One International, A.G., a wholly owned subsidiary of the Company, is engaged in a revolving trade accounts receivable securitization agreement to sell receivables to a third-party limited liability company ( LLC ). The agreement, which matures March 26, 2013, is funded through third-party loans to the LLC which is committed up to a maximum of \$100,000 in funding at any time. To the extent that the balance of the loan is less than \$100,000 the Company is subject to a 0.25% fee on the unused amount. The Company retains servicing responsibilities and subordinated interests in the receivables sold. The Company receives annual service fees of 0.5% of the outstanding balance which approximates the fair value of services to be rendered at current funding levels. Historically, credit loss and prepayments of customer receivables have been negligible. Losses on the sale of receivables are recorded as a component of other income (expense) in the statement of operations of the Company.

## Alliance One International, Inc. and Subsidiaries

## 14. SALE OF RECEIVABLES (Continued)

The following table summarizes the Company's accounts receivable securitization information as of December 31:

|   | 2009       | 2008       |
|---|------------|------------|
| Receivables outstanding in facility:                                    |            |            |
| As of April 1   | \$ 100,611 | \$ 70,862  |
| Sold  | 623,550    | 518,853    |
| Collected   | (638,221)  | (493,390)  |
| As of December 31   | \$ 85,940  | \$ 96,325  |
| Retained interest as of December 31                                     | \$ 8,084   | \$ 14,649  |
| Decreases in retained interest resulting from changes in discount rate: |            |            |
| 10%   | \$ 50      | \$ 107     |
| 20%   | \$ 100     | \$ 214     |
| Criteria to determine retained interest as of December 31:              |            |            |
| Weighted average life in days   | 70         | 76         |
| Discount rate (inclusive of 0.5% servicing fee)                         | 3.1%       | 5.6%       |
| Unused balance fee  | 0.25%      | 0.25%      |
| Cash proceeds for the nine months ended December 31:                    |            |            |
| Current purchase price  | \$ 455,011 | \$ 341,751 |
| Deferred purchase price   | 158,197    | 190,682    |
| Service fees  | 376        | 357        |
| Total   | \$ 613,584 | \$ 532,790 |
| Loss on sale of receivables:  |            |            |
| Three months ended December 31  | \$ 791     | \$ 1,393   |
| Nine months ended December 31   | \$ 1,957   | \$ 2,620   |

It is the Company's intention to maximize the receivables sold under the revolving agreement meaning that amounts collected by the pool would be reinvested in the purchase of additional eligible receivables. Since April 1, 2009, the average outstanding balance of the facility utilized has been \$74,835 with a minimum outstanding balance of \$47,174 and a maximum of \$96,365.

## 15. FAIR VALUE MEASUREMENTS

The Company adopted the current accounting guidance for fair value measurements effective April 1, 2008, for financial assets and liabilities, and effective April 1, 2009, for non-financial assets and liabilities. The financial assets and liabilities measured at fair value include derivative instruments, securitized retained interests and guarantees. The non-financial assets and liabilities under the new fair value guidance primarily include assessments of investments in subsidiaries, goodwill and other intangible assets and long-lived assets for potential impairment.

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability (an exit price) in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants. A three-level valuation hierarchy based upon observable and non-observable inputs is utilized. Observable inputs reflect market data obtained from independent sources, while unobservable inputs reflect the Company's market assumptions. Preference is given to observable inputs. These two types of inputs create the following fair value hierarchy:

.  
Level 1 Quoted prices for identical assets or liabilities in active markets.

.  
Level 2 Quoted prices for similar assets or liabilities in active markets; quoted prices for identical or similar assets or liabilities in markets that are not active; and model-derived valuations whose inputs are observable or whose significant value drivers are observable.

.  
Level 3 Significant inputs to the valuation model are unobservable.

Alliance One International, Inc. and Subsidiaries

15. FAIR VALUE MEASUREMENTS *(Continued)*

The following describes the valuation methodologies the Company uses to measure different assets or liabilities at fair value.

**Derivative financial instruments**

The fair value of foreign currency and interest rate swap contracts are based on third-party market maker valuation models that discount cash flows resulting from the differential between the contract rate and the market-based forward rate or curve capturing volatility and establishing intrinsic and carrying values. The amounts include fair value adjustments related to the Company's own credit risk and counterparty credit risk.

**Securitized retained interests**

The fair value of securitized retained interests is based upon a valuation model that calculates the present value of future expected cash flows using key assumptions for credit losses, prepayment speeds and discount rates. These assumptions are based on the Company's historical experience, market trends and anticipated performance relative to the particular assets securitized.

**Guarantees**

The fair value of guarantees is based upon the premium the Company would require to issue the same guarantee in a stand-alone arm's-length transaction with an unrelated party. Fair value is based upon internally developed models. Internally developed models utilize historical loss data for similar guarantees to develop an estimate of future losses under the guarantees outstanding at the measurement date.

The following tables present the Company's assets and liabilities measured at fair value on a recurring basis:

| December 31, 2009 | December 31, 2009 |         |         | Total Assets /<br>Liabilities,<br>at Fair Value |
|-------------------|-------------------|---------|---------|---|
|                   | Level 1           | Level 2 | Level 3 |   |

**Assets**

|                                  |      |          |          |          |
|----------------------------------|------|----------|----------|----------|
| Derivative financial instruments | \$ - | \$ 1,075 | \$ -     | \$ 1,075 |
| Securitized retained interests   | -    | -        | 8,084    | 8,084    |
| Total Assets                     | \$ - | \$ 1,075 | \$ 8,084 | \$ 9,159 |

**Liabilities**

|                                  |      |          |           |           |
|----------------------------------|------|----------|-----------|-----------|
| Derivative financial instruments | \$ - | \$ 2,716 | \$ -      | \$ 2,716  |
| Guarantees                       | -    | -        | 11,984    | 11,984    |
| Total Liabilities                | \$ - | \$ 2,716 | \$ 11,984 | \$ 14,700 |

The following tables present the changes in Level 3 instruments measured on a recurring basis for the three months and nine months ended December 31, 2009.

**Changes in Level 3 instruments for the three and nine months ended December 31, 2009**

|  | Three Months Ended<br>December 31, 2009 |            | Nine Months Ended<br>December 31, 2009 |            |
|--|---|------------|--|------------|
|  | Securitized<br>Retained<br>Interests    | Guarantees | Securitized<br>Retained<br>Interests   | Guarantees |
| Beginning Balance  | \$ 11,893                               | \$ 7,019   | \$ 26,833                              | \$ 14,584  |
| Total losses (realized / unrealized<br>included in earnings) | 791                                     | -          | 1,957                                  | -          |
| Purchases, issuances, and settlements,<br>net                | (4,600)                                 | 4,965      | (20,706)                               | (2,600)    |
| Ending Balance at December 31, 2009                          | \$ 8,084                                | \$ 11,984  | \$ 8,084                               | \$ 11,984  |

The amount of total losses for the nine months ended December 31, 2009 included in earnings attributable to the change in unrealized losses relating to assets still held at December 31, 2009 was \$524 on securitized retained interests.

Gains and losses included in earnings are reported in Other Income (Expense).

## Alliance One International, Inc. and Subsidiaries

15. FAIR VALUE MEASUREMENTS *(Continued)***Non-Recurring Fair Value Measurements**

Certain assets are not measured at fair value on an ongoing basis but are subject to fair value adjustments only in certain circumstances. During the nine months ended December 31, 2009, the Company did not have any non-recurring fair value adjustments.

## 16. RELATED PARTY TRANSACTIONS

The Company's operating subsidiaries engage in transactions with related parties in the normal course of business. The following is a summary of balances and transactions with related parties of the Company:

|                     | December 31, 2009 | December 31, 2008 | March 31, 2009    |           |
|---------------------|-------------------|-------------------|-------------------|-----------|
| Balances:           |                   |                   |                   |           |
| Accounts receivable | \$33,116          | \$21,855          | \$29,765          |           |
| Accounts payable    | 11,546            | 2,392             | 27,488            |           |
|                     |                   |                   | Nine Months Ended |           |
|                     |                   |                   | December 31,      |           |
|                     |                   |                   | 2009              | 2008      |
| Transactions:       |                   |                   |                   |           |
| Purchases           | \$69,294          | \$51,703          | \$99,003          | \$119,505 |

The Company's operating subsidiaries have entered into transactions with affiliates of the Company for the purpose of procuring inventory.

The Company's balances due to and from related parties are primarily with its deconsolidated Zimbabwe subsidiary. The remaining related party balances and transactions relate to the Company's equity basis investments in companies located in Asia which purchase and process tobacco.





Alliance One International, Inc. and Subsidiaries

Item 2. Management's Discussion and Analysis of  
Financial Condition and Results of Operations

**EXECUTIVE OVERVIEW**

The following executive overview is intended to provide significant highlights of the discussion and analysis that follows.

**Financial Results**

Volumes and sales were in line with our expectations. Year to date operating margin remained strong despite some third quarter slippage as our global operations having done a good job of controlling costs. Looking forward, our order book is solid. Additionally, the global debt markets have improved further which should help short term borrowing costs for the remainder of this year and next; however, U.S. dollar volatility versus many currencies that impact our costs remains challenging.

**Liquidity**

Liquidity requirements for our business are impacted by crop seasonality, foreign currency and interest rates, green tobacco prices, crop quality and throw and other factors. We continuously monitor and adjust funding sources as required based on business dynamics, utilizing cash from operations, our revolving credit facility, short term credit lines throughout the world, sales of accounts receivable, active working capital management and advances from customers. As of December 31, 2009, we had \$733.8 million of cash and available credit comprised of \$109.5 million of cash and \$624.3 million in available credit inclusive of \$270.0 million undrawn on our revolver, \$1.9 million of other long-term debt, \$343.4 million of notes payable to banks, and \$9.0 million exclusively for letters of credit. We continually modify the makeup of our available liquidity to enhance business flexibility and reduce costs.

**Outlook**

The operating environment will remain dynamic. Global production for the next crop cycle is currently stable, though recent flooding in Brazil and dryer weather in Malawi will impact those markets. Our debt refinancing during the second quarter has significantly extended long term debt maturities and reduced financing risk due to the onslaught of refinancing activities that we believe will be occurring in the high yield markets over the next four years, allowing management to focus on enhancing the business. As we look ahead, hopefully to a more stable global economy, we will begin to refocus on reducing our leverage again, while managing working capital and capital expenditures. Importantly, our customer centric strategy encompasses expense control, while investing for the future where appropriate returns exist, and is critical to continued plan execution and enhanced shareholder returns.



## Alliance One International, Inc. and Subsidiaries

**RESULTS OF OPERATIONS:****Condensed Consolidated Statements of Operations**

| <i>(in millions)</i>                            | Three Months Ended |           |        | Nine Months Ended |            |           |       |           |
|---|--------------------|-----------|--------|-------------------|------------|-----------|-------|-----------|
|   | December 31,       |           |        | December 31,      |            |           |       |           |
|   | Change             |           |        | Change            |            |           |       |           |
|   | 2009               | \$        | %      | 2008              | 2009       | \$        | %     | 2008      |
| Sales and other operating revenues              | \$658.4            | \$(31.6)  | (4.6)  | \$690.0           | \$ 1,744.0 | \$ (1.2)  | (0.1) | \$1,746.2 |
| Gross profit                                    | 98.1               | (21.4)    | (17.9) | 119.5             | 292.9      | 16.3      | 5.9   | 276.6     |
| Selling, administrative and general expenses    | 38.1               | 2.7       | 7.6    | 35.4              | 116.5      | 2.9       | 2.6   | 113.6     |
| Other income (expense)                          | 0.1                | 1.1       |        | (1.0)             | 2.8        | 2.3       |       | 0.5       |
| Restructuring and asset impairment charges      | -                  | -         |        | -                 | -          | (0.5)     |       | 0.5       |
| Debt retirement expense                         | -                  | -         |        | -                 | 40.4       | 39.4      |       | 1.0       |
| Interest expense                                | 29.5               | 5.5       |        | 24.0              | 87.2       | 12.4      |       | 74.8      |
| Interest income                                 | 1.0                | 0.1       |        | 0.9               | 3.1        | 0.6       |       | 2.5       |
| Income tax expense (benefit)                    | (14.9)             | (15.6)    |        | 0.7               | (5.2)      | (1.3)     |       | (3.9)     |
| Equity in net income of investee companies      | 1.3                | 0.9       |        | 0.4               | 1.3        | (0.2)     |       | 1.5       |
| Income (loss) from discontinued operations      | -                  | -         |        | -                 | -          | (0.4)     |       | 0.4       |
| Income attributable to noncontrolling interests | 0.5                | 0.4       |        | 0.1               | 1.0        | 0.6       |       | 0.4       |
| Net income attributable to the Company          | \$ 47.3            | \$(12.2)* |        | \$ 59.5*          | \$ 60.3*   | \$(34.8)* |       | \$ 95.1   |

\* Amounts do not equal column totals due to rounding.

**Sales and Other Operating Revenue Supplemental Information**

| <i>(in millions, except per kilo amounts)</i> | Three Months Ended |          |        | Nine Months Ended |           |        |       |           |
|---|--------------------|----------|--------|-------------------|-----------|--------|-------|-----------|
|   | December 31,       |          |        | December 31,      |           |        |       |           |
|   | Change             |          |        | Change            |           |        |       |           |
|   | 2009               | \$       | %      | 2008              | 2009      | \$     | %     | 2008      |
| Tobacco sales and other operating revenues:   |                    |          |        |                   |           |        |       |           |
| Sales and other operating revenues            | \$619.8            | \$(25.7) | (4.0)  | \$645.5           | \$1,692.3 | \$ 8.0 | 0.5   | \$1,684.3 |
| Kilos   | 125.1              | (18.6)   | (12.9) | 143.7             | 379.1     | (13.9) | (3.5) | 393.0     |

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|  |         |           |        |         |           |           |        |           |
|--|---------|-----------|--------|---------|-----------|-----------|--------|-----------|
| Average price per kilo                   | \$ 4.95 | \$ .46    | 10.2   | \$ 4.49 | \$ 4.46   | \$ .17    | 4.0    | \$ 4.29   |
| Processing and other revenues            | \$ 38.6 | \$ (5.9)  | (13.3) | \$ 44.5 | \$ 51.7   | \$ (10.2) | (16.5) | \$ 61.9   |
| Total sales and other operating revenues | \$658.4 | \$ (31.6) | (4.6)  | \$690.0 | \$1,744.0 | \$ (2.2)  | (0.1)  | \$1,746.2 |

**Three Months Ended December 31, 2009 Compared to Three Months Ended December 31, 2008**

*Sales and other operating revenues.* The decrease of 4.6% from \$690.0 million in 2008 to \$658.4 million in 2009 is primarily the result of a 12.9%, or 18.6 million kilos, decrease in quantities sold and a 13.3%, or \$5.9 million, decrease in processing and other revenues partially offset by a 10.2% or \$0.46 per kilo increase in overall average sales prices.

South America Region. Tobacco sales from the South American Region operating segment decreased \$12.8 million or 6.8% primarily as a result of a 9.7% decrease in higher priced lamina volumes compared to the prior year that was partially offset by increased sales prices for both lamina and by-products. The resulting increase in average sales prices per kilo was \$0.64. Decreases in by-product volumes as well resulted in a total decrease in volumes for the quarter of 8.7 million kilos. The lower lamina volumes for the quarter were the result of tighter tobacco availability.

**RESULTS OF OPERATIONS:** *(Continued)*

**Three Months Ended December 31, 2009 Compared to Three Months Ended December 31, 2008** *(Continued)*

Other Regions. Tobacco sales from the Other Regions operating segment decreased \$12.9 million or 2.8% primarily as a result of a decrease in volumes of 9.9 million kilos partially offset by an increase of \$0.37 per kilo in overall average sales prices. The decreased revenues primarily resulted from the timing of shipments in Europe. Compared to the prior year, expected shipments from Bulgaria and Macedonia are delayed into the next quarter while shipments from Turkey were accelerated into the prior quarter. The prior year also included older crop opportunistic sales from the region. Partially offsetting the impact of decreased volumes in Europe were increased average sales prices in Europe as a result of the strength of the euro compared to the prior year and product mix. Decreased revenues from Europe were mitigated by increased revenues from Asia as delayed shipments of higher priced lamina from Thailand occurred in the current quarter. Volumes and revenues were down in Africa as shipments from Malawi and Tanzania were delayed into next quarter. Decreased revenues from Africa were offset by increased revenues from North America primarily as a result of the change to direct contracting in Canada. Processing and other revenues decreased 13.3% or \$5.9 million primarily as a result of decreased processing volumes in Africa and Europe.

*Gross profit as a percentage of sales.* Gross profit decreased 17.9% from \$119.5 million in 2008 to \$98.1 million in 2009 and gross profit as a percentage of sales decreased from 17.3% in 2008 to 14.9% in 2009.

South America Region. Gross profit in the South America Region operating segment decreased \$19.4 million primarily as a result of decreased lamina volumes, losses on derivative financial instruments and significant exchange losses due to the volatility of the Brazilian real this quarter compared to the same quarter in the prior year.

Other Regions. The slight decrease in gross profit of \$2.0 million is primarily attributable to a market adjustment related to a shipment of Asian tobacco. Gross profit remained fairly constant across most areas after absorbing significant exchange losses due to the volatility of the various foreign currencies in which we buy and process tobacco compared to the same quarter in the prior year.

*Selling, administrative and general expenses* increased 7.6% from \$35.4 million in 2008 to \$38.1 million in 2009. The increase is primarily due to increased compensation costs as a result of currency fluctuations in the South America and Asia regions compared to the prior year and incremental stock-based compensation costs compared to the prior year.

*Interest expense* increased \$5.5 million from \$24.0 million in 2008 to \$29.58 million in 2009 primarily due to higher average borrowings, higher average interest rates on our seasonal borrowings and increased debt amortization expense compared to the prior year.

*Effective tax rates* were a benefit of 47.2% in 2009 and an expense of 1.2% in 2008. The effective tax rates for these periods are based on the current estimate of full year results after the effect of taxes related to specific events which are recorded in the interim period in which they occur. The significant variance in the effective tax rates between 2009 and 2008 is primarily related to foreign currency translation adjustments related to income taxes and the reversal of unrecognized tax benefit liabilities in 2009. During the three months ended December 31, 2009, we participated in various governmental tax programs in certain locations in an effort to resolve outstanding tax issues. By participating in these programs our liability for unrecognized tax benefits, including accrued interest and penalties, was reduced from \$72.6 million to \$23.3 million as compared to September 30, 2009. The decrease in the liability for unrecognized tax benefits relates to cash payments of approximately \$12.9 million, settlement of unrecognized tax benefits of approximately \$37.3 million, and an increase related to current period activity of approximately \$.9 million. As recognized in the income statement the settlement of unrecognized tax benefits is reduced by the write off of related deferred tax assets. We forecast the effective tax rate for the year ending March 31, 2010 will be an expense of 4.2% after absorption of discrete items.

Our effective tax rate can vary significantly between quarters and fiscal years as a result of foreign currency fluctuations. Foreign currencies such as the Brazilian real and the euro have been particularly volatile in the recent past. The resulting exchange gains or losses in income can fluctuate greatly which directly impact actual and forecasted effective tax rates. Exchange rate variances on the translation of foreign denominated tax account balances also directly impact actual and forecasted effective tax rates. Actual and forecasted effective tax rates for the remainder of 2009 will be updated as specific event adjustments and currency fluctuations occur.



Alliance One International, Inc. and Subsidiaries

**RESULTS OF OPERATIONS:** *(Continued)*

**Nine Months Ended December 31, 2009 Compared to Nine Months Ended December 31, 2008**

*Sales and other operating revenues.* The slight decrease from \$1,746.2 million in 2008 to \$1,744.0 million in 2009 is primarily the result of a 3.5%, or 13.9 million kilos, decrease in quantities sold and a 16.5%, or \$10.2 million, decrease in processing and other revenues partially offset by a 4.0% or \$0.17 per kilo increase in overall average sales prices.

South America Region. Tobacco sales from the South America Region operating segment decreased \$30.9 million or 4.0% primarily as a result of an 8.8% decrease in higher priced lamina volumes compared to the prior year due to the delay of some customer shipments to fiscal 2011 and tighter tobacco availability. Partially offsetting the impact of the lower lamina volumes were increased volumes of lower priced by-products and an increase of \$0.07 per kilo in overall average sales prices for the region. The overall change in volumes for the current year was a decrease of 9.0 million kilos.

Other Region. Tobacco sales from the Other Regions operating segment increased \$38.9 million or 4.3% primarily as a result of an increase of \$0.27 per kilo in overall average sales prices partially offset by a decrease in volumes of 4.9 million kilos. Average sales prices across all areas and revenues increased across all areas except Europe. Volume decreases were primarily in Europe but were partially offset by increased volumes in Asia. Significant sales of by-products at higher average sales prices this year contributed to increased revenues in Asia. Although lamina average sales prices in Asia were higher as well, the impact was offset by decreased lamina volumes due to less opportunistic sales in the current year. In Africa, volume increases in Malawi and Tanzania as a result of increased crop sizes were offset by shipments delayed into next quarter. However, improved customer pricing in Africa resulted in increased revenues for the region. In Europe, while average sales prices increased due to the strength of the euro and more sales of higher priced oriental tobacco compared to the prior year, volumes decreased primarily from expected shipments delayed into the next quarter and less older crop opportunistic sales in the current year which resulted in a slight decrease in revenues from Europe. Revenue increases in North America were primarily due to improved customer pricing in Guatemala and the change to direct contracting in Canada. Processing and other revenues decreased 16.5% or \$10.2 million primarily as a result of decreased processing volumes and prices in the Africa and Europe partially offset by increased processing volumes and prices in Asia.

*Gross profit as a percentage of sales.* Gross profit increased \$16.3 million or 5.9% from \$276.6 million in 2008 to \$292.9 million in 2009 and gross profit as a percentage of sales increased from 15.8% in 2008 to 16.8% in 2009.

South America Region. Gross profit in the South America Region operating segment increased \$7.5 million primarily as a result of higher average sales prices that mitigated increased prices of tobacco paid to farmers and the exchange rate impact on purchase and processing costs which are denominated in Brazilian real. Higher gains on derivative financial instruments were significantly offset by increased exchange losses this year compared to the prior year from the volatility of the Brazilian real.

Other Region. Gross profit increased \$8.8 million after absorbing exchange losses of \$14.8 million. The increased gross profit is primarily attributable to Africa from lower green costs of the larger current crop in Malawi and gains on derivative financial instruments. Although sales from Europe may be denominated in euros, global sales are predominately denominated in U.S. dollars while global operating costs are denominated in local currencies. The volatility of these currencies against the U.S. dollar significantly impacted operating results this year compared to the prior year.

*Selling, administrative and general expenses* increased \$2.9 million or 2.6% from \$113.6 million in 2008 to \$116.5 million in 2009. The increase is primarily due to incremental stock-based compensation costs and increased amortization of internally developed software due to our implementation of SAP. Partially offsetting these increased expenses are gains on forward currency contracts that hedge our costs for selling, administrative and general expenses denominated in foreign currencies. See Note 11 *Derivative Financial Instruments* to the *Notes to Condensed Consolidated Financial Statements* for further information.

*Other income (expense)* was \$2.8 million in 2009 compared to \$0.5 million in 2008. Gains from the sales of assets increased \$2.6 million primarily from the 2009 sale of a facility in Turkey. Partially offsetting these gains were increased losses on the sale of receivables of \$(0.3) million. Losses on sale of receivables under our revolving trade accounts receivable securitization agreement are recorded as a component of other income (expense). See Note 14 *Sale of Receivables* to the *Notes to Condensed Consolidated Financial Statements* for further information.

**RESULTS OF OPERATIONS:** *(Continued)*

**Nine Months Ended December 31, 2009 Compared to Nine Months Ended December 31, 2008** *(Continued)*

*Debt retirement expense* was \$40.4 million in 2009 compared to \$1.0 million in 2008. During the quarter ended September 30, 2009, we underwent a debt refinancing. As a result, significant one-time costs were incurred to retire our existing debt. These costs include premiums of \$22.9 million to purchase and redeem our senior notes and senior subordinated notes, fees and other related costs of \$0.6 million associated with the purchase and redemption of these notes and the non-cash accelerated recognition of \$16.9 million of debt issuance costs and original issue discounts related to the existing debt. The cost in 2008 relates to accelerated amortization of debt issuance costs as a result of debt prepayment.

*Interest expense* increased \$12.4 million from \$74.8 million in 2008 to \$87.2 million in 2009 primarily due to higher average interest rates on our seasonal borrowings compared to the prior year and increased debt amortization expense.

*Effective tax rates* were a benefit of 9.5% in 2009 and 4.4% in 2008. The effective tax rates for these periods are based on the current estimate of full year results after the effect of taxes related to specific events which are recorded in the interim period in which they occur. The significant variance in the effective tax rates between 2009 and 2008 is primarily related to foreign currency translation adjustments related to income taxes and the reversal of the unrecognized tax benefit liabilities in 2009. During the three months ended December 31, 2009, we pursued various governmental tax programs in certain locations in an effort to resolve outstanding tax issues. By participating in these programs our liability for unrecognized tax benefits, including accrued interest and penalties, was reduced from \$72.6 million to \$23.3 million as compared to September 30, 2009. The decrease in the liability for unrecognized tax benefits relates to cash payments of approximately \$12.9 million, settlement of unrecognized tax benefits of approximately \$37.3 million, and an increase related to current period activity of approximately \$.9 million. As recognized in the income statement the settlement of unrecognized tax benefits is reduced by the write off of related deferred tax assets. We forecast the effective tax rate for the year ending March 31, 2010 will be an expense of 4.2% after absorption of discrete items.

Our effective tax rate can vary significantly between quarters and fiscal years as a result of foreign currency fluctuations. Foreign currencies such as the Brazilian real and the euro have been particularly volatile in the recent past. The resulting exchange gains or losses in income can fluctuate greatly which directly impact actual and forecasted effective tax rates. Exchange rate variances on the translation of foreign denominated tax account balances also directly impact actual and forecasted effective tax rates. Actual and forecasted effective tax rates for the remainder of 2009 will be updated as specific event adjustments and currency fluctuations occur.

**LIQUIDITY AND CAPITAL RESOURCES:**

### **Overview**

We utilize capital in excess of cash flow from operations to finance accounts receivable, inventory and advances to farmers for pre-financing tobacco crops in foreign countries, including Argentina, Brazil, Guatemala, Malawi, Tanzania, Turkey and Zambia. Additionally, our business is seasonal, and purchasing, processing and selling activities have several associated peaks where cash on hand and outstanding indebtedness may be significantly greater or less than at fiscal year-end. As of December 31, 2009, we are in the process of repaying our South American related crop lines as we continue to ship inventory and collect receivables. In Africa, we continue to ship product which should continue into the first quarter of fiscal year 2011 as well as the purchase of the new crop which should begin mid-March. In Asia, the Indian Mysore and Indonesian crops are approaching the end of the processing and shipping is in full force. Europe continues shipping of the current crop and is preparing to purchase the new crop during the fourth fiscal quarter. North America has completed flue cured processing with shipping winding down and has commenced the purchasing, processing and shipping of the burley crop which should continue into the fourth fiscal quarter, seasonally elevating its working capital requirements. At the same time currency markets remain volatile, which creates challenges in protecting our non-U.S. dollar costs and can impact our working capital requirements. As such we monitor and hedge foreign currency costs. Looking forward, we may purchase, redeem, repay, retire or cancel indebtedness prior to stated maturity under our various foreign credit lines, senior secured credit agreement or indentures as permitted.

### **Working Capital**

Our working capital increased from \$620.9 million at March 31, 2009 to \$787.2 million at December 31, 2009. Our current ratio was 2.4 to 1 at December 31, 2009 compared to 2.0 to 1 at March 31, 2009. The increase in working capital is primarily related to increases in trade receivables and decreases in accounts payable. These changes are attributable to the purchasing and processing of tobacco in the United States and Malawi as well as the financing of crops in South America and Europe.

The following table is a summary of items from the Condensed Consolidated Balance Sheet and Condensed Consolidated Statements of Cash Flows.

Alliance One International, Inc. and Subsidiaries

**LIQUIDITY AND CAPITAL RESOURCES:** *(Continued)***Working Capital** *(Continued)*

| <i>(in millions except for current ratio)</i>               | December 31,<br>2009 | As of<br>2008 | March 31,<br>2009 |
|---|----------------------|---------------|-------------------|
| Cash and cash equivalents                                   | \$ 109.5             | \$ 74.6       | \$ 87.7           |
| Net trade receivables                                       | 256.3                | 238.8         | 175.7             |
| Inventories and advances on purchases<br>of tobacco         | 837.9                | 839.2         | 825.0             |
| Total current assets  | 1,346.8              | 1,313.9       | 1,232.3           |
| Notes payable to banks                                      | 286.4                | 488.8         | 261.5             |
| Accounts payable  | 50.8                 | 76.7          | 120.2             |
| Advances from customers                                     | 61.8                 | 78.2          | 44.4              |
| Total current liabilities                                   | 559.6                | 813.5         | 611.4             |
| Current ratio   | 2.4 to 1             | 1.6 to 1      | 2.0 to 1          |
| Working capital   | 787.2                | 500.4         | 620.9             |
| Total long-term debt  | 806.2                | 530.7         | 652.6             |
| Stockholders' equity of Alliance One<br>International, Inc. | 384.9                | 300.2         | 326.7             |
| Net cash provided (used) by:                                |                      |               |                   |
| Operating activities  | (32.2)               | (90.0)        |                   |
| Investing activities  | (12.9)               | (29.2)        |                   |
| Financing activities  | 66.8                 | 91.7          |                   |

**Operating Cash Flows**

Net cash used by operating activities decreased \$57.8 million in 2009 compared to 2008. The decrease in cash used was primarily due to a \$30.7 million increase in cash from advances from customers, a \$21.2 million decrease in cash used for payables, accrued expenses and other current liabilities, and \$8.0 million more cash received from accounts receivable.

**Investing Cash Flows**

Net cash used by investing activities decreased \$16.3 million in 2009 compared to 2008. The decrease in cash used is primarily attributable to foreign currency derivatives and less cash used for intangibles, primarily our SAP

implementation last year.

### **Financing Cash Flows**

Net cash provided by financing activities decreased \$24.9 million in 2009 compared to 2008. This decrease is primarily due to a \$168.5 million decrease in the net change in short-term borrowings and \$81.2 million in debt issuance, debt retirement and other debt related costs primarily associated with our refinancing transactions last quarter. Partially offsetting this decrease is a \$170.5 million increase in the net change in long-term borrowings primarily relating to our debt refinancing and a \$55.1 million decrease in net repayments of short-term demand notes.

### **Debt Financing**

We continue to finance our business with a combination of cash from operations, short-term seasonal credit lines, our revolving credit facility, long-term debt securities, customer advances and cash from operations. At December 31, 2009 we had cash of \$109.5 million and total debt outstanding of \$1,112.0 million comprised of \$286.4 million of notes payable to banks, no revolver borrowings, \$39.5 million of other long-term debt, \$641.5 million of 10% senior notes, \$29.6 million of 8.5% senior notes and \$115.0 million of 5 ½% convertible senior subordinated notes. The \$25.0 million seasonal increase in notes payable to banks from March 31, 2009 to December 31, 2009 results from anticipated seasonal fluctuation to account for the current purchase and processing of African, Brazilian, Indian and U.S. tobaccos. The \$202.4 million seasonal decrease in notes payable to banks from December 31, 2008 to December 31, 2009 is driven by the refinancing we completed during the quarter ended September 30, 2009. Available credit as of December 31, 2009 was \$624.3 million comprised of \$270.0 million under our revolver, \$1.9 million of other long-term debt, \$343.4 million of notes payable to banks and \$9.0 million of availability exclusively for letters of credit. We expect to incur \$47.0 million of capital expenditures during fiscal year 2010. Maintenance expenditures are anticipated to be between \$19.0 and \$28.0, while our continuing SAP software implementation and new Brazilian factory are major expenditures in addition to regularly scheduled maintenance. We may also decide to deploy additional discretionary amounts to enhance future business prospects, but only if stringent management return thresholds are likely to be achieved. No cash dividends were paid to stockholders during the quarter ended December 31, 2009. We believe that these sources of liquidity versus our requirements will be sufficient to fund our anticipated needs for the remainder of fiscal year 2010.

## Alliance One International, Inc. and Subsidiaries

**LIQUIDITY AND CAPITAL RESOURCES:** *(Continued)***Debt Financing** *(Continued)*

The following table summarizes our debt financing as of December 31, 2009:

| <i>(in millions except for interest rates)</i>      | Outstanding    |                   | December 31, 2009           |               |     |
|---|----------------|-------------------|-----------------------------|---------------|-----|
|   | March 31, 2009 | December 31, 2009 | Lines and Letters Available | Interest Rate |     |
| Senior secured credit facility:                     |                |                   |                             |               |     |
| Revolver  | \$ 120.0       | \$ -              | \$270.0                     |               |     |
| Senior notes:                                       |                |                   |                             |               |     |
| 10% senior notes due 2016                           | -              | 641.5             | -                           | 10.0%         |     |
| 11% senior notes due 2012                           | 264.4          | -                 | -                           | 11.0%         |     |
| 8 ½% senior notes due 2012                          | 149.5          | 29.6              | -                           | 8.5%          |     |
| Other (1)   | 10.2           | -                 | -                           |               |     |
|   | 424.1          | 671.1             | -                           |               |     |
| 5 ½% convertible senior subordinated notes due 2014 | -              | 115.0             | -                           | 5.5%          |     |
| 12 ¾% senior subordinated notes due 2012            | 84.0           | -                 | -                           | 12.8%         |     |
| Other long-term debt                                | 42.3           | 39.5              | 1.9                         | 9.1%          | (2) |
| Notes payable to banks (3)                          | 261.5          | 286.4             | 343.4                       | 6.2%          | (2) |
| Total debt  | \$ 931.9       | \$ 1,112.0        | 615.3                       |               |     |
| Short term  | \$ 261.5       | \$ 286.4          |                             |               |     |
| Long term:  |                |                   |                             |               |     |
| Long term debt current                              | \$ 17.8        | \$ 19.3           |                             |               |     |
| Long term debt                                      | 652.6          | 806.3             |                             |               |     |
|   | \$ 670.4       | \$ 825.6          |                             |               |     |

|                        |    |     |    |      |         |
|------------------------|----|-----|----|------|---------|
| Letters of credit      | \$ | 3.8 | \$ | 11.2 | 9.0     |
| Total credit available |    |     |    |      | \$624.3 |

(1) Notes redeemed in total as of December 4, 2009

(2) Weighted average rate for the nine months ended December 31, 2009

(3) Primarily foreign seasonal lines of credit

Prior to the debt refinancing, the discount amortization and repayment of the senior notes and the senior subordinated notes by fiscal year was \$(1.6) million in 2011, \$1.6 million in 2012, \$509.0 million in 2013 and \$.4 million in 2014. After the debt refinancing, the discount amortization and repayment of the senior notes and convertible senior subordinated notes by fiscal year is \$(3.3) million in 2011, \$(3.7) million in 2012, \$27.6 million in 2013, \$(4.5) million in 2014 and \$772.8 million in later fiscal years.



Alliance One International, Inc. and Subsidiaries

**LIQUIDITY AND CAPITAL RESOURCES:** *(Continued)*

We completed a number of refinancing transactions, which are described below.

**Senior Secured Credit Facility**

On July 2, 2009, Company entered into a Credit Agreement (the *Credit Agreement*), with a syndicate of banks that replaced the Company's \$305.0 million Amended and Restated Credit Agreement dated March 30, 2007 and provides for a senior secured credit facility (the *Credit Facility*) that consists of:

.  
a three and one-quarter year \$270.0 million revolver (the *Revolver*) which initially accrues interest at a rate of LIBOR plus 2.50%.

The interest rate for the *Revolver* may increase or decrease according to a consolidated interest coverage ratio pricing matrix as defined in the *Credit Agreement*. The *Credit Agreement* permits the Company to add \$55.0 million in commitments from existing or additional lenders which would increase the amount of the *Revolver* to \$325.0 million.

*First Amendment.* On August 24, 2009, the Company closed the First Amendment to the *Credit Agreement* which included the following modifications effective August 24, 2009:

.  
Amended the definition for Senior Notes to allow for the issuance of up to an additional \$100.0 million of Senior Notes due 2016 within 90 days of the First Amendment Effective Date;

.  
Amended the definition of Consolidated Total Senior Debt to exclude the Existing Senior Notes 2005;

Amended the definition of Applicable Percentage to clarify the effective date of the change in the Applicable Percentage;

Modifications to several schedules within the Credit Agreement.

*Borrowers and Guarantors.* One of the Company's primary foreign holding companies, Intabex Netherlands B.V. (Intabex), is co-borrower under the Revolver, and the Company's portion of the borrowings under the Revolver is limited to \$200.0 million outstanding at any one time. One of the Company's primary foreign trading companies, Alliance One International AG (AOIAG), is a guarantor of Intabex's obligations under the Credit Agreement. Such obligations are also guaranteed by the Company and must be guaranteed by any of its material direct or indirect domestic subsidiaries.

*Collateral.* The Company's borrowings under the Credit Facility are secured by a first priority pledge of:

100% of the capital stock of any domestic subsidiary held directly by the Company or by any material domestic subsidiary;

100% of the capital stock of any material domestic subsidiary;

100% of the capital stock of any material foreign subsidiary held directly by the Company or any domestic subsidiary; provided that not more than 65% of the voting stock of any material foreign subsidiary is required to be pledged to secure obligations of the Company or any domestic subsidiary;

U.S. accounts receivable and U.S. inventory owned by the Company or its material domestic subsidiaries (other than inventory the title of which has passed to a customer and inventory financed through customer advances and certain other exceptions); and

Intercompany notes evidencing loans or advances the Company makes to subsidiaries.

In addition, Intabex's borrowings under the Credit Facility are secured by a pledge of 100% of the capital stock of Intabex, AOIAG, certain of the Company's and Intabex's material and other foreign subsidiaries and the collateral

described above for the Company's borrowings.

*Financial Covenants.* The Credit Facility includes certain financial covenants and required financial ratios, including:

.

a minimum consolidated interest coverage ratio of not less than 1.90 to 1.00;

.

a maximum consolidated leverage ratio in an amount not more than a ratio specified for each fiscal quarter, which ratio is 5.75 to 1.00 for the fiscal quarter ended December 31, 2009;

.

a maximum consolidated total senior debt to working capital amount ratio of not more than 0.80 to 1.00; and

.

a maximum amount of annual capital expenditures of \$75.0 million during fiscal year ending March 31, 2010 and \$40.0 million during any fiscal year thereafter, with a one-year carry-forward for capital expenditures in any fiscal year below the maximum amount.

Alliance One International, Inc. and Subsidiaries

## **LIQUIDITY AND CAPITAL RESOURCES:** *(Continued)*

### **Senior Secured Credit Facility** *(Continued)*

Certain of these financial covenants and required financial ratios adjust over time in accordance with schedules in the Credit Agreement.

The Credit Agreement also contains certain customary affirmative and negative covenants, including, without limitation, restrictions on additional indebtedness, guarantees, liens and asset sales.

The Company continuously monitors its compliance with these covenants. If the Company fails to comply with any of these covenants and is unable to obtain the necessary amendments or waivers under the Credit Agreement, the lenders under the Credit Agreement have the right to accelerate the outstanding loans thereunder and demand repayment in full and to terminate their commitment to make any further loans under the Credit Facility. Certain defaults under the Credit Facility would result in a cross default under the indentures governing the Company's senior notes and convertible senior subordinated notes and could impair access to its seasonal operating lines of credit in local jurisdictions. A default under the Credit Agreement would have a material adverse effect on the Company's liquidity and financial condition. The Company records all fees and third-party costs associated with the Credit Agreement, including amendments thereto, in accordance with accounting guidance for changes in line of credit or revolving debt arrangements.

As a result of terminating the \$305.0 million Amended and Restated Credit Agreement dated March 30, 2007, the Company accelerated approximately \$5.7 million of deferred financing costs.

### **Senior Notes**

On July 2, 2009, the Company issued \$570.0 million of 10% Senior Notes due 2016 (the "Senior Notes"). The Senior Notes were priced at 95.177% of the face value, for gross proceeds of approximately \$542.5 million and representing a yield to maturity of 11.0%. On August 26, 2009, the Company issued an additional \$100.0 million tranche of 10% Senior Notes due 2016. The notes were priced at 97.500% of the face value, for gross proceeds of approximately \$97.5 million and representing a yield to maturity of 10.512%. These additional notes form part of the same series as the Senior Notes issued on July 2, 2009. The aggregate principal amount of the outstanding Senior Notes is \$670.0 million. The Senior Notes are required to be guaranteed by any material domestic subsidiaries of the Company as defined in the indenture governing the Senior Notes. Because no subsidiary is, or has been at any relevant time, a material domestic subsidiary, the Senior Notes are not guaranteed by any subsidiaries of the Company, though such a guarantee would be required if any subsidiary subsequently qualifies as a material domestic subsidiary. The indenture governing the Senior Notes contains covenants that, among other things, limit the Company's ability to incur additional indebtedness; issue preferred stock; merge, consolidate or dispose of substantially all of its assets; grant liens on its assets; pay dividends, redeem stock or make other distributions or restricted payments; repurchase or redeem capital stock or prepay subordinated debt; make certain investments; agree to restrictions on the payment of dividends to the Company by its subsidiaries; sell or otherwise dispose of assets, including equity interests of its

subsidiaries; enter into transactions with its affiliates; and enter into certain sale and leaseback transactions. If a change of control (as defined in the indenture governing the Senior Notes) occurs at any time, holders of the Senior Notes will have the right, at their option, to require the Company to repurchase all or a portion of the Senior Notes for cash at a price equal to 101% of the principal amount of Senior Notes being repurchased, plus accrued and unpaid interest.

### **Convertible Senior Subordinated Notes**

On July 2, 2009, we issued \$100.0 million of 5 ½% Convertible Senior Subordinated Notes due 2014 (the Convertible Notes ). We granted the initial purchasers of the Convertible Notes an option to purchase up to an additional \$15.0 million of Convertible Notes solely to cover over-allotments. The initial purchasers exercised the option and purchased an additional \$15.0 million of the Convertible Notes on July, 15, 2009. Holders may surrender their Convertible Notes, in integral multiples of \$1,000 principal amount, for conversion into shares of the Company's common stock at the then-applicable conversion rate until the close of business on the second scheduled trading day immediately preceding the maturity date. The initial conversion rate for the Convertible Notes is 198.8862 shares of common stock per \$1,000 principal amount of Convertible Notes. The conversion rate is subject to adjustments based on certain events as described in the indenture governing the Convertible Notes. In addition, upon the occurrence of certain fundamental changes (as defined in the indenture governing the Convertible Notes), a holder that converts its notes in connection with such a fundamental change may be entitled to receive a make-whole premium in the form of an increase in the conversion rate. In addition, if such a fundamental change occurs at any time, holders of the Convertible Notes will have the right, at their option, to require the Company to repurchase all or a portion of the Convertible Notes for cash at a price equal to 100% of the principal amount of the Convertible Notes to be repurchased plus accrued and unpaid interest.

Alliance One International, Inc. and Subsidiaries

**LIQUIDITY AND CAPITAL RESOURCES:** *(Continued)***Convertible Note Hedge and Warrant Transactions**

In connection with the offering of the Convertible Notes, the Company entered into privately negotiated convertible note hedge transactions (the convertible note hedge transactions) with three counterparties, one initial purchaser of the Convertible Notes and affiliates of two other initial purchasers (the hedge counterparties). The convertible note hedge transactions cover, subject to customary anti-dilution adjustments, the number of shares of our common stock that initially underlie the Convertible Notes. The Company also entered separately into privately negotiated warrant transactions (the warrant transactions) relating to the same number of shares of our common stock with the hedge counterparties. The convertible note hedge transactions are expected to reduce the potential dilution with respect to the common stock of the Company upon conversion of the Convertible Notes in the event that the value per share of common stock, as measured under the convertible note hedge transactions, during the applicable valuation period, is greater than the strike price of the convertible note hedge transactions, which corresponds to the \$5.0280 per share initial conversion price of the Convertible Notes and is similarly subject to customary anti-dilution adjustments. If, however, the price per share of the Company's common stock, as measured under the warrants, exceeds the strike price of the warrant transactions during the applicable valuation period, there would be dilution from the issuance of common stock pursuant to the warrants. The warrants have a strike price of \$7.3325 per share, which is subject to customary anti-dilution adjustments. The warrants expire in daily installments commencing on October 15, 2014 and ending on April 8, 2015.

**Tender of Existing Notes**

On July 2, 2009, the Company applied a portion of the net proceeds from the issuance of the Senior Notes and Convertible Notes to fund the purchase \$467.5 million aggregate principal amount of its existing notes pursuant to an early settlement of a cash tender offer (the "Tender Offer") for any and all of its 11% Senior Notes due 2012, 8 ½% Senior Notes due 2012, 12 ¾% Senior Subordinated Notes due 2012, 9 % Senior Notes due 2011, 7 ¾% Senior Notes due 2013 and 8% Senior Notes due 2012, Series B (collectively, the Existing Notes). On July 9, 2009, the Company applied a portion of the remaining net proceeds to fund the purchase of an additional \$1.1 million aggregate principal amount of Existing Notes in connection with the final settlement of the Tender Offer. The following table sets forth the principal amount of the Existing Notes outstanding at the commencement of the Tender Offer and the principal amount of the Existing Notes that we purchased:

| Existing Notes                | Issuer (1) | Principal Amount Outstanding | Principal Amount Purchased |
|-------------------------------|------------|------------------------------|----------------------------|
| 11% Senior Notes due 2012 (2) | A          | \$264.4                      | \$ 258.1                   |
| 8 ½% Senior Notes due 2012    | A          | \$150.0                      | \$ 120.4                   |
|                               | A          | \$ 89.5                      | \$ 82.1                    |

12 <sup>3</sup>/<sub>4</sub>% Senior Subordinated Notes due  
2012 (2)

|   |   |        |        |
|---|---|--------|--------|
| 9 % Senior Notes due 2011 (3)                             | D | \$ 3.4 | \$ 3.4 |
| 7 <sup>3</sup> / <sub>4</sub> % Senior Notes due 2013 (3) | D | \$ 0.4 | \$ 0.4 |
| 8% Senior Notes due 2012, Series B (3)                    | S | \$ 6.3 | \$ 4.3 |

(1) The issuer of a series of Existing Notes designated with an A is Alliance One International, Inc. In 2005, Standard Commercial Corporation ( Standard Commercial ) merged with and into DIMON Incorporated ( DIMON ), which changed its name to Alliance One International, Inc. The issuer of a series of Existing Notes designated with a D was originally DIMON and the issuer of a series of Existing Notes designated with an S was originally Standard Commercial.

(2) On July 31, 2009 funds were paid to the Trustee to defease the remaining outstanding principal and interest. The Notes were redeemed in full on August 3, 2009.

(3) On December 4, 2009 funds were paid to redeem in full the remaining outstanding principal and interest as well as the applicable redemption premium.

As a result of the repurchase, defeasance and redemption of the Existing Notes as described in the foregoing table, the Company accelerated approximately \$5.6 million of deferred financing costs and \$5.6 million of amortization of original issue discount.

### Amendment of Certain Existing Notes

On July 2, 2009, in connection with the early settlement of the Tender Offer with respect to the Company's 11% Senior Notes due 2012, 8 <sup>1</sup>/<sub>2</sub>% Senior Notes due 2012 and 12 <sup>3</sup>/<sub>4</sub>% Senior Subordinated Notes due 2012 (the Alliance One Notes ), certain amendments to the indentures governing the Alliance One Notes became operative and effective. These amendments eliminated substantially all of the restrictive covenants, eliminated requirements for subsidiary guarantees and requirements to conduct repurchase offers following certain events, including a change in control, modified redemption notice periods from 30 days to three business days, eliminated or modified certain events of default and certain conditions to defeasance of the Alliance One Notes, and eliminated or modified related provisions contained in the indentures governing the Alliance One Notes.

Alliance One International, Inc. and Subsidiaries

**LIQUIDITY AND CAPITAL RESOURCES:** *(Continued)*

**Foreign Seasonal Lines of Credit**

The Company has typically financed its non-U.S. operations with uncommitted unsecured short-term seasonal lines of credit at the local level. These operating lines are seasonal in nature, normally extending for a term of 180 to 270 days corresponding to the tobacco crop cycle in that location. These facilities are typically uncommitted in that the lenders have the right to cease making loans and demand repayment of loans at any time. These loans are typically renewed at the outset of each tobacco season. As of December 31, 2009, the Company had approximately \$286.4 million drawn and outstanding on foreign seasonal lines with maximum capacity totaling \$650.0 million subject to limitations as provided for in the Credit Agreement. Additionally against these lines there was \$20.2 million available in unused letter of credit capacity with \$11.2 million issued but unfunded.

**RECENT ACCOUNTING PRONOUNCEMENTS NOT YET ADOPTED:**

In December 2008, the FASB issued new accounting guidance on employers' disclosures about postretirement benefit plan assets. This accounting guidance relates to employers' disclosures about plan assets of a defined benefit pension or other postretirement plan. The disclosures about plan assets required by this accounting guidance are required for us in our fiscal year ending March 31, 2010. We are evaluating the impact of this new accounting guidance on our financial condition and results of operations.

In June 2009, the FASB issued new accounting guidance on accounting for transfers of financial assets. The objective of this accounting guidance is to improve the relevance, representational faithfulness, and comparability of the information that a reporting entity provides in its financial reports about a transfer of financial assets; the effects of a transfer on its financial position, financial performance, and cash flows; and a transferor's continuing involvement in transferred financial assets. This accounting guidance will be effective for us on April 1, 2010. We are evaluating the impact of this new accounting guidance on our financial condition and results of operations.

In June 2009, the FASB issued new accounting guidance on accounting for variable interest entities. The objective of this accounting guidance is to improve financial reporting by enterprises involved with variable interest entities and to provide more relevant and reliable information to users of financial statements. This accounting guidance will be effective for us on April 1, 2010. We are evaluating the impact of this new accounting guidance on our financial condition and results of operations.

In October 2009, the FASB issued new accounting guidance on accounting for multiple-deliverable revenue arrangements. The objective of this accounting guidance is to address the accounting for multiple-deliverable arrangements to enable vendors to account for products or services (deliverables) separately rather than as a combined unit. This accounting guidance will be effective for us on April 1, 2011. We are evaluating the impact of this new accounting guidance on our financial condition and results of operations.



In January 2010, the FASB issued new accounting guidance on fair value measurements and disclosures. This guidance will require reporting entities to disclose separately the amounts of significant transfers in and out of Level 1 and Level 2 fair value measurements and describe the reasons for the transfers. It will also require reporting entities to present separately information about purchases, sales, issuances, and settlements in their Level 3 fair value reconciliations. The new disclosures and clarifications of existing disclosures (the Level 1 and Level 2 changes) will be effective for us on January 1, 2010. The disclosures about purchases, sales, issuances, and settlements in the roll forward of activity in Level 3 fair value measurements will be effective for us on April 1, 2011. We do not expect these new disclosure requirements to have a material impact on our financial condition or results of operations.

#### **FACTORS THAT MAY AFFECT FUTURE RESULTS:**

Readers are cautioned that the statements contained herein regarding expectations for our performance are forward-looking statements as defined in the Private Securities Litigation Reform Act of 1995. These statements are based on current expectations of future events. If underlying assumptions prove inaccurate or unknown risks or uncertainties materialize, actual results could vary materially from our expectations and projections. Risks and uncertainties include changes in the timing of anticipated shipments, changes in anticipated geographic product sourcing, political instability in sourcing locations, currency and interest rate fluctuations, shifts in the global supply and demand position for our tobacco products, and the impact of regulation and litigation on our customers. A further list and description of these risks, uncertainties and other factors can be found in our Annual Report on Form 10-K for the fiscal year ended March 31, 2009, our Quarterly Report on Form 10-Q for the periods ended June 30, 2009 and September 30, 2009 and other filings with the Securities and Exchange Commission. We assume no obligation to update any forward-looking statements as a result of new information or future events or developments, except as required by law.

Alliance One International, Inc. and Subsidiaries

#### **Item 3. Quantitative and Qualitative Disclosures About Market Risk.**

*Derivatives policies:* Hedging interest rate exposure using swaps and hedging foreign exchange exposure using forward contracts are specifically contemplated to manage risk in keeping with management's policies. We may use derivative instruments, such as swaps or forwards, which are based directly or indirectly upon interest rates and currencies to manage and reduce the risks inherent in interest rate and currency fluctuations.

We do not utilize derivatives for speculative purposes, and we do not enter into market risk sensitive instruments for trading purposes. Derivatives are transaction specific so that a specific debt instrument, contract, or invoice determines the amount, maturity, and other specifics of the hedge.

*Foreign exchange rates:* Our business is generally conducted in U.S. dollars, as is the business of the tobacco industry as a whole. However, local country operating costs, including the purchasing and processing costs for tobaccos, are subject to the effects of exchange fluctuations of the local currency against the U.S. dollar. We attempt to minimize such currency risks by matching the timing of our working capital borrowing needs against the tobacco purchasing and processing funds requirements in the currency of the country where the tobacco is grown. Also, in some cases, our sales pricing arrangements with our customers allow adjustments for the effect of currency exchange fluctuations on local purchasing and processing costs. Fluctuations in the value of foreign currencies can significantly affect our operating results. We have recognized exchange gains in our cost of goods and services sold of \$1.6 million and \$9.0 million for the three months ended December 31, 2009 and 2008, respectively. For the nine months ended December 31, 2009 and 2008, we have recognized exchange gains (losses) of \$(16.6) million and \$12.0 million, respectively, in our cost of goods and services sold. We have recognized exchange gains (losses) related to tax balances in our tax expense (benefit) of \$19.3 million and \$(8.8) million for the three months ended December 31, 2009 and 2008, respectively, and \$20.4 million and \$(11.5) million for the nine months ended December 31, 2009 and 2008, respectively.

Our consolidated selling, administrative and general expenses denominated in foreign currencies are subject to translation risks from currency exchange fluctuations. These foreign denominated expenses are primarily denominated in the euro, sterling and Brazilian real.

*Interest rates:* We manage our exposure to interest rate risk through the proportion of fixed rate and variable rate debt in our total debt portfolio. A 1% change in interest rates would have increased or decreased our reported interest cost by approximately \$3.0 million and \$8.9 million for the three months and nine months ended December 31, 2009. A substantial portion of our borrowings are denominated in U.S. dollars and bear interest at commonly quoted rates.

#### **Item 4. Controls and Procedures**

##### **Evaluation of Disclosure Controls and Procedures**

We maintain disclosure controls and procedures (as defined in Rule 13a-15(e) of the Securities Exchange Act of 1934, as amended (the Exchange Act)) designed to provide reasonable assurance that the information required to be disclosed in the reports we file or submit under the Exchange Act is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms and that this information is accumulated and communicated to our management, including our Chief Executive Officer and Chief Financial Officer, as appropriate, to allow for timely decisions regarding required disclosure. It should be noted that, because of inherent limitations, our disclosure controls and procedures, however well designed and operated, can provide only reasonable, and not absolute, assurance that the objectives of the disclosure controls and procedures are met.

In connection with the preparation of this Quarterly Report on Form 10-Q, our management, with the participation of our Chief Executive Officer and Chief Financial Officer, evaluated the effectiveness of the design and operation of our disclosure controls and procedures (as required by Rule 13a-15(b) of the Exchange Act), as of December 31, 2009. Based on this evaluation, our Chief Executive Officer and Chief Financial Officer concluded our disclosure controls and procedures (as defined in Rule 13a-15(e) of the Exchange Act) were effective to provide reasonable assurance as of December 31, 2009.

### **Changes in Internal Control Over Financial Reporting**

As required by Rule 13a-15(d) under the Exchange Act, the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, have evaluated the Company's internal control over financial reporting to determine whether any changes occurred during the quarter covered by this quarterly report that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Alliance One International, Inc. and Subsidiaries

#### **Item 4. Controls and Procedures** *(Continued)*

##### **Changes in Internal Control Over Financial Reporting** *(Continued)*

The Company is currently implementing an ERP system using SAP applications. The implementation is part of a multi-year plan to install SAP at certain operations throughout the world to improve the Company's business processes and deliver enhanced operational and financial performance. During the three months ended December 31, 2009, further developments to the financial reporting process were implemented for the United Kingdom, U.S., and Brazil operations and the Company substantially completed the process of implementing SAP in two of its African operations. This phase of the project has involved changes to certain internal controls over financial reporting, which the Company believes were material.

Other than the financial reporting developments for the Company's United Kingdom, U.S., and Brazil operations and implementation of SAP in two of the African operations discussed above there were no changes that occurred during the three months ended December 31, 2009 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.



## Part II. Other Information

### Item 1. Legal Proceedings

In October 2001, the Directorate General for Competition ( DGCOMP ) of the European Commission ( EC ) began an administrative investigation into certain tobacco buying and selling practices alleged to have occurred within the leaf tobacco industry in some countries within the European Union, including Spain, Italy, Greece and potentially other countries. The Company and its subsidiaries in Spain, Italy and Greece have been subject to these investigations. In respect of the investigation into practices in Spain, in 2004, the EC fined the Company and its Spanish subsidiaries €4.4 million (US\$5.6 million). In respect of the investigation into practices in Italy, in October 2005, the EC announced that the Company and its Italian subsidiaries have been assessed a fine in the aggregate amount of €24.0 million (US\$28.8 million). With respect to both the Spanish and Italian investigations, the fines imposed on the Company and its predecessors and subsidiaries were part of fines assessed on several participants in the applicable industry. With respect to the investigation relating to Greece, the EC informed the Company in March 2005 it had closed its investigation in relation to the Greek leaf tobacco industry buying and selling practices. The Company, along with its applicable subsidiaries, has appealed the decisions of the EC with respect to Spain and Italy to the Court of First Instance of the European Commission for the annulment or modification of the decision, but the outcome of the appeals process as to both timing and results is uncertain. The Company has fully recognized the impact of each of the fines set forth above and has paid all of such fines as part of the appeal process.

In March 2004, the Company discovered potential irregularities with respect to certain bank accounts in southern Europe and central Asia. The Audit Committee of the Company's Board of Directors engaged an outside law firm to conduct an investigation of activity relating to these accounts. That investigation revealed that, although the amounts involved were not material and had no material impact on the Company's historical financial statements, there were payments from these accounts that may have violated the U.S. Foreign Corrupt Practices Act. In May 2004, the Company voluntarily reported the matter to the U.S. Department of Justice ( Justice ). Soon thereafter, the Company closed the accounts in question, implemented personnel changes and other measures designed to prevent similar situations in the future, including the addition of new finance and internal audit staff and enhancement of existing training programs, and disclosed these circumstances in its filings with the SEC. In August 2006, the Company learned that the SEC had issued a formal order of investigation of the Company and others to determine if these or other actions, including those in other countries in which the Company does business, may have violated certain provisions of the Securities Exchange Act of 1934 and rules thereunder. In May 2008, the Company learned that Justice is conducting an investigation into possible violations of federal laws stemming from the same actions being investigated by the SEC.

The Company has been advised by Justice and the SEC that such agencies believe that violations of applicable federal laws have occurred. The Company is engaging in discussions with Justice and the SEC to effect a resolution which may involve, among other things, injunctive relief, disgorgement, fines, penalties and modifications to business practices and the appointment of a monitor. Because of existing uncertainty with respect to the scope of any possible violations and with respect to the methodology for determining the amount of potential fines, penalties or disgorgement related to any such violations, an estimate of the amount of loss, or a reliable range of estimated loss, cannot be made. Accordingly, the Company has not accrued any loss, though it believes that a loss is probable. The resolution could materially adversely affect the Company's results of operations. The Company intends to continue to cooperate with the authorities as resolution discussions proceed.

Alliance One International, Inc. and Subsidiaries

Item 1. Legal Proceedings (*Continued*)

The Company had previously disclosed that it had received notice from Mindo, S.r.l., the purchaser in June 2004 of the Company's Italian subsidiary Dimon Italia, S.r.l., of its intent to assert against the Company, or its subsidiaries, a claim arising out of that sale transaction. That claim, which may be followed by additional claims, was filed before the Court of Rome on April 12, 2007. The claim, allegedly arising from a guaranty letter issued by a consolidated subsidiary of the Company in connection with the sale transaction, seeks the recovery of €7.4 million (US\$10.6 million) plus interest and costs.

On December 13, 2007, the Public Prosecutors' offices in the States of Santa Catarina and Parana filed claims against the Company's Brazilian subsidiary, Alliance One Brazil Exportadora de Tabacos Ltda. and a number of other tobacco processors, on behalf of all tobacco farmers in those states. The lawsuits primarily assert that there exists an employment relationship between tobacco processors and tobacco farmers.

At the initial hearing in Santa Catarina, on January 29, 2008, the Court granted the Company's motion to have the case moved to the Labor Court in Brasilia. No hearing date has yet been set.

In the state of Parana, the relief sought by the Public Prosecutor was granted by the local Labor Court. The Company appealed that initial ruling and it was overturned in part and affirmed in part. The Company has appealed from that part of the initial ruling which was affirmed and no ruling has yet been rendered on the appeal. The Company has separately asserted, on April 11, 2008, a lack of jurisdiction motion similar to that which it asserted in the case in Santa Catarina which resulted in the transfer of that case to the Labor Court in Brasilia. No hearing date for that motion has been set.

On July 23, 2009, the Company received notice that Sharpmind Enterprises, Ltd., a British Virgin Islands company, had filed in the United States District Court for the Eastern District of North Carolina, a claim against the Company seeking unspecified damages for an alleged breach of a sales representation agreement between the Company and Sharpmind. Sharpmind has indicated that it would seek damages in excess of \$2.0 million. The Company views the claim as baseless and intends to vigorously defend it.





Item 1A. Risk Factors

None.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

None.

Item 3. Defaults Upon Senior Securities

None.

Item 4. Submission of Matters to a Vote of Security Holders

None.

Item 5. Other Information

None.

Item 6. Exhibits

|              |  |
|--------------|--|
| <u>4.01</u>  | Specimen of common stock certificate (filed herewith).   |
| <u>31.01</u> | Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith). |
| <u>31.02</u> | Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (filed herewith). |

Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith).

Alliance One International, Inc. and Subsidiaries

SIGNATURE

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

Alliance One International, Inc.

Date: February 8, 2010

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Hampton R. Poole, Jr.  
Vice President - Controller  
(Chief Accounting Officer)



INDEX OF EXHIBITS

Exhibits

|              |  |
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| <u>32</u>    | Certification of Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (filed herewith). |