

**UNITED STATES BANKRUPTCY COURT
WESTERN DISTRICT OF MISSOURI**

In Re:)	In Proceedings Under Chapter 11
)	
FARMLAND INDUSTRIES, INC.)	Case No. 02-50557-JWV
)	
Debtor.)	

**AFFIDAVIT OF ROBERT W. SCHULLER IN SUPPORT OF THE EXPEDITED MOTION
OF THE DEBTORS PURSUANT TO SECTIONS 105(a), 363(b)(1), AND 365 OF THE
BANKRUPTCY CODE AUTHORIZING THE DEBTORS TO ADOPT AND IMPLEMENT
A KEY EMPLOYEE RETENTION AND INCENTIVE PLAN, INCLUDING THE
ASSUMPTION AND MODIFICATION OF CERTAIN EMPLOYMENT AGREEMENTS**

STATE OF MISSOURI)	
)	ss.
COUNTY OF JACKSON)	

ROBERT W. SCHULLER being duly sworn, deposes and says:

1. I have personal knowledge of the facts set forth herein, and if called upon to testify, I could and would competently testify thereto.

2. Farmland Industries, Inc. and the other above-captioned debtors and debtors-in-possession (collectively, the “Debtors”) commenced these Chapter 11 proceedings on May 31, 2002. The Debtors continue to operate their businesses as debtors-in-possession.

3. I am employed as a Vice President of Farmland Industries, Inc. (“Farmland”), and I serve as Farmland’s General Counsel and Corporate Secretary. As such, I oversee all of the legal issues facing the Debtors. I am intimately involved monitoring the day-to-day affairs of the Debtors, including employee issues. As General Counsel of Farmland, I am familiar with the labor and employee policies of the Debtors, including compensation and severance structure, as well as the Debtors’ efforts to retain those employees that are vital to the Debtors’ future success.

4. I have been employed by the Debtors for approximately nine years.

5. I have read the Expedited Motion of the Debtors Pursuant to Sections 105(a), 363(b)(1), and 365 of the Bankruptcy Code for an Order Approving the Adoption of a Key Employee Retention and Incentive Target Plan, Including the Assumption and Modification of Certain Employment Agreements (the “Motion”), including all exhibits thereto, which was filed by the Debtors on October 23, 2002. To the best of my knowledge and belief, the statements contained in the Motion and this Affidavit are true and accurate.

6. The Debtors engage in a wide array of specialized industries, including the manufacture and marketing of fertilizer, the operation of a petroleum refinery, an integrated food and food processing business, the wholesale and retail farm supply business and a transportation brokerage business. The Debtors’ aggregate gross annual sales for the 2001 fiscal year were approximately \$11.7 billion.

7. The Debtors employ approximately 8,000 salaried and hourly employees.

8. The Debtors’ businesses are highly competitive, and the Debtors depend heavily on the skills of their management and employees to give them a competitive advantage in those industries. Due to the nature, magnitude and complexity of the Debtors’ business activities and the uncertainty surrounding these Chapter 11 proceedings, the Debtors’ ability to protect their businesses and reorganize successfully largely depends upon the retention of a select group of key employees identified in the Motion (the “Key Employees”).

9. The Key Employees have been identified by the Debtors as those employees that are absolutely essential to the Debtors’ prospects for a successful reorganization. They are employees who possess specialized knowledge, expertise or skills, and cannot be easily replaced. The

loss of the Key Employees would not only be costly for the Debtors and their estates—it could be devastating to the Debtors’ chances for reorganization and maximization of value.

10. Because the Debtors have announced the intention to sell certain business units, many of the Key Employees are experiencing a great deal of anxiety with respect to their future with the Debtors. Several of the Debtors’ employees that were extremely important to the Debtors’ businesses have recently left for other employment in the wake of the Debtors’ financial difficulties. The loss of any more Key Employees could severely disrupt the Debtors’ businesses and adversely affect the Debtors’ ability to function competitively in their industries.

11. Those Key Employees that remain with the Debtors are fearful of the unknown future of the Debtors and their own jobs. As part of their employment duties, many Key Employees have been asked to attempt to sell parts of the Debtors’ businesses. If such sales are consummated, those Key Employees may be left without employment; in other words, many Key Employees are concerned that they may be presently working themselves out of their jobs.

12. For almost five months, the Key Employees have continued to provide services and create value for the Debtors and these estates without any security with respect to the status of their employment. It has been difficult for the Key Employees to concentrate on their work without worrying about the future of their jobs. Murmurs can be heard throughout the company regarding the possibility that Key Employees might leave the Debtors for a more certain future.

13. The Key Employees must be incentivized to remain in the Debtors’ employ throughout the remainder of these Chapter 11 proceedings. Without them, the Debtors’ value will be substantially decreased, and the Debtors’ prospects for a successful reorganization will be greatly diminished.

14. The Debtors seek to implement a Key Employee Retention and Incentive Target Plan (the “KERIT Plan”), as set forth in the Motion and the attachments thereto, in order to induce the Key Employees to remain with the Debtors throughout these Chapter 11 proceedings. This Court’s approval of the KERIT Plan is in the best interests of the Debtors, their estates and all parties-in-interest, and it is essential to ensure that the Debtors preserve the going concern value of their assets.

15. The Debtors have included ninety-six Key Employees in the KERIT Plan. The Key Employees were painstakingly chosen by the Debtors through a difficult evaluation and review process. The Debtors have included only those employees who are absolutely necessary to the future success of the Debtors. These are employees without whom the Debtors’ chances for reorganization decrease dramatically.

16. The Key Employees possess rare skills, knowledge or expertise that would be extremely difficult, if not impossible, to replace. The cost of attempting to replace the Key Employees would be exceedingly high, and it would include such things as the fees of executive search firms, increased salaries and starting bonuses. The KERIT Plan is designed to prevent these expenditures from being made.

17. I have personally been involved in the formulation, structuring and negotiation of the KERIT Plan from its inception. The KERIT Plan is the result of many hours of analytical thought and thorough research regarding the goals to be accomplished and the costs to realize them. The KERIT Plan was the subject of many, many hours of negotiations with the Debtors’ creditor constituents. The KERIT Plan as presented is supported by both of the official committees appointed in these Chapter 11 proceedings, as well as the Debtors’ senior secured prepetition and postpetition lenders. The Debtors’ senior management (including myself) have exercised their best business

judgment in approving the KERIT Plan and all of its individual components and determining that the KERIT Plan is in the best interests of the Debtors and all parties-in-interest.

18. The KERIT Plan consists of three separate components: (i) an Incentive Pay Program; (ii) a Severance Program; and (iii) the modification and assumption of the employment agreements of three Key Employees. The Incentive Pay Program is further broken down into two sub-components: (i) a Fixed Incentive; and a (ii) Variable Compensation Incentive.

19. The Fixed Incentive will provide a set payment for each of the Key Employees which will be paid out in installments over the course of these Chapter 11 proceedings. It is designed to provide the Key Employees with an incentive to continue employment with the Debtors until they emerge from bankruptcy, and it is a small step toward making up for lost compensation opportunities that have not been realized in the recent past.

20. The Variable Compensation Incentive component of the KERIT Plan follows the Debtors' historical policy of providing a compensation opportunity for their employees which is based on the financial performance of the Debtors. Traditionally, the Debtors have paid below-market salaries to their employees, instead opting to provide a variable compensation opportunity for employees which is dependent upon the overall financial success of the Debtors. This variable compensation opportunity is meant to be a regular part of each employee's compensation, and it is the only way that the Debtors' salaries remain near market-competitive.

21. However, given the Debtors' financial difficulties of the recent past, employees have generally not received the expected value of the variable compensation component of their salaries. This has resulted in the Debtors' compensation package becoming relatively less competitive in the marketplace.

22. The KERIT Plan complements the Debtors' Variable Compensation Plan with a modest extra incentive of \$1.5 million for Key Employees if the Debtors reach their "target" level of performance over the next fiscal year. The Variable Compensation Incentive aligns the interests of both the Key Employees and the creditors of these Estates, as the Key Employees will be rewarded for their success in their unique roles in the creation of maximum value. The added amount of the potential Variable Compensation Incentive is quite small when compared with the Debtors' overall revenues and total assets.

23. The Severance Program component of the KERIT Plan is also basically a continuation of the historical, prepetition policy of the Debtors. Under the Debtors' prepetition severance policy, a terminated employee was given two weeks' pay per year of service. The KERIT Plan simply augments the historical program by providing a floor for Key Employees, as provided in the Motion. This floor provides a meaningful "safety net" of severance for those Key Employees whose service time is not long enough to provide them with a significant severance benefit in comparison to their value to the Debtors.

24. The severance component is meant to provide some comfort for Key Employees that their efforts in operating the Debtors and attempting to sell parts of the Debtors' businesses will not result in their termination, "not-for-cause", without appropriate compensation. The maximum incremental cost of severance over the Debtors' prepetition policy, which is added by the severance floor explained in the Motion, is approximately \$3.5 million. However, the calculation of the maximum incremental cost assumes that all Key Employees are terminated without cause prior to the consummation of the Debtors' plan of reorganization, which scenario is extremely unlikely. Key Employees who are offered comparable employment with any successor organization in a sale of any of

the Debtors' businesses are not eligible to receive severance payments. In addition, the severance payable to the Key Employees in the top three tiers of the Severance Program is subject to mitigation should they secure like employment, thus further reducing the likely cost of the program.

25. The Debtors seek to assume the Employment Agreements of three of their Key Employees in connection with the implementation of the KERIT Plan. These Employment Agreements contain relatively standard terms and conditions. Moreover, in accordance with the Motion and the KERIT Plan, the incentive payment and severance portions of the Employment Agreements will be modified so that the terms of the KERIT Plan control with respect to any discrepancies. The economic terms of the KERIT Plan are less favorable to the Key Employees than the Employment Agreements. These three employees have agreed to the changes effected in connection with the KERIT Plan. Additionally, rejection of the Employment Contracts would give rise to substantial claims.

26. The Debtors, their advisors and the other parties-in-interest involved in the formulation and negotiation of the KERIT Plan have spent a great deal of time and effort in creating a retention program that is as cost-effective as possible, while still accomplishing its goals. The Debtors have carefully weighed the costs and benefits of the KERIT Plan, and have determined that the benefits that will be realized from implementing the plan far outweigh any incremental costs that may be incurred as a result.

27. The Key Employees have been chosen carefully, and they are absolutely necessary to the ongoing success of the Debtors and the prospects for their reorganization.

28. The Debtors have been thoughtful and methodical in their structuring of the KERIT Plan. The suggestions and comments of all constituent groups have been considered, analyzed and incorporated into the KERIT Plan that is now before the Court. All parties agree that the KERIT

Plan is in the best interests of the Debtors, their estates and creditors.

29. The KERIT Plan is the least costly method for the Debtors to realize the value that the Key Employees can produce. The amount of money that will be required to implement the KERIT Plan is quite small relative to the Debtors' annual revenues and total assets. Without such a plan, the Debtors likely will experience inordinate disruption, and they will lose far more value as an ongoing enterprise than the incremental costs to implement the plan.

30. Implementation of the KERIT Plan as described in the Motion is essential to the preservation of the value of the Debtors' businesses.

31. In my judgment, and considering all of the factors involved, the failure to obtain approval of the KERIT Plan could result in the loss of the Debtors' Key Employees and a reduction in the morale of those Key Employees that remain, and it may cause a significant adverse economic impact upon the Debtors' businesses and the value of these estates.

I declare under penalty of perjury that the foregoing is true and correct.

Executed this 29 day of October, 2002, at Kansas City, Missouri.

/s/ Robert W. Schuller

Subscribed and sworn to before me this 29th day of October, 2002.

/s/ Molly A. Forge

Notary Public

My Commission Expires:

January 5, 2003