UNITED STATES
SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

☒ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

For the fiscal year ended October 31, 2009.

Or

☐ **TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934**

for the transition period from to .

Commission File Number 000-51825

Heron Lake BioEnergy, LLC

(Exact name of registrant as specified in its charter)

Minnesota	**41-2002393**
(State or other jurisdiction of incorporation or organization)	(IRS Employer Identification No.)

91246 390 th Avenue, Heron Lake, MN 56137-1375
(Address of principal executive offices)

Registrant's telephone number, including area code: **(507) 793-0077**

Securities registered pursuant to Section 12(b) of the Act:	Securities registered pursuant to Section 12(g) of the Act:
Class A Units	**None**

Name of Exchange on Which Registered: **None**

Indicate by check mark whether the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act: Yes ☐ No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act: Yes ☐ No ☒

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 ☒ 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 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer or a non-accelerated filer.

Large Accelerated Filer ☐	Accelerated Filer ☐
Non-Accelerated Filer ☐	Smaller Reporting Company ☒

Indicate by check mark whether the registrant is a shell company (as defined in Rule 126-2 of the Act) Yes ☐ No ☒

The aggregate market value of the Company's Class A Units held by non-affiliates is not able to be calculated. The Company is a limited liability company whose outstanding common equity, consisting of its Class A Units, is subject to significant restrictions on transfer under its Member Control Agreement. No public market for common equity of Heron Lake BioEnergy, LLC is established and it is unlikely in the foreseeable future that a public market for its common equity will develop.

As of January 26, 2010, the Company had outstanding 27,104,625 Class A Units.

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the registrant's definitive proxy statement for its 2010 Annual Meeting of Members, to be filed within 120 days after the end of the fiscal year covered by this report, are incorporated by reference into Part III hereof.

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PART I

When we use the terms "Heron Lake BioEnergy," "we," "us," "our," the "Company", "HLBE" or similar words in this Annual Report on Form 10-K, unless the context otherwise requires, we are referring to Heron Lake BioEnergy, LLC and its subsidiary, Lakefield Farmers Elevator, LLC with grain facilities at Lakefield and Wilder, Minnesota. Additionally, when we refer to "units" in this Annual Report on Form 10-K, unless the context otherwise requires, we are referring to the Class A units of Heron Lake BioEnergy, LLC.

Forward-Looking Statements

CAUTIONARY STATEMENTS REGARDING FORWARD-LOOKING STATEMENTS

This annual report contains historical information, as well as forward-looking statements that involve known and unknown risks and relate to future events, our future financial performance, or our expected future operations and actions. In some cases, you can identify forward-looking statements by terminology such as "may," "will," "should," "expect," "plan," "anticipate," "believe," "estimate," "future," "intend," "could," "hope," "predict," "target," "potential," or "continue" or the negative of these terms or other similar expressions. These forward-looking statements are only our predictions based on current information and involve numerous assumptions, risks and uncertainties. Our actual results or actions may differ materially from these forward-looking statements for many reasons, including the reasons described in this report under Part I, Item 1A. "Risk Factors" of this Form 10-K.

We undertake no duty to update these forward-looking statements, even though our situation may change in the future. We caution you not to put undue reliance on any forward-looking statements, which speak only as of the date of this report.

ITEM 1. BUSINESS

Overview

We were organized as a Minnesota limited liability company on April 12, 2001 under the name "Generation II, LLC." In June 2004, we changed our name to Heron Lake BioEnergy, LLC.

We were formed for the purpose of constructing and operating an ethanol manufacturing facility near Heron Lake, Minnesota. On September 21, 2007, we began operations at our dry mill, coal fired ethanol plant. Fiscal year 2007 was the first fiscal year that includes any revenue generated from our operations. In our fiscal year 2009 which ended October 31, 2009, we sold approximately 46.5 million gallons of ethanol. At nameplate, the ethanol plant has the capacity to process approximately 18.0 million bushels of corn each year, producing approximately 50 million gallons per year (mgy) of fuel-grade ethanol and approximately 160,000 tons of distillers' grains with solubles ("DGS").

The following table sets forth a summary of significant milestones in our company's history until we began operations at our plant.

Date	Milestone
February 2002	We obtained an option on land that is now part of the 216 acre site of our ethanol plant.
October 2003	We entered into an industrial water supply development and distribution agreement with the City of Heron Lake, Jackson County, and Minnesota Soybean Processors.
Early 2004	We selected Fagen, Inc. to be the design-build firm to build our ethanol plant near Heron Lake, Minnesota, using process technology provided by ICM, Inc.
September 2005	We entered into a Standard Form of Agreement between Owner and Designer — Lump Sum with Fagen, Inc.
December 2005	We purchased certain assets relating to elevator and grain storage facilities in Lakefield, Minnesota and Wilder, Minnesota with a combined storage capacity of approximately 2.8 million bushels.
May 2006	We entered into an industrial water supply treatment agreement with the City of Heron Lake and Jackson County.
August 2006	We entered into an electric service agreement with Interstate Power and Light Company (a wholly-owned subsidiary of Alliant Energy Corporation).
December 2006	We entered into a contract with Federated Rural Electric Association for the construction of the distribution system and electrical substation for the plant.
June 2007	We entered into a master coal supply agreement with Northern Coal Transportation Company (NCTC) to provide Powder River Basin (PRB) coal for the plant.
June 2007	We entered into a coal transloading agreement with Southern Minnesota Beet Sugar Cooperative (SMBSC).
September 2007	We began operations at our dry mill, coal fired ethanol plant.

Production

Since the beginning of operations at our ethanol plant, our primary business is the production and sale of ethanol and co-products, including dried distillers' grains. We currently do not have or anticipate we will have any other lines of business or other significant sources of revenue other than the sale of ethanol and ethanol co-products.

Our Ethanol Plant

Our ethanol plant was designed and built by Fagen Inc. under a September 2005 design-build agreement. Under the design-build agreement, Fagen, Inc. also agreed to utilize certain proprietary property and information of ICM, Inc. in the design and construction of our ethanol plant.

Our ethanol plant uses a dry milling process to produce fuel-grade ethanol and distillers' grains. The dry milling process involves grinding the entire corn kernel into flour and the starch is converted to ethanol through fermentation that also produces carbon dioxide and distillers' grains.

The ethanol plant consists principally of a coal handling, storage and combustion area; storage and processing areas for corn; a fermentation area comprised mainly of fermentation tanks; a distillation finished product storage area; and a drying unit for processing the dried distillers' grains. Additionally, the ethanol plant contains receiving facilities that have the ability to receive corn by rail and truck, store it for use in the plant and prepare the corn to be used in the plant. We have storage tanks on site to store the ethanol we produce. The plant also contains a storage building and silos to hold distillers' grains until it is shipped to market.

The Union Pacific Railroad is the railroad adjacent to our ethanol plant. The ethanol plant has the facilities necessary to receive corn by truck and rail, coal by truck, and to load ethanol and distillers grains onto trucks and rail cars.

As part of our design-build agreement with Fagen, Inc., we received performance guarantees on the production through put and process efficiencies of our ethanol plant. Fagen, Inc. has also warranted that the air emissions on our ethanol facility, taken as a whole, when operating at nameplate capacity meeting all of the performance guarantee criteria, will meet the requirements of a synthetic minor source within six months following the date of substantial completion. If this warranty is not met, Fagen, Inc. will pay all design, engineering, equipment, labor and construction costs associated with making the necessary corrections to meet the warranty, subject to certain restrictions. Notwithstanding that we began operations on September 21, 2007, our plant does not yet meet the warranties relating to air emissions.

We have made payments to Fagen, Inc. as required under the design-build agreement and as provided in the design-build agreement. We retained 10% of each payment until 50% of the required work was completed by Fagen, Inc. As of October 31, 2009, we have retained approximately $3.8 million in payments to Fagen, Inc. We have been unsuccessful in resolving a dispute with Fagen, Inc, with regard to its liability for our claims under the design-build agreement. On September 18, 2009, we commenced an arbitration action against Fagen, Inc. following these unsuccessful attempts. Our claims are for breach of warranty, breach of contract, and negligence, among other counts, and we are asking for total damages of approximately $22.8 million. A revised demand for arbitration was served and filed on December 23, 2009 following an unsuccessful attempt to mediate the dispute. Fagen, Inc. responded to the demand for arbitration by denying liability and asserting various affirmative defenses. In addition, Fagen, Inc. brought a counterclaim alleging that it is entitled to payment of the retainage we hold in the amount of approximately $3.8 million. In addition, Fagen, Inc. alleges that it performed additional work and provided additional labor and materials to the plant in the amount of approximately $2.2 million, which did not constitute warranty or guarantee work and therefore, it claims it is entitled to payment of this additional amount. We responded to the counterclaim by denying the allegations and asserting various affirmative defenses. On January 4, 2010, Fagen, Inc. requested to join ICM, Inc. as a party to the arbitration action, claiming that joinder was necessary for proper resolution of the claims and defenses in the arbitration action. On January 27, 2010, ICM, Inc. responded to the request, agreeing to be joined provided certain procedures are established. In its response, ICM also indicated that it intends to assert claims against us under the license agreement we entered into with ICM as part of the design build agreement with Fagen. On January 27, 2010, we filed our response and objections to Fagen's request to join ICM as a party, and requested that a special arbitrator be appointed to resolve the joinder issues. We intend to defend against the Fagen counterclaims and any claims brought by ICM, Inc. and assert our defenses vigorously. Please see Part I, Item 3 "Legal Proceedings" of this Form 10-K for a description of the arbitration action against Fagen, Inc. relating to the design-build agreement.

Our ethanol plant requires significant and uninterrupted amounts of electricity, coal and water. We have entered into agreements for our supply of electricity, coal and water.

Currently, fly-ash generated from the coal burned by our plant is hauled to a landfill. If it qualifies to predefined industry standards, fly-ash can be used as an admixture for cement mixes instead of being hauled to landfills. We are continuing to explore revenue-generating alternatives from fly-ash rather than incurring expense associated with shipping the fly-ash to landfills.

Our Principal Products

The principal products that we produce are fuel grade ethanol and distillers' grains. Raw carbon dioxide is also a product of the ethanol production process, but we do not capture or market any carbon dioxide gas.

Ethanol

Ethanol is a type of alcohol produced in the U.S. principally from corn. Ethanol is primarily used in the U.S. gasoline fuel market as:

- an octane enhancer in fuels;
- an oxygenated fuel additive that can reduce ozone and carbon monoxide vehicle emissions;
- a gasoline substitute generally known as E85, a fuel blend composed of 85% ethanol; and
- as a renewable fuel to displace consumption of imported oil.

Ethanol used as an octane enhancer or fuel additive is blended with unleaded gasoline and other fuel products. The principal purchasers of ethanol are generally wholesale gasoline distributors or blenders.

Distillers' Grains

The principal co-product of the ethanol production process is distillers' grains, a high protein and high-energy animal feed ingredient.

Dry mill ethanol processing creates three primary forms of distillers' grains: wet distillers' grains, modified wet distillers' grains, and dried distillers' grains with solubles. Wet distillers' grains are processed corn mash that contains a substantial amount of moisture. It has a shelf life of approximately three days and is primarily sold to feeders of beef animals within the immediate vicinity of the ethanol plant. Modified wet distillers' grains are similar to wet distillers' grains except that it has been partially dried and contains less moisture. Modified wet distillers' grains has a shelf life of a maximum of fourteen days, contains less water to transport, is more easily adaptable to some feeding systems, and is sold to both local and regional markets, primarily for both beef and dairy animals. Dried distillers' grains with solubles are corn mash that has been dried to approximately 10% moisture. It has an almost indefinite shelf life and may be sold and shipped to any market and to almost all types of livestock. Most of the distillers' grains that we sell are in the form of dried distillers' grains.

Procurement and Marketing Agreements

Corn Procurement

The primary raw material used in the production of ethanol at our plant is corn. We need to procure approximately 18 million bushels of corn per year for our dry mill ethanol process. We generally do not have long-term, fixed price contracts for the purchase of corn and our members are not obligated to deliver corn to us. Typically, we purchase our corn directly from grain elevators, farmers, and local dealers within approximately 80 miles of Heron Lake, Minnesota.

We generally purchase corn through cash fixed-price contracts and may utilize hedging positions in the corn futures market for a portion of our corn requirements to manage the risk of excessive corn price fluctuations. Our fixed-price forward contracts specify the amount of corn, the price and the time period over which the corn is to be delivered. These forward contracts are at fixed prices or prices based on the Chicago Board of Trade (CBOT) prices. Our corn requirements can be forward contracted on either a fixed-price basis or futures only contracts. The parameters of these contracts are based on the local supply and demand situation and the seasonality of the price. We also purchase a portion of our corn on a spot basis.

The price and availability of corn is subject to significant fluctuation depending upon a number of factors that affect commodity prices generally. These include, among others, crop conditions, crop production, weather, government programs, and export demands. We believe that our corn storage facilities in Lakefield and Wilder, Minnesota enable us to more favorably procure corn for the operation of our plant.

Coal Procurement

We have constructed a coal receiving, handling and storage facility next to the ethanol plant. Due to air permitting, and performance and emissions guarantees of the design-build contract with Fagen, Inc., a Wyoming/Montana-sourced coal must be used. As a result, in June 2007, we entered into a master coal supply agreement with Northern Coal Transportation Company (NCTC) to provide Powder River Basin (PRB) coal for the plant. The master coal supply agreement expires upon 60 days notice by either party. We are obligated to purchase coal and NCTC is obligated to sell coal identified in a confirmation that sets forth the quantity, price, term, mine and other relevant terms. Under a letter confirmation dated July 2007, we agreed to purchase a minimum number of tons in each contract year which runs from June 1 to May 31 through the five year period ending May 31, 2012. The letter confirmation also sets the price per ton for each contract year. Also, in June 2007, we entered into a coal transloading agreement with Southern Minnesota Beet Sugar Cooperative (SMBSC). SMBSC also uses coal of the same type as our ethanol plant to fuel its beet sugar plant. In order to achieve transportation efficiencies, we and SMBSC entered into the coal transloading agreement so that both of our coal orders could be delivered to a single facility (the transloading facility) owned by SMBSC. The coal is transferred from the transloading facility to each of our respective plants and we pay SMBSC a per ton charge handling fee for the use of the transloading facility.

Ethanol Marketing

Effective September 30, 2009, we entered into an ethanol marketing agreement with C&N Ethanol Marketing Corporation (“C&N”). Under the Agreement, C&N will purchase, market and re-sell all of the ethanol produced at the Company’s plant for the three year term of the Agreement. Following the three year term, the Agreement will automatically renew for subsequent year terms unless either party terminates the agreement 60 days before the end of the term. C&N will provide the Company with a remittance by Wednesday of each week for shipments of ethanol in the previous week and the Company will receive payment against that remittance on the following Wednesday. C&N will pay the Company the gross sales price to the customer less expenses and a 1% marketing fee after expenses. The Agreement also contains provisions addressing other matters, including forecasting, the quality of product, transfer of title and auditing of records.

The Company has notified RPMG, Inc. (“RPMG”) of the termination effective September 30, 2009 of the Ethanol Fuel Marketing Agreement between the Company and RPMG, Inc. dated August 7, 2006 (the “Prior Agreement”). Under the Prior Agreement, RPMG marketed all ethanol produced by the Company’s ethanol plant pursuant to a pooled marketing arrangement. The Company received a price equal to the actual pooled price received by RPMG, less the expense of distribution and a marketing fee charged per gallon of ethanol sold.

Ethanol revenues during the period ended October 31, 2009 were approximately $70.4 million, comprising 80% of our revenues. Sales of ethanol through September 30, 2009 were made pursuant to the terms of our ethanol marketing agreement with RPMG, Inc. under which our ethanol was pooled with the ethanol of other ethanol producers whose ethanol was marketed by RPMG. We paid RPMG a marketing fee and RPMG paid us a netback price per gallon that is based upon the difference between the pooled average delivered ethanol selling price and the pooled average distribution expense. These averages were calculated based upon each pool participant’s selling price and expense averaged in direct proportion to the volume of ethanol supplied by each participant to the pool.

We believe that the ethanol market structure has changed since we entered into our ethanol marketing agreement with RPMG, and in particular during the past one to two years. We determined, in light of those changes, that the pool marketing arrangement used by RPMG was no longer an effective arrangement under the current market structure and circumstances. We accordingly notified RPMG that the ethanol marketing agreement would be terminated effective September 30, 2009.

Distillers’ Grains Marketing

In addition to ethanol, our ethanol plant produces wet, modified wet and dried distillers’ grains.

In October 2005, we entered a marketing agreement with Commodity Specialists Corporation for the sale to Commodity Specialists Corporation of all distillers’ grains produced by our ethanol plant. The term of the agreement is for a one-year period from the date of start-up of our operations, and thereafter, the agreement will remain in effect unless terminated by either party upon 90 days’ written notice. Under the terms of the agreement, we receive a price equal to the selling price, less a charge of 2% or 4% of the price for distillers’ grains and a fee of $2.00 per ton of solubles, less the cost of delivering the product to the customer. In August 2007, as part of CHS Inc.’s acquisition of Commodity Specialist Corporation, our agreement with Commodity Specialist Corporation was assigned to CHS Inc. with our consent.

Pricing of Corn and Ethanol

The sale of ethanol represented approximately 80% of our revenue for the year ended October 31, 2009. The cost of corn represented approximately 70% of our cost of sales for the year ended October 31, 2009. In the future, we expect that ethanol sales will represent our primary revenue source and corn will represent our primary component of cost of goods sold. Therefore, changes in the price at which we can sell the ethanol we produce and the price at which we buy corn for our ethanol plant present significant operational risks inherent in our business.

Generally, the price at which ethanol can be sold does not track with the price at which corn can be bought. Historically, ethanol prices have tended to correlate with wholesale gasoline prices, with demand for and the price of ethanol increasing as supplies of petroleum decreased or appeared to be threatened, crude oil prices increased and wholesale gasoline prices increased. However, the prices of both ethanol and corn do not always follow historical trends. Trends in ethanol prices and corn prices are subject to a number of factors and are difficult to predict.

Demand for Ethanol

In recent years, the demand for ethanol has increased, particularly in the upper Midwest, in part because of two major programs established by the Clean Air Act Amendments of 1990: the Oxygenated Gasoline Program and the Reformulated Gasoline Program. Under these programs, an additive (oxygenate) was required to be added to the gasoline used in areas with excessive carbon monoxide or ozone pollution to help mitigate these conditions. Because of the potential health and environmental issues associated with methyl tertiary butyl ether (MTBE) and the actions of the EPA, ethanol is now used as the primary oxygenate in those areas requiring an oxygenate additive under programs associated with the Clean Air Act Amendments of 1990 or other federal law. According to the EPA, as of May 2007, various regions of 15 states and the District of Columbia were required to comply with the Reformulated Gasoline Program and all or a portion of an additional 13 states have voluntarily opted into the program.

In addition to demand for ethanol as an oxygenate, ethanol demand has increased because of the adoption of programs setting national renewable fuels standards (RFS). The first RFS program was introduced through the Energy Policy Act of 2005. The Energy Policy Act of 2005 introduced a RFS program that set a national minimum usage requirement that would phase in over seven years, beginning with approximately 4.0 billion gallons in 2006 and increasing to 7.5 billion gallons by 2012. The minimum usage requirements under the 2005 RFS program were increased with the Energy Independence and Security Act of 2007. Currently, the minimum usage requirements are 13.2 billion gallons of renewable biofuels by 2012 and 15.0 billion gallons by 2015. The Energy Independence and Security Act of 2007 also mandates a minimum requirement of 36 billion gallons of renewable fuels by 2022, with conventional biofuels accounting for 15 billion gallons of this total. Conventional biofuel is ethanol derived from corn starch and conventional ethanol facilities that commence construction after the date of enactment and must achieve a 20 percent greenhouse gas (GHG) emissions reduction compared to baseline lifecycle GHG emissions. Advanced biofuels are defined as cellulosic ethanol and other biofuels derived from feedstock other than corn starch that achieves a 50 percent GHG emissions reduction requirement. Cellulosic ethanol is any cellulose, hemicellulose, or lignin that is derived from renewable biomass and achieves a 60 percent GHG emission reduction requirement. We believe the RFS program creates greater market for renewable fuels, such as ethanol, as a substitute for petroleum-based fuels.

In addition to the RFS program, one important incentive for the ethanol industry and its customers is the Volumetric Ethanol Excise Tax Credit, commonly referred to as the “blender’s credit.” The tax credit is provided to gasoline distributors as an incentive to blend their gasoline with ethanol. For each gallon of gasoline blended with ethanol, the distributors receive a tax credit. For 2008, the tax credit is 51¢ per gallon of pure ethanol or 5.1¢ per gallon of gasoline blended with 10% ethanol. The per gallon credit was reduced to 45¢ per gallon of pure ethanol in 2009. The tax credit is authorized through December 21, 2010.

In Minnesota, a market we serve, the demand for ethanol is driven, in part, by state specific requirements. Minnesota has enacted a law that requires all Minnesota gasoline to be blended with 20 percent ethanol. The new E-20 mandate would take effect in 2013 unless ethanol has already replaced 20 percent of the state’s motor vehicle fuel by 2010. The rule would expire at the end of 2010 if Minnesota is not granted federal approval to use E-20 gasoline blends. Minnesota has North America’s largest network of E-85 (85% ethanol blend) gas stations with approximately 350 stations now available to consumers. Minnesota was the first state to require the use of ethanol in gasoline. Other states are beginning to enact similar legislation and this may also drive the demand for ethanol in markets we serve.

Markets for Ethanol

There are local, regional and national markets for ethanol. Typically, a regional market is one that is outside of the local market, yet within the neighboring states. Some regional markets include large cities that are subject to anti-smog measures in either carbon monoxide or ozone non-attainment areas, or that have implemented oxygenated gasoline programs, such as Chicago, St. Louis, Denver and Minneapolis. We consider our primary regional market to be large cities within a 450-mile radius of our ethanol plant. In the national ethanol market, the highest demand by volume is primarily in the southern United States and the east and west coast regions.

The markets in which our ethanol is sold will depend primarily upon the efforts of C&N, which buys and markets our ethanol. However, we believe that local markets will be limited and must typically be evaluated on a case-by-case basis. Although local markets will be the easiest to service, they may be oversold because of the number of ethanol producers near our plant, which may depress the price of ethanol in those markets.

We transport our ethanol primarily by rail. In addition to rail, we service certain regional markets by truck from time to time. We believe that regional pricing tends to follow national pricing less the freight difference.

We believe that the E10 “blend wall” is one of the most critical governmental policies currently facing the ethanol industry. The “blend wall” issue arises because of several conflicting requirements. First, the renewable fuels standards dictate a continuing increase in the amount of ethanol blended into the national gasoline supply. Second, the Environmental Protection Agency (EPA) mandates a limit of 10% ethanol inclusion in non-flex fuel vehicles, and the E85 vehicle marketplace is struggling to grow due to lacking infrastructure. Total gasoline usage by the U.S. is currently around 138 billion gallons, and is expected to decrease to less than 130 billion gallons over the next 5 years as fuel mileage standards are changed. The RFS dictates an increasing amount of ethanol blending: 13.95 billion gallons in 2011, 15.2 billion gallons in 2012, and increasing to 36 billion gallons by 2022. To reach the standard as dictated by the RFS in 2011, assuming 135 billion gallons of total gasoline usage nationally, each gallon of gasoline sold would have to be blended with greater than 10% ethanol. The EPA policy of 10% and the RFS increasing blend rate are at odds, which is sometimes referred to as the “blend wall.” One industry group has petitioned the EPA for a waiver of the E10 law and an increase to E15. The EPA has currently postponed the expected December 2009 decision. This issue is a major risk to the ethanol industry.

Markets for Distillers’ Grains

We sell distillers’ grains as animal feed for beef and dairy cattle, poultry and hogs. However, the modified wet distillers’ grains typically have a shelf life of a maximum of fourteen days. This provides for a much smaller market and makes the timing of its sale critical. Further, because of its moisture content, the modified wet distillers’ grains are heavier and more difficult to handle. The customer must be close enough to justify the additional handling and shipping costs. As a result, modified wet distillers’ grains are principally sold only to local feedlots and livestock operations.

Various factors affect the price of distillers’ grain, including, among others, the price of corn, soybean meal and other alternative feed products, the performance or value of distillers’ grains in a particular feed market, and the supply and demand within the market. Like other commodities, the price of distillers’ grains can fluctuate significantly.

Competition

Producers of Ethanol

We sell our ethanol in a highly competitive market. We are in direct competition with numerous other ethanol producers, both regionally and nationally, many of which have more experience and greater resources than we have. Some of these producers are, among other things, capable of producing a significantly greater amount of ethanol or have multiple ethanol plants that may help them achieve certain benefits that we could not achieve with one ethanol plant. Further, new products or methods of ethanol production developed by larger and better-financed competitors could provide them competitive advantages over us and harm our business. A majority of the ethanol plants in the U.S. and the greatest number of gallons of ethanol production are located in the corn-producing states, such as Iowa, Nebraska, Illinois, Minnesota, South Dakota, Indiana, Ohio, Kansas, and Wisconsin.

Below is the U.S. ethanol production by state in millions of gallons for the ten states with the most total ethanol production, either online or under construction/expansion, as of January 2009:

State	Online	Under Construction/ Expansion	Total
Iowa	*3,076.0*	*690.0*	*3,766.00*
Nebraska	*1,444.0*	*319.0*	*1,763.0*
Illinois	*1,190.0*	*293.0*	*1,483.0*
Minnesota	*1,081.6*	*50.0*	*1,131.6*
South Dakota	*1,016.0*	*33.0*	*1,049.0*
Indiana	*899.0*	*88.0*	*987.0*
Ohio	*470.0*	*65.0*	*535.0*
Kansas	*491.5*	*20.0*	*511.5*
Wisconsin	*498.0*	*0.0*	*498.0*
Texas	*250.0*	*115.0*	*365.0*

Source: Renewable Fuels Association, January 2009

Accordingly, we face increased competition because of the location of our ethanol plant in Minnesota. We believe that the competition in the ethanol market will increase in the near term as the ethanol plants recently sold through bankruptcy proceedings return to production. For example, in May 2009, Valero Energy Corporation and its subsidiaries purchased seven idle plants from VeraSun Energy Corporation as part of VeraSun's reorganization. Several of our competitors including certain subsidiaries of Otter Tail Ag Enterprises, Pacific Ethanol, Inc. and Aventine Renewable Energy Holdings, Inc. have filed to reorganize under federal bankruptcy laws as a result of margin pressure, inadequate liquidity and other considerations.

According to the Renewable Fuel Association (RFA), as of October 2009, 202 U.S. facilities have the capacity to produce approximately 13.1 billion gallons of ethanol annually. Despite the rapid increase in production, consumption of ethanol has been outpacing production for the past few years, which has led to increased imports in the United States, primarily from Brazil. According to the RFA, from January to October of 2008, the U.S. produced 7.5 billion gallons of fuel ethanol and imported 515.6 million gallons. In addition to intense competition with local, regional and national producers of ethanol, we expect increased competition with imported ethanol and foreign producers of ethanol.

Producers of Other Fuel Additives and Alternative Fuels

In addition to competing with ethanol producers, we also compete with producers of other gasoline oxygenates. Many gasoline oxygenates are produced by other companies, including oil companies, that have far greater resources than we have. Historically, as a gasoline oxygenate, ethanol primarily competed with two gasoline oxygenates, both of which are ether-based: MTBE (methyl tertiary butyl ether) and ETBE (ethyl tertiary butyl ether). Many states have enacted legislation prohibiting the sale of gasoline containing certain levels of MTBE or are phasing out the use of MTBE because of health and environmental concerns. As a result, national use of MTBE has decreased significantly in recent years. Use of ethanol now exceeds that of MTBE and ETBE as a gasoline oxygenate.

While ethanol has displaced these two gasoline oxygenates, the development of ethers intended for use as oxygenates is continuing and we will compete with producers of any future ethers used as oxygenates.

A number of automotive, industrial and power generation manufacturers are developing alternative fuels and power systems, both for vehicles and other applications. Fuel cells have emerged as a potential alternative power system to certain existing power sources because of their higher efficiency, reduced noise and lower emissions. Fuel cell industry participants are currently targeting the transportation, stationary power and portable power markets in order to decrease fuel costs, lessen dependence on crude oil and reduce harmful emissions.

Additionally, there are more than a dozen alternative and advanced fuels currently in development, production or use, including the following alternative fuels that, like ethanol, have been or are currently commercially available for vehicles:

- biodiesel
- electricity
- hydrogen
- methanol
- natural gas
- propane

Several emerging fuels are currently under development. Many of these fuels are also considered alternative fuels and may have other benefits such as reduced emissions or decreasing dependence upon oil. Examples of emerging fuels include:

- Biobutanol: Like ethanol, biobutanol is an alcohol that can be produced through the processing of domestically grown crops, such as corn and sugar beets, and other biomass, such as fast-growing grasses and agricultural waste products.

- Biogas: Biogas is produced from the anaerobic digestion of organic matter such as animal manure, sewage, and municipal solid waste. After it is processed to required standards of purity, biogas becomes a renewable substitute for natural gas and can be used to fuel natural gas vehicles.

- Fischer-Tropsch Diesel: Diesel made by converting gaseous hydrocarbons, such as natural gas and gasified coal or biomass, into liquid fuel, including transportation fuel

- Hydrogenation-Derived Renewable Diesel (HDRD): The product of fats or vegetable oils—alone or blended with petroleum—that has been refined in an oil refinery

- P-Series: A blend of natural gas liquids (pentanes plus), ethanol, and the biomass-derived co-solvent methyltetrahydrofuran (MeTHF) formulated to be used in flexible fuel vehicles

- Ultra-Low Sulfur Diesel: This is diesel fuel with 15 parts per million or lower sulfur content. This ultra-low sulfur content enables the use of advanced emission control technologies on vehicles using ULSD fuels produced from non-petroleum and renewable sources that are considered alternative fuels.

Additionally, there are developed and developing technologies for converting natural gas, coal and biomass to liquid fuel, including transportation fuels such as gasoline, diesel, and methanol.

We expect that competition will increase between ethanol producers, such as Heron Lake BioEnergy, LLC and producers of these or other newly developed alternative fuels or power systems, especially to the extent they are used in similar applications such as vehicles.

Producers of Distillers' Grains

The amount of distillers' grains produced annually in North America is expected to increase significantly as the number of ethanol plants increase. We compete with other producers of distillers' grains products both locally and nationally, with more intense competition for sales of distillers' grains among ethanol producers in close proximity to our ethanol plant. There are 7 ethanol plants within an approximate 50 mile radius of our plant with a combined ethanol capacity of 436 mgy that will produce approximately 1.4 million tons of distillers' grains. These competitors may be more likely to sell to the same markets that we target for our distillers' grains.

Additionally, distillers' grains compete with other feed formulations, including corn gluten feed, dry brewers' grain and mill feeds. The primary value of these products as animal feed is their protein content. Dry brewers' grain and distillers' grains have about the same protein content, and corn gluten feed and mill feeds have slightly lower protein contents. Distillers' grains contain nutrients, fat content, and fiber that we believe will differentiate our distillers' grains products from other feed formulations. However, producers of other forms of animal feed may also have greater experience and resources than we do and their products may have greater acceptance among producers of beef and dairy cattle, poultry and hogs

Competition for Corn

We will compete with ethanol producers in close proximity for the supplies of corn we will require to operate our plant. Ethanol production consumes a significant portion of Minnesota's corn crop, approximately 30% for 2009. The existence and development of other ethanol plants, particularly those in close proximity to our plant, will increase the demand for corn that may result in higher costs for supplies of corn. There are 7 ethanol plants within an approximate 50 mile radius of our plant with a combined ethanol capacity of 436 mgy will use approximately 160 million bushels of corn.

We compete with other users of corn, including ethanol producers regionally and nationally, producers of food and food ingredients for human consumption (such as high fructose corn syrup, starches, and sweeteners), producers of animal feed and industrial users. According to the U.S. Department of Agriculture, for 2009: 3.7 billion bushels of U.S. corn was used in ethanol production, with 1.3 billion bushels being used in food and other industrial uses, and 2.0 billion bushels used for export.

Competition for Personnel

We will also compete with ethanol producers in close proximity for the personnel we will require to operate our plant. The existence and development of other ethanol plants will increase competition for qualified managers, engineers, operators and other personnel. We also compete for personnel with businesses other than ethanol producers and with businesses located outside the community of Heron Lake, Minnesota.

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Hedging

We may hedge anticipated corn purchases and ethanol and distillers' grain sales through a variety of mechanisms.

We procure corn through spot cash, fixed-price forward, basis only, futures only, and delayed pricing contracts. Additionally, we may use hedging positions in the corn futures and options market to manage the risk of excessive corn price fluctuations for a portion of our corn requirements.

For our spot purchases, we post daily corn bids so that corn producers can sell to us on a spot basis. Our fixed-price forward contracts specify the amount of corn, the price and the time period over which the corn is to be delivered. These forward contracts are at fixed prices indexed to Chicago Board of Trade, or CBOT, prices. Our corn requirements can be contracted in advance under fixed-price forward contracts or options. The parameters of these contracts are based on the local supply and demand situation and the seasonality of the price. For delayed pricing contracts, producers will deliver corn to our elevators, but the pricing for that corn and the related payment will occur at a later date.

To hedge a portion of our exposure to corn price risk, we may buy and sell futures and options positions on the CBOT. In addition, our facilities have significant corn storage capacity. We generally maintain inventories of corn at our ethanol plant, but can draw from our elevators at Lakefield and Wilder to protect against supply disruption. At the ethanol plant, we have the ability to store approximately 10 days of corn supply and our elevators have capacity for approximately an additional 50 days of supply.

We currently market all of our ethanol through C&N and until September 2009 marketed all of our ethanol through RPMG, Inc. Our marketers are obligated to use reasonable efforts to obtain the best price for our ethanol. To mitigate ethanol price risk and to obtain the best margins on ethanol that is marketed and sold by our marketer, we may utilize ethanol swaps, over-the-counter ("OTC") ethanol swaps, or OTC ethanol options that are typically settled in cash, rather than gallons of the ethanol we produce.

Our marketing and risk management committee, consisting of Doug Schmitz, David J. Woestehoff, Timothy O. Helgemoe, and David M. Reinhart, assists the board and our risk management personnel to, among other things, establish appropriate policies and strategies for hedging and enterprise risk.

Compliance with Environmental Laws and Other Regulatory Matters

Our business subjects us to various federal, state and local environmental laws and regulations, including those relating to discharges into the air, water and ground; the generation, storage, handling, use, transportation and disposal of hazardous materials; and the health and safety of our employees.

These laws and regulations require us to obtain and comply with numerous permits to construct and operate our ethanol plant, including water, air and other environmental permits. On March 12, 2007, we entered into an agreement with Fagen Engineering, LLC, an affiliate of Fagen, Inc., for the development of environmental compliance programs and related services, which was completed in September 2007. On March 26, 2008, we entered into an agreement with Fagen Engineering, LLC for environmental compliance training services.

The costs associated with obtaining these permits and meeting the demands of regulators reflected in the permits have increased our costs of construction and production. In particular, we have incurred additional costs relating to an air-emission permit from the Minnesota Pollution Control Agency ("MPCA"). We applied for a synthetic minor air-emissions source permit in July 2004 that was granted by the MPCA in May 2005. In June 2005, a coalition of two environmental groups and one energy group challenged the grant of this air emissions permit by an appeal to the Minnesota Court of Appeals. In July 2006, the Minnesota Court of Appeals affirmed the MPCA's issuance of the permit. In conjunction with the permit and the permit dispute and to prevent further appeals by the coalition, we entered into a compliance agreement with the MPCA on January 23, 2007 that currently governs the air emissions from our plant. Under the compliance agreement, we agreed to submit an amendment to our air permit to qualify our facility as a "major emissions source". The compliance agreement also allowed us to continue with the construction of our facility. Under the compliance agreement, we agreed to operate our facility in a manner such that the emissions of each of the criteria pollutants generated by our ethanol plant, as determined on a 12 month rolling sum, do not exceed 95 tons per year and agreed to comply in all other respects with the air emissions permit previously issued by the MPCA. Accordingly, we submitted a major amendment to our existing air-emissions permit in December 2008, and, following air pollution control device testing, we submitted a second major amendment in September 2009, both seeking amendments to our air permit, including amendments to permit conditions and adjustments to other components of plant operations and production. However, we are continuing discussions with the MPCA regarding the necessity for qualifying our facility as a major emissions source, particularly in light of changes in federal law that increased the limit of certain emissions allowed as a synthetic minor source. On March 13, 2008, MPCA issued a notice of violation to us for violations of certain rules, statutes, and permit conditions (as modified by the compliance agreement), including emission violations and reporting violations. As part of our continuing discussions with MPCA, we are seeking to resolve these violations by agreement with MPCA. Such resolution may result in the payment of a civil penalty or other sanctions and remedies available to MPCA. Pending the resolution of this air permit issue, we continue to operate subject to the compliance agreement.

Other than as discussed above, we have obtained all permits we believe are necessary for the operation of our ethanol plant.

Compliance with these laws and permits in the future could require expensive pollution control equipment or operational changes to limit actual or potential impacts to the environment, as well as significant management time and expense. A violation of these laws, regulations or permit conditions can result in substantial fines, natural resource damage, criminal sanctions, permit revocations and/or plant shutdown, any of which could have a material adverse effect on our operations. We have incurred costs associated with obtaining the air permits and costs associated with the compliance agreement of approximately $187,000 in fiscal year 2007, $208,000 in fiscal year 2008 and $452,000 in fiscal year 2009. In addition, we have incurred costs associated with equipment failures and/or warranty and other claims against Fagen, Inc. of approximately $2,700,000.

Employees

As of October 31, 2009, we had 51 full-time employees, of which 42 are in operations and 9 are in executive, general management and administration. We also have three part-time employees in operations. We also have engaged Brett L. Frevert of CFO Systems, LLC as our interim chief financial officer on a contract basis. We do not maintain an internal sales organization, but instead rely upon third-parties to market and sell the ethanol and distillers' grains that we produce.

Corporate Information

Our principal executive offices are located at 91246 390 th Avenue, Heron Lake, Minnesota 56137 and our telephone number is 507-793-0077. We maintain an Internet website at www.heronlakebioenergy.com. We make available free of charge on or through our Internet website, www.heronlakebioenergy.com, all of our reports and all amendments to those reports as soon as reasonably practicable after such material is electronically filed with, or furnished to, the Securities and Exchange Commission (SEC). We will provide electronic or paper copies of these documents free of charge upon request.

Additionally, the SEC maintains an Internet site that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the SEC at www.sec.gov.

ITEM 1A. RISK FACTORS

If any of the following risks actually occur, our results of operations, cash flows and the value of our units could be negatively impacted.

Risks Related to Our Business and Operations

We are in default of our master loan agreement with AgStar Financial Services, PCA ("AgStar").

At October 31, 2009, we were in default of covenants of our master loan agreement with AgStar requiring us to maintain at least $5.0 million minimum working capital; at least $39.5 million of tangible net worth; and a fixed charge ratio of 1.20 to 1.00 or greater. Additionally, we do not expect to be in compliance with one or more covenants of the master loan agreement as of fiscal year end 2010. All of our assets and real property are subject to security interests and mortgages in favor of AgStar as security for the obligations of the master loan agreement. Our failure to maintain the required amount of working capital constitutes an event of default under the master loan agreement, entitling the lender to accelerate and declare due all amounts outstanding under the master loan agreement.

As a result of these defaults, we have classified $49.3 in long-term debt as a current liability. As a result, current liabilities as of October 31, 2009 totaled approximately $69.1 million, including this $49.3 million. This compares to cash and cash equivalents (other than restricted cash) at October 31, 2009 of approximately $3.2 million, current assets of approximately $12.9 million and total assets of approximately $113.1 million. In the absence of a waiver of the covenant defaults, amendment to the master loan agreement or refinancing of the master loan agreement, we do not have adequate capital to repay all of the amounts that would become due upon acceleration.

Also part of our master loan agreement with AgStar is a line of credit for up to $6,750,000. Effective December 8, 2009, AgStar agreed to extend the maturity date of this line of credit to February 1, 2010. At October 31, 2009 and January 20, 2010, the outstanding balance of the revolving line of credit was $5.0 million.

We are currently in negotiations with AgStar to extend the maturity of the line of credit and to waive the event of default arising from the failure to meet the covenants described above. In the absence of a waiver or an amendment to the line of credit to extend the maturity date, we do not have adequate capital to repay the currently outstanding amounts on the line of credit. There is no assurance that any amendment or extension of maturity will be provided by the lender or that the line of credit, if renewed, will allow for up to $6.75 million in available borrowing. Further, while an event of default exists, we are not permitted to borrow additional funds under our line of credit or revolving term note unless AgStar consents.

If we do not receive waiver of the events of default under the master loan agreement and an extension of maturity of our line of credit, we may be required to attempt to refinance our debt, curtail significantly, or stop our business activities. If the lender enforces its rights under the master loan agreement to accelerate the indebtedness or proceed against our assets to collect on the indebtedness, we may lose control of our business and be forced to sell assets, restructure our indebtedness or submit to foreclosure proceedings, all of which could result in a material adverse effect upon our business, results of operations and financial condition.

We are involved in a dispute with Fagen, Inc. relating to the design-build agreement for our ethanol plant and the performance guarantees and warranties relating to our plant, including those relating to air emissions.

Our ethanol plant was constructed under a design-build agreement with Fagen, Inc. ("Fagen") as the design-builder. We have retained approximately $3.8 million in payments to Fagen under the design-build agreement. Under the design-build agreement, Fagen has warranted that within six months following the date of substantial completion, the emissions of our ethanol plant will meet the requirements of a synthetic minor source. Notwithstanding that we began operations on September 21, 2007, our plant does not yet meet the warranties relating to air emissions and therefore, we continue to withhold approximately $3.8 million in retainage.

We have tested a number of possible solutions to enable our plant to meet the air emissions warranties. To date, none of these solutions has been effective and there may be no solution that will allow our plant to meet the warranties relating to air emissions. Further, in testing these potential solutions, we have suffered substantial reduction in daily ethanol production and plant shutdowns as a result. As we attempt new solutions in the future, we also expect that we will be required to limit production or shutdown our plant, which will impair our ability to produce ethanol and generate revenue.

On September 18, 2009, we commenced an arbitration action against Fagen relating to the design-build agreement and we are seeking approximately $22.8 million in damages. Please see Part I, Item 3 "Legal Proceedings" of this Form 10-K for a description of the arbitration action against Fagen, Inc. relating to the design-build agreement. In response, Fagen has asserted counterclaims, including for payment of the approximately $3.8 million in retainage and for approximately $2.2 million in additional labor and materials it claims it provided to us. In addition, Fagen has requested to join ICM, Inc. as a party to the arbitration action. In its response, ICM also indicated that it intends to assert claims against us under the license agreement we entered into with ICM as part of the design build agreement with Fagen. We objected to Fagen's request to join ICM as a party to the arbitration action.

There is no assurance that we will resolve the air emissions warranty or the dispute with Fagen to our satisfaction or that we will resolve it without significant additional expense, including costs of our attorneys and experts in the arbitration or payments to Fagen or others as a result of the arbitration or otherwise. Additionally, we may incur additional expense because of modifications to our plant to achieve compliance with the air emissions warranties, to achieve compliance with the more stringent minor source emissions limits, or to qualify our facility as a major emissions source. We also may experience increased costs of operations, even if our plant is modified to comply with the air emissions warranty. Our ongoing attempts bring our plant into compliance with the warranties relating to air emissions have had and may have in the future a material adverse effect on our business, financial condition and results of operations.

Our business is highly dependent on commodity prices, which are subject to significant volatility and uncertainty, so our results could fluctuate significantly.

We generally do not have long-term, fixed price contracts for the purchase of corn, our principal input, or for the sale of ethanol, our principal product. Therefore, our results of operations, financial position and business outlook are substantially dependent on commodity prices, especially prices for corn, ethanol and unleaded gasoline. Prices for these commodities are generally subject to significant volatility and uncertainty. As a result, our future financial results may fluctuate substantially.

In addition, we may experience periods of declining prices for our ethanol and increasing costs for our raw materials, which could result in operating losses. We may attempt to offset a portion of the effects of such fluctuations by entering into forward contracts to supply ethanol or to purchase corn, or by engaging in transactions involving options and futures contracts. These activities involve substantial cost and substantial risk, and ultimately may be ineffective in mitigating the fluctuations in corn and ethanol prices.

Corn prices will fluctuate and could increase significantly, which will increase our operating costs and could adversely affect our operating results because we generally cannot pass on increases in corn prices to our customers.

Corn is the principal raw material we use to produce ethanol and distillers' grains. At certain levels, corn prices would make ethanol uneconomical to use in fuel markets. The price of corn is influenced by weather conditions (including droughts) and other factors affecting crop yields, farmers' planting decisions and general economic, market and regulatory factors, including governmental policies and subsidies with respect to agriculture and international trade, and global and local supply and demand. In particular, increasing domestic ethanol capacity could boost demand for corn and result in increased corn prices. Any decline in the corn harvest, caused by farmers' planting decisions or otherwise, could cause corn prices to increase and negatively impact our gross margins. The price of corn has fluctuated significantly in the past and may fluctuate significantly in the future. Generally, we are unable to pass along increased corn costs to our customers, and accordingly, rising corn prices will tend to produce lower profit margins.

Fluctuations in the selling price and production cost of gasoline may reduce our profit margins.

Ethanol is marketed both as a fuel additive to reduce vehicle emissions from gasoline and as an octane enhancer to improve the octane rating of gasoline with which it is blended. As a result, ethanol prices are influenced by the supply and demand for gasoline and our business, future results of operations and financial condition may be materially adversely affected if gasoline demand or prices decrease.

The price of distillers' grains is affected by the price of other commodity products, such as soybeans, and decreases in the price of these commodities could decrease the price of distillers' grains.

Distillers' grains compete with other protein-based animal feed products. The price of distillers' grains may decrease when the price of competing feed products decrease. The prices of competing animal feed products are based in part on the prices of the commodities from which they are derived. Downward pressure on commodity prices, such as soybeans, will generally cause the price of competing animal feed products to decline, resulting in downward pressure on the price of distillers' grains. The price of distillers' grains is not tied to production costs. However, decreases in the price of distillers' grains would result in less revenue from the sale of distillers' grains and could result in lower profit margins.

As more ethanol plants are built, ethanol production will increase and, if demand does not sufficiently increase, the price of ethanol and distillers' grains may decrease.

According to the RFA, domestic ethanol production capacity has increased steadily from 1.5 billion gallons per year in 1999 to 13.0 billion gallons per year in 2009. However, demand for ethanol may not increase as quickly as expected or to a level that exceeds supply, or at all. Recently, several ethanol companies have announced the postponement of ethanol plants under construction due, in part, to concerns about excess production capacity in the ethanol industry and its impact on ethanol prices.

Excess ethanol production capacity also may result from decreases in the demand for ethanol or increased imported supply, which could result from a number of factors, including regulatory developments and reduced gasoline consumption in the U.S. Reduced gasoline consumption could occur as a result of increased prices for gasoline or crude oil, which could cause businesses and consumers to reduce driving or acquire vehicles with more favorable gasoline mileage, or as a result of technological advances, such as the commercialization of engines utilizing hydrogen fuel-cells, which could supplant gasoline-powered engines. There are a number of governmental initiatives designed to reduce gasoline consumption, including tax credits for hybrid vehicles and consumer education programs.

If ethanol prices decline for any reason, including excess production capacity in the ethanol industry, our business, results of operations and financial condition may be materially and adversely affected.

In addition, because ethanol production produces distillers' grains as a co-product, increased ethanol production will also lead to increased production of distillers' grains. An increase in the supply of distillers' grains, without corresponding increases in demand, could lead to lower prices or an inability to sell our distillers' grains production. A decline in the price of distillers' grains or the distillers' grains market generally could have a material adverse effect on our business, results of operations and financial condition.

Our operations could be adversely affected by infrastructure disruptions and the price of our ethanol could be depressed by lack of adequate transportation and storage infrastructure in certain areas.

We ship our ethanol to our customers primarily by the railroad adjacent to our site. We also have the potential to receive inbound corn via the railroad, although we currently receive corn by truck from our facilities in Lakefield, Minnesota and Wilder, Minnesota, each of which is less than 15 miles away from our plant. Our customers require appropriate transportation and storage capacity to take delivery of the products we produce. Therefore, our business is dependent on the continuing availability of rail, highway and related infrastructure. Any disruptions in this infrastructure network, whether caused by labor difficulties, earthquakes, storms, other natural disasters, human error or malfeasance or other reasons, could have a material adverse effect on our business. We rely upon third-parties to maintain the rail lines from our plant to the national rail network, and any failure on their part to maintain the lines could impede our delivery of products, impose additional costs on us and could have a material adverse effect on our business, results of operations and financial condition.

In addition, lack of this infrastructure prevents the use of ethanol in certain areas where there might otherwise be demand and results in excess ethanol supply in areas with more established ethanol infrastructure, depressing ethanol prices in those areas. In order for the ethanol industry to grow and expand into additional markets and for our ethanol to be sold in these new markets, there must be substantial development of infrastructure including:

- additional rail capacity;

- additional storage facilities for ethanol;
- increases in truck fleets capable of transporting ethanol within localized markets;
- expansion of refining and blending facilities to handle ethanol; and
- growth in service stations equipped to handle ethanol fuels.

The substantial investments that will be required for these infrastructure changes and expansions may not be made on a timely basis, if at all, and decisions regarding these infrastructure improvements are outside of our control. Significant delay or failure to improve the infrastructure that facilitates the distribution could curtail more widespread ethanol demand or reduce prices for our products in certain areas, which would have a material adverse effect on our business, results of operations or financial condition.

We face intense competition from competing ethanol producers.

Competition in the ethanol industry is intense. We face formidable competition in every aspect of our business from established producers of ethanol, including Archer Daniels Midland Company, Cargill, Inc., Valero Energy Corporation, and from other companies that are seeking to develop large-scale ethanol plants and alliances. According to the RFA, the top ten producers accounted for approximately 20% of the ethanol production capacity in the U.S. in 2009. Some of our competitors are divisions of substantially larger enterprises and have substantially greater financial, operational, procurement, marketing, distribution and technical resources than we have. Additionally, smaller competitors, such as farmer-owned cooperatives and independent companies owned by farmers and investors, have been able to compete successfully in the ethanol industry. Some of these competitors have business advantages, such as the ability to more favorably procure corn by operating smaller plants that may not affect the local price of corn as much as a larger-scale plant like ours or requiring their farmer-owners to sell them corn as a requirement of ownership. A significant portion of production capacity in our industry consists of smaller-sized plants. We expect competition to increase, both from large and small competitors, as the ethanol industry becomes more widely known and demand for ethanol increases.

We also face increasing competition from international suppliers. Although there is a tariff on foreign-produced ethanol (which is scheduled to expire in 2010) that is roughly equivalent to the federal ethanol tax incentive, ethanol imports equivalent to up to 7.0% of total domestic production from certain countries are exempted from this tariff under the Caribbean Basin Initiative to spur economic development in Central America and the Caribbean. Currently, international suppliers produce ethanol primarily from sugar cane, which is a significantly more efficient raw material from which to produce ethanol than corn, and have cost structures that can be substantially lower than ours.

Competing ethanol producers may also introduce competitive pricing pressures that may adversely affect our sales levels and margins or our ability to procure corn at favorable prices. As a result, we cannot assure you that we will be able to compete successfully with existing or new competitors.

We have a limited operating history and a history of losses, and our business may not be successful.

We were organized as a Minnesota limited liability company in April 2001 and did not begin producing ethanol until September 21, 2007. In October 2007, we began recording revenues from our ethanol production activity. Accordingly, we have a limited operating history from which to evaluate our business and prospects. Despite net income of approximately $8.6 million in fiscal year 2008, we have incurred a net loss for fiscal year 2007 of $5.4 million and a net loss for fiscal year 2009 of $11.3 million.

Our prospects must be considered in light of the risks and uncertainties encountered by an early-stage company and in a rapidly evolving market, such as the ethanol market, where supply and demand may change significantly in a short period of time. In addition, most of our governors and executive officers have no expertise in the ethanol industry or governing and operating a public company. While our governors and executive officers are experienced in business generally, their lack of experience in the ethanol industry and managing a public company may present additional risks to our business.

Some of the risks and uncertainties we may encounter relate to our potential inability to:

- effectively manage our business and operations, in particular the pricing risks inherent in the sale of ethanol and purchase of corn;
- comply with federal and state environmental laws and regulations;
- recruit and retain key personnel;

- comply with our obligations as a public reporting company while maintaining a low-cost structure; and
- address the other risks described throughout this annual report on Form 10-K.

If we cannot successfully address these risks, our business, future results of operations and financial condition may be materially adversely affected.

Certain provisions of our master loan agreement with AgStar present special risks to our business.

As of October 31, 2009, our debt with AgStar consists of approximately $40.8 million in fixed rate obligations and $18.7 million in variable rate obligations after giving effect to our election under our master loan agreement with AgStar to fix an interest rate of 6.58% on $45.0 million of our debt effective May 1, 2008 through April 30, 2011. The variable rate on a portion of our debt may make us vulnerable to increases in prevailing interest rates. If the interest rate on our variable rate debt were to increase, our aggregate annualized interest and principal payments would also increase and could increase significantly.

The principal and interest payments on our $53.4 million term loan are calculated using an amortization period of ten years even though the note will mature on October 1, 2012, five years from the date of its issuance. As a result, at maturity of the term loan, there would be approximately $38.9 million in principal remaining under the term loan, without any additional payments that may be required under the master loan agreement. In order to finance this large payment of principal that would be due at maturity, we may attempt to extend the term of the loan under the master loan agreement, refinance the indebtedness under the master loan agreement, in full or in part, or obtain a new loan to repay the term loan. We cannot assure you that will be successful in obtaining an extension of or refinancing our indebtedness. We also cannot assure you that we will be able to obtain a new loan in an amount that is sufficient for our needs, in a timely manner or on terms and conditions acceptable to us or our members.

We also have a $4.0 million revolving term loan. As of October 31, 2009, we have used approximately $1.1 million of AgStar's commitment under this loan. The loan will mature on October 1, 2012. As with the term loan, at maturity we may attempt to extend, refinance, or obtain a new loan to repay any outstanding balance. We cannot assure you that any alternative will be sufficient for our needs, available in a timely manner or on terms and conditions acceptable to us or our members. We cannot draw on the unused portion of this debt as long as we are not in compliance with the covenants of our master loan agreement.

If we are unable to service our debt, we may lose control of our business and be forced to reduce or delay planned capital expenditures, sell assets, restructure our indebtedness or submit to foreclosure proceedings, all of which would result in a material adverse effect upon our business.

We engage in hedging transactions which involve risks that can harm our business.

In an attempt to offset some of the effects of volatility of ethanol prices and corn costs, we may enter into cash fixed-price contracts to sell a portion of our ethanol and distillers' grains production or purchase a portion of our corn requirements. We may use exchange-traded futures contracts and options to manage commodity risk. The impact of these activities depends upon, among other things, the prices involved and our ability to sell sufficient products to use all of the corn for which we have futures contracts. Hedging arrangements also expose us to the risk of financial loss in situations where the other party to the hedging contract defaults on its contract or, in the case of exchange-traded contracts, where there is a change in the expected differential between the underlying price in the hedging agreement and the actual prices paid or received by us. Hedging activities can themselves result in losses when a position is purchased in a declining market or a position is sold in a rising market. A hedge position is often settled in the same time frame as the physical commodity is either purchased (corn) or sold (ethanol). We may experience hedging losses in the future. We also vary the amount of hedging or other price mitigation strategies we undertake, and we may choose not to engage in hedging transactions at all. As a result, whether or not we engage in hedging transactions, our business, results of operations and financial condition may be materially adversely affected by increases in the price of corn or decreases in the price of ethanol.

Operational difficulties at our plant could negatively impact our sales volumes and could cause us to incur substantial losses.

Our operations are subject to labor disruptions, unscheduled downtime and other operational hazards inherent in our industry, such as equipment failures, fires, explosions, abnormal pressures, blowouts, pipeline ruptures, transportation accidents and natural disasters. Some of these operational hazards may cause personal injury or loss of life, severe damage to or destruction of property and equipment or environmental damage, and may result in suspension of operations and the imposition of civil or criminal penalties. Our insurance may not be adequate to fully cover the potential operational hazards described above or we may not be able to renew this insurance on commercially reasonable terms or at all. Furthermore, we may have difficulty managing the necessary process maintenance required to maintain our nameplate production capacity of 50 mgy. If our ethanol plant does not produce ethanol and distillers' grains at the levels we expect, our business, results of operations, and financial condition may be materially adversely affected.

Competition for qualified personnel in the ethanol industry is intense and we may not be able to hire and retain qualified personnel to operate our ethanol plant.

Our success depends in part on our ability to attract and retain competent personnel. For our ethanol plant, we must hire qualified managers, operations personnel, accounting staff and others, which can be challenging in a rural community. Competition for employees in the ethanol industry is intense, and we may not be able to attract and retain qualified personnel. If we are unable to hire productive and competent personnel and retain our existing personnel, our business may be adversely affected and we may not be able to efficiently operate our ethanol business and comply with our other obligations.

Technology in our industry evolves rapidly, potentially causing our plant to become obsolete, and we must continue to enhance the technology of our plant or our business may suffer.

We expect that technological advances in the processes and procedures for processing ethanol will continue to occur. It is possible that those advances could make the processes and procedures that we utilize at our ethanol plant less efficient or obsolete. These advances could also allow our competitors to produce ethanol at a lower cost than we are able. If we are unable to adopt or incorporate technological advances, our ethanol production methods and processes could be less efficient than those of our competitors, which could cause our ethanol plant to become uncompetitive.

Ethanol production methods are constantly advancing. The current trend in ethanol production research is to develop an efficient method of producing ethanol from cellulose-based biomass such as agricultural waste, forest residue and municipal solid waste. This trend is driven by the fact that cellulose-based biomass is generally cheaper than corn and producing ethanol from cellulose-based biomass would create opportunities to produce ethanol in areas that are unable to grow corn. Another trend in ethanol production research is to produce ethanol through a chemical or thermal process, rather than a fermentation process, thereby significantly increasing the ethanol yield per pound of feedstock. Although current technology does not allow these production methods to be financially competitive, new technologies may develop that would allow these methods to become viable means of ethanol production in the future. If we are unable to adopt or incorporate these advances into our operations, our cost of producing ethanol could be significantly higher than those of our competitors, which could make our ethanol plant obsolete. Modifying our plant to use the new inputs and technologies would likely require material investment.

If ethanol fails to compete successfully with other existing or newly-developed oxygenates or renewable fuels, our business will suffer.

Alternative fuels, additives and oxygenates are continually under development. Alternative fuels and fuel additives that can replace ethanol are currently under development, which may decrease the demand for ethanol. Technological advances in engine and exhaust system design and performance could reduce the use of oxygenates, which would lower the demand for ethanol, and our business, results of operations and financial condition may be materially adversely affected.

Our level of indebtedness may adversely affect our ability to react to changes in our business, and we may be limited in our ability to refinance our existing debt or use debt to fund future capital needs.

We have a substantial amount of indebtedness. Because of our substantial debt, demands on our cash resources are higher than they otherwise would be which could negatively impact our business, results of operations and financial condition. As a result of our substantial indebtedness, we may be more vulnerable to general adverse economic and industry conditions. We may find it more difficult to obtain additional financing to fund future working capital, capital expenditures and other general operating requirements. We will be required to dedicate a substantial portion of our cash flow from operations to the payment of principal and interest on our debt, reducing the available cash flow to manage our corn and ethanol price risk, fund operations or make capital expenditures. We may have a competitive disadvantage relative to other companies in our industry with less debt. We may also experience decreases in our regular trade credit from vendors, which could adversely impact our cash flow if we need to start prepaying for items we have been able to purchase on trade credit in the past. In early 2007, a crisis began in the subprime mortgage sector, as a result of rising delinquencies and credit quality deterioration, and has subsequently spread throughout the credit market. There can be no assurances that this credit crisis will not worsen or impact our availability and cost of debt financing including with respect to any refinancings.

The EPA imposed E10 "blend wall" if not overcome will have an adverse affect on demand for ethanol.

We believe that the E10 "blend wall" is one of the most critical governmental policies currently facing the ethanol industry. The "blend wall" issue arises because of several conflicting requirements. First, the renewable fuels standards dictate a continuing increase in the amount of ethanol blended into the national gasoline supply. Second, the Environmental Protection Agency (EPA) mandates a limit of 10% ethanol inclusion in non-flex fuel vehicles, and the E85 vehicle marketplace is struggling to grow due to lacking infrastructure. Total gasoline usage by the U.S. is currently around 138 billion gallons, and is expected to decrease to less than 130 billion gallons over the next 5 years as fuel mileage standards are changed. The RFS dictates an increasing amount of ethanol blending: 13.95 billion gallons in 2011, 15.2 billion gallons in 2012, and increasing to 36 billion gallons by 2022. To reach the standard as dictated by the RFS in 2011, assuming 135 billion gallons of total gasoline usage nationally, each gallon of gasoline sold would have to be blended with greater than 10% ethanol. The EPA policy of 10% and the RFS increasing blend rate are at odds, which is sometimes referred to as the "blend wall." One industry group has petitioned the EPA for a waiver of the E10 law and an increase to E15. The EPA has currently postponed the expected December 2009 decision. This issue is a major risk to the ethanol industry.

We are subject to financial reporting and other requirements for which our accounting, internal audit and other management systems and resources may not be adequately prepared.

We are subject to reporting and other obligations under the Securities Exchange Act of 1934, as amended, or the Exchange Act. Only one of our governors and our interim chief financial officer has served as such with a company that is required to file reports under the Exchange Act. These reporting and other obligations will place significant demands on our management, administrative, operational, and accounting resources. As a result, we may not be able or qualified to efficiently manage our financial accounting and preparation of the Exchange Act reports. If we are unable to manage our financial accounting and prepare our Exchange Act reports, we may be exposed to significant liabilities and have difficulty raising additional capital.

Our failure to achieve and maintain effective internal controls over financial reporting may have a material effect on our business.

We are in the process of upgrading our systems, implementing additional financial and management controls, and reporting systems and procedures. We are currently preparing for compliance with the reporting requirement of Section 404 of the Sarbanes-Oxley Act of 2002. This effort, under the direction of senior management, includes documentation, and testing of our controls and business processes. We are currently in the process of formalizing an internal control audit plan that includes performing a risk assessment, establishing a reporting methodology and testing internal controls and procedures over financial reporting. Some of these efforts to prepare for the reporting requirement have resulted in changes to our internal control over financial reporting.

However, there has been no change in our internal control over financial reporting (as defined in Rule 13a-15(f) under the Exchange Act) that occurred in the fiscal year ended October 31, 2009 that has materially affected, or is reasonably likely to materially affect, our internal control over financial reporting.

Certain of our members exert significant influence over us. Their interests may not coincide with ours or the interests of our unitholders, and they may make decisions with which we or our unitholders may disagree.

As of January 1, 2010, Project Viking, LLC beneficially owned 21.8% of our outstanding units. Project Viking is owned by Roland J. (Ron) Fagen and Diane Fagen, the principal shareholders of Fagen, Inc., our design-build firm. Project Viking, together with our executive officers and governors, together control approximately 25.8% of our outstanding units as of January 1, 2010. As a result, these unitholders, acting individually or together, could significantly influence our management and affairs and all matters requiring member approval, including the election of governors and approval of significant corporate transactions. This concentration of ownership may also have the effect of delaying or preventing a change in control of our company and might affect the market price of our units.

The interests of these members may not coincide with our interests or the interests of our other members. For example, Fagen, Inc. has invested and may continue to invest in a number of other ethanol producers, some of whom may compete with us. Additionally, in September 2005, we entered into a design-build agreement with Fagen, Inc. for the construction of our plant. In September 2009, we commenced an arbitration action against Fagen, Inc. relating to its design-build agreement with us. Please see Part I, Item 3 "Legal Proceedings" of this Form 10-K for a description of this arbitration action. This dispute is another instance in which our interests and those of Project Viking and the Fagen affiliates are not aligned.

As a result of these and other potential conflicting interests, these existing members may make decisions with respect to us with which we or our members may disagree.

Because we are primarily dependent upon one product, our business is not diversified, and we may not be able to adapt to changing market conditions or endure any decline in the ethanol industry.

Our success depends on our ability to efficiently produce and sell ethanol, and, to a lesser extent, distillers' grains. We do not have any other lines of business or other significant sources of revenue to rely upon if we are unable to produce and sell ethanol and distillers' grains, or if the market for those products decline. Our lack of diversification means that we may not be able to adapt to changing market conditions, changes in regulation, increased competition or any significant decline in the ethanol industry.

Our sales will decline, and our business will be materially harmed if our third party marketers do not effectively market or sell the ethanol and distillers grains we produce or if there is a significant reduction or delay in orders from our marketers.

We have entered into an agreement with a third party to market our supply of ethanol. We have also entered into an agreement with another third party to market our supply of distillers grains. Our marketers are independent businesses that we do not control. We cannot be certain that these marketers will market or sell our ethanol and distillers' grains effectively. Our agreements with these marketers do not contain requirements that a certain percentage of such parties' sales are of our products, nor do the agreements restrict their ability to choose alternative sources for ethanol or distillers grains.

Our success in achieving revenue from the sale of ethanol and distillers grains will depend upon the continued viability and financial stability of our marketers. These marketers may choose to devote their efforts to other ethanol producers or reduce or fail to devote the necessary resources to provide effective sales and marketing support of our products. We believe that our financial success will continue to depend in large part upon the success of our marketers in operating their businesses. If these marketers do not effectively market and sell our ethanol and distillers grains, our revenues may decrease and our business will be harmed.

Our business is subject to extensive occupational safety and health regulations that could increase our operating costs.

We are subject to various occupational safety and health regulations, and we have incurred expense in training employees in occupational safety compliance. We will continue to be subject to such safety and health regulations and will continue to incur expense with respect to training and compliance. We do not expect that compliance with these rules and regulations will have a material impact on our business or as to our competitive stance in the industry, as these rules apply to other ethanol plants as well. However, any increase in OSHA compliance costs could negatively affect our profitability.

Approval of a Low Carbon Fuel Standard ("LCFS") by the California Air Resources Board ("CARB") may have a negative impact on our ability to market our ethanol in California.

The CARB recently proposed rules to implement a LCFS, which would set standards for the carbon intensity of fuels used in the State of California starting in 2011. While the proposed rules are still subject to rulemaking process in California, certain provisions of the proposed LCFS rules have the potential to ban ethanol produced at our plant from being sold in California. While we believe there may be some negative impact to our sales from the approval of the LCFS in California, we believe we will still be able to market all the ethanol produced by our plant. However, if additional states where our ethanol is marketed, or the federal government, adopt similar provisions it could have a severe negative impact on our ability to sell all of the ethanol produced at our plant.

Risks Related to the Units

There is no public market for our units and no public market is expected to develop.

There is no established public trading market for our units, and we do not expect one to develop in the foreseeable future. To maintain our partnership tax status, we do not intend to list the units on any stock exchange or automatic quotation system such as OTC Bulletin Board. As a result, units held by our members may not be easily resold and members may be required to hold their units indefinitely. Even if members are able to resell our units, the price may be less than the members' investment in the units or may otherwise be unattractive to the member.

There are significant restrictions on the transfer of our units.

To protect our status as a partnership for tax purposes and to assure that no public trading market in our units develops, our units are subject to significant restrictions on transfer and transfers are subject to approval by our board of governors. All transfers of units must comply with the transfer provisions of our Member Control Agreement and the unit transfer policy adopted by our board of governors. Our board of governors will not approve transfers which could cause us to lose our tax status or violate federal or state securities laws. On November 5, 2008, our board of governors adopted a revised unit transfer policy. While the revised policy permits transfers of our units under certain circumstances, including certain transfers of units for value, there continue to be significant restrictions on transfer of our units. Among other things, the revised unit transfer policy places limits on the number of units that may be transferred during any fiscal year and requires the transferor and transferee to complete a unit transfer agreement and application form and submit these to us along with the required documents and an application fee. As a result, members may not be able to transfer their units and may be required to assume the risks of the investment for an indefinite period of time.

A transferee may be admitted as a member only upon approval by the board of governors and upon satisfaction of certain other requirements, including the transferee meeting the minimum unit ownership requirements to become a member (which for our present units requires holding a minimum of 2,500 units). Any transferee that is not admitted as a member will be deemed an unadmitted assignee. An unadmitted assignee will be a non-member unit holder and will have the same financial rights as other unit holders, such as the right to receive distributions that we declare or that are available upon our dissolution or liquidation. As a non-member unit holder, an unadmitted assignee will not have the voting or other governance rights of members and will not be entitled to any information or accountings regarding our business or to inspect our books and records.

There is no assurance that we will be able to make distributions to our unit holders, which means that holders could receive little or no return on their investment.

Distributions of our net cash flow may be made at the sole discretion of our board of governors, subject to the provisions of the Minnesota Limited Liability Company Act, our Member Control Agreement and restrictions imposed by our creditors. There is no assurance that we will generate any distributable cash from operations. Although our intention is to make cash distributions sufficient to discharge our members' anticipated tax liabilities arising from any taxable income generated, our board may elect to retain cash for operating purposes, debt retirement, plant improvements or expansion. Consequently, members may receive little or no return on their investment in the units.

We may authorize and issue units of new classes which could be superior to or adversely affect holders of our outstanding units.

Our board of governors, upon the approval of a majority in interest of our members, has the power to authorize and issue units of classes which have voting powers, designations, preferences, limitations and special rights, including preferred distribution rights, conversion rights, redemption rights and liquidation rights, different from or superior to those of our present units. New units may be issued at a price and on terms determined by our board of governors. The terms of the units and the terms of issuance of the units could have an adverse impact on your voting rights and could dilute your financial interest in us.

Our use of a staggered board of governors and allocation of governor appointment rights may reduce the ability of investors to affect the composition of the board.

We are managed by a board of governors, currently consisting of eight elected governors and two appointed governors. The seats on the board that are not subject to a right of appointment will be elected by the other members. The initial board designated from among themselves three classes of governors. The terms of the three classes of governors is staggered such that, beginning in 2008, our members will elect one-third (or as nearly as possible) of the non-appointed members of the board of governors annually. An appointed governor serves indefinitely at the pleasure of the member appointing him or her (so long as such member and its affiliates continue to hold a sufficient number of units to maintain the applicable appointment right) until a successor is appointed, or until the earlier death, resignation or removal of the appointed governor.

The effect of these provisions may make it more difficult for a third party to acquire, or may discourage a third party from acquiring, control of us and may discourage attempts to change our management, even if an acquisition or these changes would be beneficial to our members.

Our units represent both financial and governance rights, and loss of status as a member would result in the loss of the holder's voting and other rights and would allow us to redeem such holder's units.

Holders of units are entitled to certain financial rights, such as the right to any distributions, and to governance rights, such as the right to vote as a member. If a unit holder does not continue to qualify as a member or such holder's member status is terminated, the holder would lose certain rights, such as voting rights, and we could redeem such holder's units. The minimum number of units presently required for membership is 2,500 units. In addition, holders of units may be terminated as a member if the holder dies or ceases to exist, violates our Member Control Agreement or takes actions contrary to our interests, and for other reasons. Although our Member Control Agreement does not define what actions might be contrary to our interests, and our board of governors has not adopted a policy on the subject, such actions might include providing confidential information about us to a competitor, taking a board or management position with a competitor or taking action which results in significant financial harm to us in the marketplace. If a holder of units is terminated as a member, our board of governors will have no obligation to redeem such holder's units.

Voting rights of members are not necessarily equal and are subject to certain limitations.

Members of our company are holders of units who have been admitted as members upon their investment in our units and who are admitted as members by our board of governors. The minimum number of units required to retain membership is 2,500 units. Any holder of units who is not a member will not have voting rights. Transferees of units must be approved by our board of governors to become members. Members who are holders of our present units are entitled to one vote for each unit held. The provisions of our Member Control Agreement relating to voting rights applicable to any class of units will apply equally to all units of that class. However, our Member Control Agreement gives members who hold significant amounts of equity in us the right to designate governors to serve on our board of governors. For every 9% of our units held, the member has the right to appoint one person to our board. Project Viking, LLC has the right to appoint two persons to our board pursuant to this provision. If units of any other class are issued in the future, holders of units of that other class will have the voting rights that are established for that class by our board of governors with the approval of our members. Consequently, the voting rights of members may not be completely proportional to the number of units held. Cumulative voting for governors is not allowed, which makes it substantially less likely that a minority of members could elect a member to the board of governors. Members do not have dissenter's rights. This means that they will not have the right to dissent and seek payment for their units in the event we merge, consolidate, exchange or otherwise dispose of all or substantially all of our property. Holders of units who are not members have no voting rights. These provisions may limit the ability of members to change the governance and policies of our company.

All members will be bound by actions taken by members holding a majority of our units, and because of the restrictions on transfer and lack of dissenters' rights, members could be forced to hold a substantially changed investment.

We cannot engage in certain transactions, such as a merger, consolidation, dissolution or sale of all or substantially all of our assets, without the approval of our members. However, if holders of a majority of our units approve a transaction, then all members will also be bound to that transaction regardless of whether that member agrees with or voted in favor of the transaction. Under our Member Control Agreement, members will not have any dissenters' rights to seek appraisal or payment of the fair value of their units. Consequently, because there is no public market for the units, members may be forced to hold a substantially changed investment.

Government and Regulatory Risks

Federal and state regulation heavily influence the ethanol industry and changes in government regulation that adversely affect the demand for or supply of ethanol will have a material adverse effect on our business.

Various federal and state laws, regulations and programs impact the supply of and demand for ethanol. Some government regulation, for example those that provide economic incentives to ethanol producers, stimulate supply of ethanol by encouraging production and the increased capacity of ethanol plants. Others, such as a federal excise tax incentive program that provides gasoline distributors who blended ethanol with gasoline to receive a federal excise tax rate reduction for each blended gallon they sell, stimulate demand for ethanol by making it price competitive with other oxygenates. Further, tariffs generally apply to the import of ethanol from certain other countries, where the cost of production can be significantly less than in the U.S. These tariffs are designed to increase the cost of imported ethanol to a level more comparable to the cost of domestic ethanol by offsetting the benefit of the federal excise tax program. Tariffs have the effect of maintaining demand for domestic ethanol. Additionally, the federal government has established renewable fuels standard (RFS) programs, most recently under the Energy Independence and Security Act of 2007, which set minimum national standards for use of renewable fuels. The RFS and other state programs that require or provide incentives for the use of ethanol create demand for ethanol. Government regulation and government programs that create demand for ethanol may also indirectly create supply for ethanol as additional producers expand or new companies enter the ethanol industry to capitalize on demand.

Federal and state laws, regulations and programs are constantly changing. We cannot predict what material impact, if any, these changes might have on our business. Future changes in regulations and programs could impose more stringent operational requirements or could reduce or eliminate the benefits we receive, directly and indirectly, under current regulations and programs. Future changes in regulations and programs may increase or add benefits to ethanol producers other than us or eliminate or reduce tariffs or other barriers to entry into the U.S. ethanol market, any of which could prove beneficial to our competitors, both domestic and international. Future changes in regulation may also hurt our business by providing economic incentives to producers of other renewable fuels or oxygenates or encouraging use of fuels or oxygenates that compete with ethanol. In addition, both national and state regulation is influenced by public opinion and changes in public opinion. For example, certain states oppose the use of ethanol because, as net importers of ethanol from other states, the use of ethanol could increase gasoline prices in that state and because that state does not receive significant economic benefits from the ethanol industry, which are primarily experienced by corn and ethanol producing states. Further, some argue that the use of ethanol will have a negative impact on gasoline prices to consumers, result in rising food prices, add to air pollution, harm car and truck engines, and actually use more fossil energy, such as oil and natural gas, than the amount of ethanol that is produced. We cannot predict the impact that opinions of consumers, legislators, industry participants, or competitors may have on the regulations and programs currently benefiting ethanol producers.

We may be adversely affected by environmental laws, regulations and liabilities.

We are subject to various federal, state and local environmental laws and regulations, including those relating to the discharge of materials into the air, water and ground.

Some of these laws and regulations require our plant to operate under permits that are subject to renewal or modification. These laws, regulations and permits may require pollution control equipment or operational changes to limit actual or potential impacts to the environment.

The costs associated with obtaining and complying with permits and complying with environmental laws have increased our costs of construction and production. In particular, we have incurred additional costs relating to an air-emission permit from the Minnesota Pollution Control Agency ("MPCA"). We applied for a synthetic minor air-emissions source permit in July 2004 that was granted by the MPCA in May 2005. In June 2005, a coalition of two environmental and one energy group challenged the grant of this air emissions permit by an appeal to the Minnesota Court of Appeals and in July 2006, the Minnesota Court of Appeals affirmed the MPCA's issuance of the permit. In conjunction with the permit and the permit dispute and to prevent further appeals by the coalition, we entered into a compliance agreement with the MPCA on January 23, 2007 that currently governs the air emissions from our plant. Under the compliance agreement, we also agreed to submit an amendment to our air permit to qualify our facility as a "major emissions source". Accordingly, we submitted a major amendment to our existing air-emissions permit in December 2008, and, following air pollution control device testing, we submitted a second major amendment in September 2009, both seeking amendments to our air permit, including amendments to permit conditions and adjustments to other components of plant operations and production. However, we are continuing discussions with the MPCA regarding the necessity for qualifying our facility as a major emissions source, particularly in light of changes in federal law that increased the limit of certain emissions allowed as a synthetic minor source. On March 13, 2008, MPCA issued a notice of violation to us for violations of certain rules, statutes, and permit conditions (as modified by the compliance agreement), including emission violations and reporting violations. As part of our continuing discussions with MPCA, we are seeking to resolve these violations by agreement with MPCA. Such resolution may result in the payment of a civil penalty or other sanctions and remedies available to MPCA. Pending the resolution of this air permit issue, we continue to operate subject to the compliance agreement.

In September 2009, we commenced an arbitration action against Fagen, Inc. relating to its design-build agreement with us and in particular, the failure of our ethanol plant to comply with air emissions guarantees and warranties. Please see Part I, Item 3 "Legal Proceedings" of this Form 10-K for a description of this arbitration action.

There can be no assurance that we will be able to comply with any of the conditions of the compliance agreement, any of our other permits, or with environmental laws applicable to us. Compliance with these laws and permits could require expensive pollution control equipment or operational changes to limit actual or potential impacts to the environment, as well as significant management time and expense. However, if the requested air permit modification is granted without change by the MPCA, it will substantially increase our ability to operate consistently at or below limitations as a synthetic minor source. The resolution of our air emissions permit issue will likely involve significant management time and expense and may involve ongoing operational expense or further modifications to the design or equipment in our plant. There can be no assurance that we will succeed in our discussions with the MPCA to qualify our ethanol plant as a minor emissions source. A violation of environmental laws, regulations or permit conditions can result in substantial fines, natural resource damage, criminal sanctions, permit revocations or plant shutdown, any of which could have a material adverse effect on our operations.

Federal and state regulations affecting the operation of our ethanol plant are subject to future change. We cannot predict what material impact, if any, these changes might have on our business. Future changes in regulations or enforcement policies could impose more stringent requirements on us, compliance with which could require additional capital expenditures, increase our operating costs or otherwise adversely affect our business. These changes may also relax requirements that could prove beneficial to our competitors and thus adversely affect our business. In addition, regulations of the EPA and the MCPA depend heavily on administrative interpretations. We cannot assure you that future interpretations made by the EPA, or other regulatory authorities, with possible retroactive effect, will not adversely affect our business, financial condition and results of operations.

We also plan to evaluate the effectiveness of the current emissions monitoring system in preparation for possible green house gas emissions regulatory changes. Being able to monitor emissions more effectively could lead to further reductions in emissions which would lead to lower fees. Reductions in emissions can make us a better environmental company. By attempting to adjust to possible upcoming regulatory changes, we hope to be better positioned to take advantage of the changes from the beginning. We believe that all companies will be faced with higher fees for future emissions based on recent federal legislative proposals.

Failure to comply with existing or future regulatory requirements could have a material adverse effect on our business, financial condition and results of operations.

Risks Related to Tax Issues in a Limited Liability Company

EACH UNIT HOLDER SHOULD CONSULT THE INVESTOR'S OWN TAX ADVISOR WITH RESPECT TO THE FEDERAL AND STATE TAX CONSEQUENCES OF AN INVESTMENT IN HERON LAKE BIOENERGY, LLC AND ITS IMPACT ON THE INVESTOR'S TAX REPORTING OBLIGATIONS AND LIABILITY.

If we are not taxed as a partnership, we will pay taxes on all of our net income and you will be taxed on any earnings we distribute, and this will reduce the amount of cash available for distributions to holders of our units.

We consider Heron Lake BioEnergy, LLC to be a partnership for federal income tax purposes. This means that we will not pay any federal income tax, and our members will pay tax on their share of our net income. If we are unable to maintain our partnership tax treatment or qualify for partnership taxation for whatever reason, then we may be taxed as a corporation. We cannot assure you that we will be able to maintain our partnership tax classification. For example, there might be changes in the law or our company that would cause us to be reclassified as a corporation. As a corporation, we would be taxed on our taxable income at rates of up to 38% for federal income tax purposes. Further, distributions would be treated as ordinary dividend income to our unit holders to the extent of our earnings and profits. These distributions would not be deductible by us, thus resulting in double taxation of our earnings and profits. This would also reduce the amount of cash we may have available for distributions.

Your tax liability from your allocated share of our taxable income may exceed any cash distributions you receive, which means that you may have to satisfy this tax liability with your personal funds.

As a partnership for federal income tax purposes, all of our profits and losses "pass-through" to our unit holders. You must pay tax on your allocated share of our taxable income every year. You may incur tax liabilities from allocations of taxable income for a particular year or in the aggregate that exceed any cash distributions you receive in that year or in the aggregate. This may occur because of various factors, including but not limited to, accounting methodology, the specific tax rates you face, and payment obligations and other debt covenants that restrict our ability to pay cash distributions. If this occurs, you may have to pay income tax on your allocated share of our taxable income with your own personal funds.

You may not be able to fully deduct your share of our losses or your interest expense.

It is likely that your interest in us will be treated as a "passive activity" for federal income tax purposes. In the case of unit holders who are individuals or personal services corporations, this means that a unit holder's share of any loss incurred by us will be deductible only against the holder's income or gains from other passive activities, e.g., S corporations and partnerships that conduct a business in which the holder is not a material participant. Some closely held C corporations have more favorable passive loss limitations. Passive activity losses that are disallowed in any taxable year are suspended and may be carried forward and used as an offset against passive activity income in future years. Upon disposition of a taxpayer's entire interest in a passive activity to an unrelated person in a taxable transaction, suspended losses with respect to that activity may then be deducted.

Interest paid on any borrowings incurred to purchase units may not be deductible in whole or in part because the interest must be aggregated with other items of income and loss that the unit holder has independently experienced from passive activities and subjected to limitations on passive activity losses.

You may be subject to federal alternative minimum tax

Individual taxpayers are subject to an "alternative minimum tax" if that tax exceeds the individual's regular income tax. For alternative minimum tax purposes, an individual's adjusted gross income is increased by items of tax preference. We may generate such preference items, the most significant of which is accelerated depreciation. Accordingly, preference items from our operations together with other preference items you may have may cause or increase an alternative minimum tax to a unit holder. You are encouraged and expected to consult with your individual tax advisor to analyze and determine the effect on your individual tax situation of the alternative minimum taxable income you may be allocated, particularly in the early years of our operations.

Preparation of your tax returns may be complicated and expensive.

The tax treatment of limited liability companies and the rules regarding partnership allocations are complex. We will file a partnership income tax return and will furnish each unit holder with a Schedule K-1 that sets forth our determination of that unit holder's allocable share of income, gains, losses and deductions. In addition to United States federal income taxes, unit holders will likely be subject to other taxes, such as state and local taxes, that are imposed by various jurisdictions. It is the responsibility of each unit holder to file all applicable federal, state and local tax returns and pay all applicable taxes. You may wish to engage a tax professional to assist you in preparing your tax returns and this could be costly to you.

Any audit of our tax returns resulting in adjustments could result in additional tax liability to you.

The IRS may audit our tax returns and may disagree with the positions that we take on our returns or any Schedule K-1. If any of the information on our partnership tax return or a Schedule K-1 is successfully challenged by the IRS, the character and amount of items of income, gains, losses, deductions or credits in a manner allocable to some or all our unit holders may change in a manner that adversely affects those unit holders. This could result in adjustments on unit holders' tax returns and in additional tax liabilities, penalties and interest to you. An audit of our tax returns could lead to separate audits of your personal tax returns, especially if adjustments are required.

ITEM 1B. UNRESOLVED STAFF COMMENTS

Not applicable.

ITEM 2. PROPERTIES

We own approximately 216 acres of land located near Heron Lake, Minnesota on which we have constructed our ethanol plant, which also includes corn, coal, ethanol, and distillers' grains storage and handling facilities. Located on these 216 acres is an approximately 7,320 square foot building that serves as our headquarters. Our address is 91246 390 th Avenue, Heron Lake, Minnesota 56137-3175.

We also own elevator and grain storage facilities in Lakefield, Minnesota and Wilder, Minnesota. The elevator and grain storage facilities at each location have grain handling equipment and both upright and flat storage capacity. The storage capacity of the Lakefield, Minnesota facility is approximately 1.9 million bushels and the storage capacity of the Wilder, Minnesota facility is approximately 900,000 bushels.

All of our real property is subject to mortgages in favor of AgStar as security for loan obligations.

ITEM 3. LEGAL PROCEEDINGS

On September 28, 2005, HLBE executed a Design-Build Agreement with Fagen, Inc. by which Fagen, Inc. agreed to design and build a 50 million gallon per year coal-fired ethanol plant in Heron Lake, Minnesota, for a contract price of approximately $76,000,000. The agreement contained numerous warranty and guarantee provisions as well as a liquidated damages provision. Construction began in late 2005, and after several delays the first corn grind took place on September 21, 2007. The plant, however, has not been able to meet the air emissions warranties or operate as a "synthetic minor source" as warranted and intended under the design-build agreement.

By the terms of the Design-Build Agreement, claims or controversies between HLBE and Fagen, Inc. arising out of or relating to the Design-Build Agreement, or the breach thereof, are ultimately to be decided by Arbitration in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association. On September 18, 2009 HLBE served and filed its Demand for Arbitration and Request for Mediation. A Revised Demand for Arbitration was served and filed on December 23, 2009 following an unsuccessful attempt to mediate the dispute. In these Demands for Arbitration, HLBE alleges that Fagen, Inc. breached the terms and conditions of the Design-Build Agreement including its warranties and guarantees, was negligent in its efforts to correct various performance and emissions problems, had not completed the plant on a timely basis in accordance with the Design-Build Agreement, and prior to the execution of the Agreement had made certain negligent misrepresentations with respect to coal-fired ethanol plants. In the Demand for Arbitration, HLBE seeks damages for breach of contract and breach of the warranties and guarantees, damages resulting from the negligent efforts to correct the problems, damages for the negligent misrepresentations, as well as liquidated damages for delays in the plant construction. HLBE seeks damages in the amount of $22,800,000.

Fagen, Inc. responded to the Demand for Arbitration by denying liability and asserting various affirmative defenses. In addition, Fagen, Inc. brought a Counterclaim alleging that it is entitled to payment of a retainage held by HLBE in the amount of approximately $3.8 million. In addition, Fagen, Inc. alleges that it performed additional work and provided additional labor and materials to the plant in the amount of approximately $2.2 million; it alleges that this did not constitute warranty or guarantee work and therefore it claims it is entitled to payment of this additional amount. HLBE responded to the Counterclaim by denying the allegations and asserting various affirmative defenses. On January 4, 2010, Fagen, Inc. requested to join ICM, Inc. as a party to the arbitration action, claiming that joinder was necessary for proper resolution of the claims and defenses in the arbitration action. On January 27, 2010, ICM, Inc. responded to the request, agreeing to be joined provided certain procedures are established. In its response, ICM also indicated that it intends to assert claims against us under the license agreement we entered into with ICM as part of the design build agreement with Fagen. On January 27, 2010, we filed our response and objections to Fagen's request to join ICM as a party, and requested that a special arbitrator be appointed to resolve the joinder issues. We intend to defend against the Fagen counterclaims and any claims brought by ICM, Inc. and assert our defenses vigorously.

The arbitration proceeding is in its early phase, and arbitrators have not yet been selected.

ITEM 4. ___________________ SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

ITEM 5 . MARKET FOR THE REGISTRANT'S COMMON EQUITY, RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market Information

Although matching services may be available to help match buyers and seller of our units, there is no established public trading market for the units and we do not expect one to develop in the foreseeable future. To maintain our partnership tax status, we do not intend to list the units on any stock exchange or over-the-counter securities market such as the OTC Bulletin Board.

Holders of Record

As of January 1, 2010, there were 27,104,625 Class A units outstanding and held of record by 1,098 persons. There are no other classes of units outstanding. As of January 1, 2010, there were no outstanding options or warrants to purchase, or securities convertible into, our units.

Distributions

We have never declared distributions. Our agreements with lenders currently materially limit our ability to make distributions to our members and these agreements are likely to limit materially the future payment of distributions. For a further description of these restrictions, please see "Item 7 Management's Discussion and Analysis of Financial Condition and Results of Operations" and Note 9 of the notes to our audited consolidated financial statements. In September 2007, we began operation of our ethanol plant and began generating revenue. If our financial performance and loan covenants permit, we expect to make cash distributions at times and in amounts that will permit our members to make income tax payments. If our financial performance and loan covenants further permit, we intend to make distributions in excess of those amounts. Cash distributions are not assured, however, and we may never be in a position to make distributions.

Under Minnesota law, we cannot make a distribution to a member if, after the distribution, we would not be able to pay our debts as they become due or our liabilities, excluding liabilities to our members on account of their capital contributions, would exceed our assets.

Securities Authorized for Issuance under Equity Compensation Plans

There are no "compensation plans" (including individual compensation arrangements) under which any of our equity securities are authorized for issuance.

ITEM 6. SELECTED FINANCIAL DATA

Selected Consolidated Financial Data

The following table presents selected consolidated financial and operating data as of the dates and for the periods indicated. The selected financial data for October 31, 2009, 2008 and 2007 has been derived from the audited consolidated financial statements included elsewhere in this Annual Report on Form 10-K.

This selected consolidated financial data should be read in conjunction with “Management’s Discussion and Analysis of Financial Condition and Results of Operations” within Item 7 and the consolidated financial statements and the accompanying notes included elsewhere in this Annual Report on Form 10-K. Among other things, those financial statements include more detailed information regarding the basis of presentation for the following consolidated financial data.

	Fiscal Year Ended		
	October 31, 2009	October 31, 2008	October 31, 2007
Statement of Operations Data:			
Revenues	$ 88,304,596	$ 131,070,642	$ 23,560,498
Cost of goods sold	90,857,247	114,411,541	24,313,695
Gross profit (loss)	(2,552,651)	16,659,101	(753,197)
Operating expenses	4,515,476	3,351,252	3,527,199
Operating income (loss)	(7,068,127)	13,307,849	(4,280,396)
Other income (expense)	(4,261,307)	(4,689,810)	(1,167,890)
Net income (loss)	$ (11,329,434)	$ 8,618,039	$ (5,448,286)
Weighted average units outstanding	27,104,625	27,104,625	26,361,406
Net income (loss) per unit — Basic and diluted	$ (0.42)	$ 0.32	$ (0.21)

	As of	
	October 31, 2009	October 31, 2008
Balance Sheet Data:		
Assets:		
Current assets	$ 12,926,672	$ 27,223,185
Property and equipment	98,560,605	103,882,039
Other assets	1,602,000	2,295,586
Total assets	$ 113,089,277	$ 133,400,810
Current liabilities	$ 69,059,726	$ 23,552,096
Long-term debt	4,775,804	59,265,534
Members’ equity	39,253,747	50,583,180
Total liabilities and members’ equity	$ 113,089,277	$ 133,400,810

ITEM 7. MANAGEMENT’S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion should be read in conjunction with our financial statements and related notes contained elsewhere in this Annual Report on Form 10-K. This discussion may contain forward-looking statements based upon current expectations that involve risks and uncertainties. Our actual results and the timing of selected events could differ materially from those anticipated in these forward-looking statements as a result of selected factors, including those set forth under “Risk Factors” in Part I, Item 1A of this Form 10-K. All forward-looking statements included herein are based on information available to us as of the date hereof, and we undertake no obligation to update any such forward-looking statements.

We prepared the following discussion and analysis to help readers better understand our financial condition, changes in our financial condition, and results of operations for the fiscal year ended October 31, 2009. Since our plant became operational in September 2007, the financial data derived from our operations and related production and sales data for the twelve months ended October 31, 2007 is not comparable to that of fiscal year ended October 31, 2009 or 2008.

Overview

Heron Lake BioEnergy, LLC is a Minnesota limited liability company that was formed April 12, 2001 under the name "Generation II, LLC". In June 2004, we changed our name to Heron Lake BioEnergy, LLC. We were formed for the purpose of constructing and operating a dry mill corn-based ethanol plant near Heron Lake, Minnesota. The plant has a stated capacity to produce 50 million gallons of denatured fuel grade ethanol and 160,000 tons of dried distillers' grains per year. Production of ethanol and distillers' grains at the plant began, in September 2007. We began recording revenue from plant production in October 2007, the last month of our fiscal year. Our revenues are derived from the sale and distribution of our ethanol throughout the continental United States and in the sale and distribution of our distillers' grains locally, and throughout the continental United States.

Our operating results are largely driven by the prices at which we sell ethanol and distillers grains and the costs related to their production, particularly the cost of corn. Historically, the price of ethanol tended to fluctuate in the same direction as the price of unleaded gasoline and other petroleum products. However, during fiscal 2008 and continuing into fiscal 2009, it appears ethanol prices tended to move up and down proportionately, with changes in corn prices. The price of ethanol can also be influenced by factors such as general economic conditions, concerns over blending capacities, and government policies and programs. The price of distillers grains is generally influenced by supply and demand, the price of substitute livestock feed, such as corn and soybean meal, and other animal feed proteins. Our largest component of and cost of production is corn. The cost of corn is affected primarily by factors over which we lack any control such as crop production, carryout, exports, government policies and programs, and weather. The growth of the ethanol industry has increased the demand for corn. We believe that continuing increase in global demand will result in corn prices above historic averages. As an example of our potential sensitivity to price changes, if the price of ethanol rises or falls $.10 per gallon, our revenues may increase or decrease accordingly by approximately $5.0 million, assuming no other changes in our business. Additionally, if the price of corn rises or falls $0.25 per bushel, our cost of goods sold may increase or decrease by $5.0 million, again assuming no other changes in our business. During our fiscal 2009, the market price of ethanol and corn were extremely volatile. The price of corn hit a high of $4.73 per bushel in June, 2009 and a low of $3.06 in September, 2009 while the price of ethanol fluctuated from a high of $2.20 in October, 2009 and a low of $1.50 in July, 2009.

Trends and Uncertainties Impacting Our Operations

Our current and future results of operation are affected and will continue to be affected by factors such as (a) volatile and uncertain pricing of ethanol and corn; (b) availability of corn that is, in turn, affected by trends such as corn acreage, weather conditions, and yields on existing and new acreage diverted from other crops; and (c) the supply and demand for ethanol, which is affected by acceptance of ethanol as a substitute for fuel, public perception of the ethanol industry, government incentives and regulation, and competition from new and existing construction, among other things. Other factors that may affect our future results of operation include those factors discussed in "Item 1. Business" and "Item 1A. Risk Factors."

Critical Accounting Estimates

We review long-lived assets and estimates related to inventory and forward purchase commitments for impairment whenever events or changes in circumstances indicate that the related carrying amounts may not be recoverable. Impairment testing for assets requires various estimates and assumptions, including an allocation of cash flows to those assets and, if required, an estimate of the fair value of those assets. Our estimates are based upon assumptions believed to be reasonable, but which are inherently uncertain and unpredictable. These valuations require the use of management's assumptions, which do not reflect unanticipated events and circumstances that may occur. In our analysis, we consider future corn costs and ethanol prices, break-even points for our plant and our risk management strategies in place through our derivative instruments and forward contracts. Given the significant assumptions required and the possibility that actual conditions will differ, we consider the assessment of impairment of our long-lived assets to be a critical accounting estimate.

We reviewed our long-lived assets for impairment at October 31, 2009. As a result of this review and our related analysis, we believe our long-lived assets were not impaired as of October 31, 2009.

We enter forward contracts for corn purchases to supply the plant. These contracts represent firm purchase commitments which along with inventory on hand must be evaluated for potential losses. We have estimated a loss on these firm purchase commitments to corn contracts in place and for corn on hand at October 31, 2009 where the price of corn exceeds the market price and upon being used in the manufacturing process and eventual sale of products we anticipate losses. Our estimates include various assumptions including the future prices of ethanol, distillers grains and corn.

Fiscal Year Ended October 31, 2009 Compared to Fiscal Year Ended October 31, 2008

The following table shows the results of our operations and the percentage of revenues, cost of goods sold, operating expenses and other items to total revenues in our statements of operations for the fiscal year ended October 31, 2009 and 2008:

	2009		2008	
Income Statement Data	**Amount**	**%**	**Amount**	**%**
Revenues	$ 88,304,596	100.0	$ 131,070,642	100.0
Cost of Goods Sold	90,857,247	102.9	114,411,541	87.3
Gross Margin	(2,552,651)	(2.9)	16,659,101	12.7
Selling, General, and Administrative Expenses	4,515,476	5.1	3,351,252	2.5
Operating Income (Loss)	(7,068,127)	(8.0)	13,307,849	10.2
Other Expense	(4,261,307)	(4.8)	(4,689,810)	(3.6)
Net Income (Loss)	$ (11,329,434)	(12.8)	$ 8,618,039	6.6

Revenues

Ethanol revenues during the period ended October 31, 2009 were approximately $70.4 million, comprising 80% of our revenues. Sales of ethanol through September 30, 2009 were made pursuant to the terms of our ethanol marketing agreement with RPMG, Inc. under which our ethanol was pooled with the ethanol of other ethanol producers whose ethanol was marketed by RPMG. We paid RPMG a marketing fee and RPMG paid us a netback price per gallon that is based upon the difference between the pooled average delivered ethanol selling price and the pooled average distribution expense. These averages were calculated based upon each pool participant's selling price and expense averaged in direct proportion to the volume of ethanol supplied by each participant to the pool.

We believe that the ethanol market structure has changed since we entered into our ethanol marketing agreement with RPMG, and in particular during the past one to two years. We determined, in light of those changes, that the pool marketing arrangement used by RPMG was no longer an effective arrangement under the current market structure and circumstances. We accordingly notified RPMG that the ethanol marketing agreement would be terminated effective September 30, 2009.

Sales of ethanol subsequent to September 30, 2009 were made pursuant to the terms of our ethanol marketing agreement with C&N Ethanol Marketing Corporation ("C&N"). Under the Agreement, C&N purchases, markets and re-sells all of the ethanol produced at the Company's plant for the three year term of the Agreement. C&N will pay us the gross sales price to the customer less expenses and a 1% marketing fee after expenses.

For the year ended October 31, 2009, we sold approximately 46.4 million gallons of ethanol at an average price of $1.52 per gallon. For the year ended October 31, 2008, we sold approximately 48.4 million gallons of ethanol at an average price of $2.10 per gallon. We believe that the number of gallons of ethanol sold was affected by the plant's productivity that was impacted by scheduled and unscheduled downtime during the year, including as a result of testing and process changes relating to our air emissions. Further, the price of ethanol during our fiscal year was affected by the demand for ethanol as a motor fuel which is affected by, among other factors, regulatory developments, gasoline consumption, and the price of crude oil. Gasoline consumption was volatile during the fiscal year as the price for crude oil fluctuated radically. The price was also affected by federal RFS blending mandates.

We may hedge anticipated ethanol sales through a variety of mechanisms. Our marketers, whether RPMG or C&N, are obligated to use reasonable efforts to obtain the best price for our ethanol. To mitigate ethanol price risk and to obtain the best margins on ethanol that is marketed and sold by a marketer, we may utilize ethanol swaps, over-the-counter ("OTC") ethanol swaps, or OTC ethanol options that are typically settled in cash, rather than gallons of the ethanol we produce. For the years ended October, 31, 2009 and 2008, we recorded gains of $0.4 million and $3.6 million respectively related to ethanol derivative instruments. There are timing differences in the recognition of gains on derivatives as compared to the corresponding sale of ethanol. As such, the gains recognized could be associated with related sales in fiscal years 2007, 2008 or 2009.

We expect to see fluctuations in ethanol prices over the next fiscal year. While the demand for ethanol is expected to continue since gasoline blenders will need increasing amounts of ethanol to meet the Renewable Fuels Standard's blending requirements, the supply is also expected to increase as additional production facilities are completed or return to production. In addition, low prices for petroleum and gasoline will exert downward pressure on ethanol prices. If ethanol prices decline, our earnings will also decline, particularly if corn prices remain substantially higher than historic averages, as they were in our fiscal year 2009. Future prices for fuel ethanol will be affected by a variety of factors beyond our control including, the demand for ethanol as a motor fuel, federal incentives for ethanol production, the amount and timing of additional domestic ethanol production and ethanol imports and petroleum and gasoline prices.

Total sales of DGS during fiscal years 2009 and 2008 equaled approximately $12.8 million and $18.2 million, respectively, comprising 14% of our revenues for each year. Under a marketing agreement with CHS, Inc., CHS markets and sells all distillers' grains produced by our ethanol plant. Under the terms of the agreement, we receive a price equal to the selling price, less a charge of 2% or 4% of the price for distillers' grains and a fee of $2.00 per ton of solubles, less the cost of delivering the product to the customer. In fiscal year 2009 we sold approximately 119,000 tons of dried distillers' grain compared to 113,000 tons sold in fiscal year 2008. The average price we received for distillers' grain was approximately $107 per ton in fiscal year 2009 and approximately $147 per ton in fiscal year 2008.

The prices for DGS increased significantly during the first three quarters of fiscal 2008, due to the rising price of corn, soybean meal, and other animal feed proteins that are substitutes for DGS. These factors were not present in fiscal year 2009. However, during the last quarter of fiscal 2008, decreasing corn prices placed downward pressure on DGS prices which continued through fiscal 2009. In addition, the average price we received for our DGS in fiscal 2008 was limited by forward wet distillers grains contracts locking in a portion of our DGS prices.

Prices for distillers' grains are affected by a number of factors beyond our control such as the supply of and demand for distillers' grains as an animal feed and prices for competing feeds. We believe that current market prices for distillers' grains are approaching levels that can be sustained long-term as long as the prices of competing animal feeds remain steady or increase, livestock feeders continue to create demand for alternative feed sources such as distillers' grains and the supply of distillers' grains remains relatively stable. On the other hand, if competing commodity price values retreat and distillers' supplies increase due to growth in the ethanol industry, distillers' grains prices may decline.

Cost of Goods Sold

Our costs of sales include, among other things, the cost of corn used in ethanol and DGS production (which is the largest component of costs of sales), coal, processing ingredients, electricity, and wages, salaries and benefits of production personnel. We use approximately 1.5 million bushels of corn per month at the plant. We contract with local farmers and elevators for our corn supply. We are able to store corn that we purchase in our elevators in Lakefield and Wilder, Minnesota, as well as in on-site storage at the plant.

Our costs of sales (including lower of cost or market adjustments) as a percentage of revenues were 102.9% and 87.3% for the twelve months ended October 31, 2009 and, 2008, respectively. The per bushel cost of corn purchased (net of losses realized in fiscal year 2008 for bushels delivered in fiscal 2009) decreased approximately 19% in the twelve months ended October 31, 2009 as compared to the twelve months ended October 31, 2008. Cost of goods sold includes lower of cost or market adjustments of $5.4 million for the fiscal year ended October 31, 2009, which related to forward purchase contracts and inventory where the fixed price was more than the estimated realizable value. The lower of cost or market adjustment for the twelve months ended October 31, 2008 was $8.7 million We had gains related to corn derivative instruments of approximately $1.2 million and $6.3 million for the twelve months ended October 31, 2009 and 2008, respectively, which reduced cost of sales. In summary, lower of cost or market adjustments decreased $3.3 million for the fiscal year ended October 31, 2009 as compared to the fiscal year ended October 31, 2008. During the same periods, gains on derivatives decreased $5.1 million. These increased net costs combine with the 28% decrease in the per gallon sales price of ethanol caused the increase in the cost of goods sold as a percent of revenues for the twelve months ended October 31, 2009 **.** Our gross margin (loss) for the twelve months ended October 31, 2009 decreased to (2.9%) from 12.7% for the twelve months ended October 31, 2008. We had a negative gross margin in fiscal year 2009 as compared to positive gross margin in fiscal year 2008 due to the decline in ethanol prices; increased costs of goods sold, relative to revenues, due to losses on forward contracts; and decreased gains on derivative instruments. In addition, lower production levels and fixed costs contributed to the negative gross margin incurred.

The cost of corn fluctuates based on supply and demand, which, in turn, is affected by a number of factors that are beyond our control. We expect our gross margin to fluctuate in the future based on the relative prices of corn and fuel ethanol. We use futures and options contracts to minimize our exposure to movements in corn prices, but there is no assurance that these hedging strategies will be effective. Through October 31, 2009, none of our derivative contracts were designated as hedges and, as a result, changes to the market value of these contracts were recognized as an increase or decrease to our costs of goods sold. As a result, gains or losses on derivative instruments do not necessarily coincide with the related corn purchases. This may cause fluctuations in cost of goods sold. While we do not use hedge accounting to match gains or losses on derivative instruments, we believe the derivative instruments provide an economic hedge.

Costs of sales also include expenses directly attributable to the repair and maintenance of the plant. During the three months ended July 31, 2009, we incurred costs of approximately $300,000 as part of a five day planned annual shutdown and maintenance procedure. Upon shutdown, portions of the refractory section of the boiler collapsed. While there were no injuries sustained, significant additional costs were incurred to secure the refractory, ensure the safety of the workers completing repairs and to complete the repairs. This added eleven days to the shutdown for a total of sixteen days shutdown during May.

During the three months ended July 31, 2009, we entered into an amendment to our agreement with a leasing company under which we lease certain rail cars. The terms of the amendment reduce the rail cars under lease by 50 cars and increase the monthly rental amount per remaining rail car until July 1, 2014. This will result in a monthly cash savings of $425 per rail car or $21,250.

We have forward contracts in place for corn purchases of approximately 1.8 million bushel through May 2010 which represents approximately 9% of our anticipated purchases in fiscal 2010. Currently, some of these corn contract prices are above the current market price for corn. Upon taking delivery under these contracts, we would incur a loss. Accordingly, we recorded a loss on these purchase commitments of approximately $5.0 million for the twelve months ended October 31, 2009. Of the amount recorded in costs of goods sold, we have realized $3.8 million upon delivery and may realize the remaining $1.2 million in fiscal 2010. The loss, along with a write down of inventory on hand of $0.4 million, was recorded as a lower of cost or market adjustment on the statement of operations. The amount of the loss was determined by applying a methodology similar to that used in the lower of cost or market evaluation with respect to inventory. Given the uncertainty of future ethanol prices, this loss may or may not be recovered, and further losses on the outstanding purchase commitments could be recorded in future periods. At October 31, 2009, 1.2 million bushel subject to future contracted prices had contracted prices less than current market prices. Unrealized gains on these contracts have not been recorded. In order to mitigate risk associated with price fluctuations of coal, the Company has entered into coal supply agreements with a minimum commitment of approximately $4,950,000 per year until May 2012, including transportation, with provisions for fuel surcharges and adjustments for inflation.

Selling, General, and Administrative Expense

Operating expenses include wages, salaries and benefits of administrative employees at the plant, insurance, professional fees and similar costs and generally do not vary with the level of production at the plant. These expenses were $4.5 million for the twelve months ended October 31, 2009 up 34.7% from $3.3 million for the twelve months ended October 31, 2008. Upon a planned annual shutdown, portions of the refractory section of the boiler collapsed. While there were no injuries sustained, significant additional costs were incurred to secure the refractory, ensure the safety of the workers completing repairs and to complete the repairs. Costs associated with the unplanned repairs were approximately $700,000 and are included in operating expenses. Professional fees increased for the twelve months ended October 31, 2009 as compared to the prior year period because of additional legal, accounting and internal control consulting work in anticipation of required compliance with the Sarbanes-Oxley Act of 2002 and SEC reporting requirements, as well as the arbitration action we commenced against Fagen, Inc. Decreased revenue for the fiscal year ended October 31, 2009 negatively affected operating expenses as a percentage of revenue as total revenues declined approximately 33%.

Operating Income

Our loss from operations for fiscal year 2009 totaled $7.1 million compared to income from operations for fiscal year 2008 of approximately $13.3 million.

Other Income and (Expense)

Other expense consisted primarily of interest expense. Interest expense consists primarily of interest payments on our credit facilities described below. Interest expense for fiscal year 2009, which is down approximately 16.5% as compared to the twelve months ended October 31, 2008, is dependent on the balances outstanding and on interest rate fluctuations. As of October 31, 2009, debt balances were down slightly as compared to balances at October 31, 2008. The average 1 month LIBOR rate for the twelve months ended October 31, 2009 was 0.52% compared to 3.25% for the twelve months ended October 31, 2008. From May 1, 2009 through May 29, 2009, AgStar added a 2.0% surcharge to the interest rate on the outstanding amounts under the Company's master loan agreement. Also included in other expense is the write-off of loan costs of approximately $445,000. Because we have not obtained a waiver from AgStar for actual or expected violations of our master loan agreement, our long-term debt with AgStar was classified as a current liability. As such, we wrote-off the remaining loan costs rather than amortizing them over the original contractual term of the loans.

Year Ended October 31, 2008 Compared to Year Ended October 31, 2007

Income Statement Data	2008 Amount	2008 %	2007 Amount	2007 %
Revenues	$ 131,070,642	100.0	$ 23,560,498	100.0
Cost of Goods Sold	114,411,541	87.3	24,313,695	103.2
Gross Margin	16,659,101	12.7	(753,197)	(3.2)
Selling, General, and Administrative Expenses	3,351,252	2.5	3,527, 199	15.0
Operating Income (Loss)	13,307,849	10.2	(4,280,396)	(18.2)
Other Expense	(4,689,810)	(3.6)	(1,167,890)	(4.9)
Net Income (Loss)	$ 8,618,039	6.6	(5,448,286)	(23.1)

Revenues

As previously noted, commercial production of fuel ethanol and distillers' grains began in September 2007. Accordingly, our first full year of revenues from the sale of fuel ethanol and distillers' grains with solubles ("DGS") produced at the plant occurred during the fiscal year ended October 31, 2008. Ethanol revenues during the period ended October 31, 2008 were approximately $101.8 million, comprising 78% of our revenues. All sales of ethanol were made pursuant to the terms of our ethanol marketing agreement with RPMG, Inc. Under the agreement, RPMG must use its best efforts to market all ethanol produced by our ethanol plant pursuant to a pooled marketing arrangement. We receive a price equal to the actual pooled price received by RPMG, less the expense of distribution and a marketing fee charged per gallon of ethanol sold. For the year ended October 31, 2008, we sold approximately 48.4 million gallons of ethanol at an average price of $2.10 per gallon. For the 2008 fiscal year, we believe that the number of gallons of ethanol sold were affected by the plant's productivity that was impacted by scheduled and unscheduled downtime during the year, including as a result of testing and process changes relating to our air emissions. Further, the price of ethanol during our fiscal year was affected by the demand for ethanol as a motor fuel which is affected by, among other factors, regulatory developments, gasoline consumption, and the price of crude oil. Gasoline consumption was volatile during the fiscal year as the price for crude oil fluctuated radically. The price was also affected by federal RFS blending mandates.

We may hedge anticipated ethanol sales through a variety of mechanisms. We market all of our ethanol through RPMG, Inc., which is obligated to use reasonable efforts to obtain the best price for our ethanol. To mitigate ethanol price risk and to obtain the best margins on ethanol that is marketed and sold by RPMG, we may utilize ethanol swaps, over-the-counter ("OTC") ethanol swaps, or OTC ethanol options that are typically settled in cash, rather than gallons of the ethanol we produce. For the year ended October, 31, 2008, we recorded gains of $3.6 million related to derivative instruments. There are timing differences in the recognition of gains on derivatives as compared to the corresponding sale of ethanol. As such, the gains recognized could be associated with related sales in fiscal years 2007, 2008 or 2009.

Ethanol prices reached $2.95 per gallon in July 2008, but have declined substantially since that time. Lower ethanol prices continued into the first quarter of fiscal 2009, and we expect to see continuing fluctuations in ethanol prices over the next fiscal year. While the demand for ethanol is expected to continue since gasoline blenders will need increasing amounts of ethanol to meet the Renewable Fuels Standard's blending requirements, the supply is also expected to increase as additional production facilities are completed. In addition, low prices for petroleum and gasoline will exert downward pressure on ethanol prices. If ethanol prices decline, our earnings will also decline, particularly if corn prices remain substantially higher than historic averages.

Future prices for fuel ethanol will be affected by a variety of factors beyond our control including, the demand for ethanol as a motor fuel, federal incentives for ethanol production, the amount and timing of additional domestic ethanol production and ethanol imports and petroleum and gasoline prices.

Total sales of DGS during fiscal year 2008 equaled approximately $18.2 million, comprising 14% of our revenues. Under a marketing agreement with CHS, Inc., CHS markets and sells all distillers' grains produced by our ethanol plant. Under the terms of the agreement, we receive a price equal to the selling price, less a charge of 2% or 4% of the price for distillers' grains and a fee of $2.00 per ton of solubles, less the cost of delivering the product to the customer. In fiscal year 2008 we sold approximately 113,000 tons of dried distillers' grains at an average price of approximately $147 per ton. In fiscal year 2008 we sold approximately 32,000 tons of modified wet distillers' grains at an average price of approximately $48 per ton.

Similarly, the prices for DGS increased significantly during the first three quarters of fiscal 2008, due to the rising price of corn, soybean meal, and other animal feed proteins that are substitutes for DGS. However, during the last quarter of fiscal 2008, decreasing corn prices placed downward pressure on DGS prices. In addition, the average price we received for our DGS in fiscal 2008 was limited by forward wet distillers grains contracts locking in a portion of our DGS prices.

Prices for distillers' grains are affected by a number of factors beyond our control such as the supply of and demand for distillers' grains as an animal feed and prices for competing feeds. We believe that current market prices for distillers' grains are approaching levels that can be sustained long-term as long as the prices of competing animal feeds remain steady or increase, livestock feeders continue to create demand for alternative feed sources such as distillers' grains and the supply of distillers' grains remains relatively stable. On the other hand, if competing commodity price values retreat and distillers' supplies increase due to growth in the ethanol industry, distillers' grains prices may decline.

Cost of Goods Sold

Cost of goods sold during the year ended October 31, 2008 was $114,411,541 million, representing 87% of total revenues. Cost of goods sold consists primarily of the costs of corn, coal, depreciation, electricity and denaturant. We use approximately 1.5 million bushels of corn and 8,000 tons of coal per month at our ethanol plant. We contract with local farmers and elevators for our corn supply and secure coal under our agreement with Northern Coal Transport Company. Corn prices on the Chicago Board of Trade reached $7.60 per bushel during mid-summer of 2008. Prices declined significantly since that time, but the average price paid for corn during the fiscal year ended October 31, 2008 was $4.78 per bushel

The cost of both corn and coal fluctuates based on supply and demand which, in turn, is affected by a number of factors which are beyond our control. We expect our gross margin to fluctuate in the future based on the relative prices of corn, coal and fuel ethanol. We use futures and options contracts to minimize our exposure to movements in corn prices, but there is no assurance that these hedging strategies will be effective. At October 31, 2008, none of our derivative contracts were designated as hedges and, as a result, changes to the market values of these contracts are recognized as an increase or decrease to our costs of goods sold. For the year ended October 31, 2008, we recognized a gain of approximately $6.3 million with respect to these contracts, which decreased costs of goods sold during the period by this amount.

The Company had forward contracts in place for corn purchases of approximately $31,663,000 through October 2009, which represents approximately 38% of the Company's anticipated purchases in fiscal 2009. Some of these corn contract prices were above current market prices for corn. Given the recent declining price of corn and ethanol, upon taking delivery under these contracts, the Company would incur a loss. Accordingly, the Company recorded a loss on these purchase commitments of approximately $7,123,000 at October 31, 2008. The loss, along with a write down of inventory on hand of $1,628,000, was recorded as a lower of cost or market adjustment on the statement of operations. The amount of the loss was determined by applying a methodology similar to that used in the lower of cost or market evaluation with respect to inventory. Based on the positions at October 31, 2008, further adverse price changes of 10% in the price of ethanol and corn subsequent to year-end would result in additional losses of approximately $1,254,000.

In order to mitigate risk associated with price fluctuations of coal, The Company has entered into coal supply agreements with a minimum commitment of approximately $4,950,000 per year until May 2012, including transportation, with provisions for fuel surcharges and adjustments for inflation.

Selling, General, and Administrative Expense

Selling, general and administrative expenses include wages, salaries and benefits of administrative employees at the plant, insurance, professional fees and similar costs. These expenses decreased in fiscal year 2008 as compared to fiscal year 2007 by approximately $192,000 to $3.3 million or 2.5% of total revenues. The decrease is due, in part, to increased expenses in fiscal year 2007 resulting from the delayed production start date.

Operating Income

Our income from operations for fiscal year 2008 totaled approximately $13.3 million, compared to an operating loss of approximately $4.3 million for fiscal year 2007. This change was a result of our transition from a development stage company to an operational company.

Other Income and (Expense)

Other income and expense consists primarily of interest expense of approximately $4.81 million. Interest expense consists primarily of interest payments under our agreements with AgStar). Also included in other income and expense were interest income and other income totaling approximately $118,000.

Liquidity and Capital Resources

As of October 31, 2009, we had cash and cash equivalents (other than restricted cash) of approximately $3.2 million, current assets of approximately $12.9 million and total assets of approximately $113.1 million.

Our principal sources of liquidity consist of cash provided by operations, cash and cash equivalents on hand, and available borrowings under our master loan agreement with AgStar. Under the master loan agreement, we have three forms of debt: a term note, a revolving term note and a line of credit. The total indebtedness to AgStar at October 31, 2009 consists of $53.4 million under the term note, $1.1 million under the revolving term note and $5.0 million under the line of credit. Among other provisions, our master loan agreement contains covenants requiring us to maintain various financial ratios and tangible net worth. It also limits our annual capital expenditures and membership distributions. All of our assets and real property are subject to security interests and mortgages in favor of AgStar as security for the obligations of the master loan agreement. As of October 31, 2009, we were in default of covenants of our master loan agreement with AgStar requiring us to maintain at least $5.0 million minimum working capital; at least $39.5 million of tangible net worth; and a fixed charge ratio of 1.20 to 1.00 or greater.

In May 2008, we locked in an interest rate of 3.58% plus 3.00%, which totals 6.58%, on $45.0 million of the term note, for three years ending April 30, 2011. The remainder of the amounts outstanding on the term note is subject to the variable rate based on the one-month LIBOR plus 3.25%. We are required to make equal monthly payments of principal and interest of approximately $640,000 to amortize the note over a period not to exceed ten years, with a final balloon payment due in October 2012. In addition, we are required to make additional payments on the term note of excess cash flow, as defined in the agreement, up to $2.0 million per year to the lending institution until we meet certain minimum tangible owner's equity, as defined in the agreement. As part of the debt financing, the premium above LIBOR may be reduced based on the ratio of members' equity to assets. AgStar implemented a 2.0% interest rate surcharge effective May 1, 2009 through May 29, 2009, on the total debt outstanding in accordance with the terms of the master loan agreement due to the defaults explained below.

Our principal uses of cash are to pay operating expenses of the plant and to make debt service payments on our long-term debt. During the twelve months ended October 31, 2009, we used cash to make principal payments of approximately $5.0 million against our long-term debt. During the same period, we drew $5.0 million on our line of credit described below.

The following table summarizes our sources and uses of cash and equivalents from our condensed consolidated statements of cash flows for the periods presented (in thousands):

	Year Ended October 31		
	2009	2008	2007
Net cash provided by (used in) operating activities	$ (8,334)	$ 23,193	$ (12,721)
Net cash used in investing activities	(232)	(1,436)	(4,175)
Net cash provided by (used in) financing activities	395	(13,492)	17,362
Net increase (decrease) in cash and equivalents	$ (8,171)	$ 8,265	$ 466

Year Ended October 31, 2009 Compared to Year Ended October 31, 2008

During the twelve months ended October 31, 2009, we used $8.3 million in cash for operating activities. This use consists primarily of funding a net loss of $5.2 million exclusive of depreciation and amortization of $6.1 million; and payments for corn under deferred payment agreements and other payables of $3.2 million.

During the twelve months ended October 31, 2009, we used approximately $232,000 for investing activities to pay for capital expenditures and intangibles, and do not anticipate any significant capital expenditures during fiscal 2010.

During the twelve months ended October 31, 2009, we generated $395,000 from financing activities consisting primarily of advances on the line of credit of $5.0 million, payments on long term debt of approximately $5.0 million and the release of restricted cash in the amount of $0.4 million.

At October 31, 2009, we were in default of covenants of our master loan agreement with AgStar requiring us to maintain at least $5.0 million minimum working capital; at least $39.5 million of tangible net worth; and a fixed charge ratio of 1.20 to 1.00 or greater. Additionally, we do not expect to be in compliance with one or more covenants of the master loan agreement as of fiscal year end 2010 unless amendments are issued. Our failure to maintain the required amount of working capital constitutes an event of default under the master loan agreement, entitling the lender to accelerate and declare due all amounts outstanding under the master loan agreement. Therefore, we have classified $49.3 million of the AgStar debt as a current liability that would otherwise be classified as long term. As a result, current liabilities as of October 31, 2009 totaled approximately $69.1 million, including $49.3 million of long-term debt reclassified as current liabilities. In connection with the renewal of our revolving line of credit effective May 29, 2009, AgStar waived the Company's noncompliance with the working capital covenant of the master loan agreement as of and for the periods ending January 31, 2009 and April 30, 2009. On September 9, 2009, AgStar waived the Company's noncompliance with the working capital covenant of the master loan agreement for the period ended July 31, 2009. Our debt with AgStar remains classified as a current liability based on current and projected violations of debt covenants within the next year.

Our line of credit under the master loan agreement with AgStar renewed at a maximum commitment of $6,750,000. Effective May 29, 2009, we entered into an Amendment No. 3 to the Fifth Supplement to our master loan agreement, as previously amended and supplemented, with AgStar. Among other things, the effect of this amendment was to renew the Company's revolving line of credit loan at a maximum commitment of $6,750,000 and a maturity date of November 1, 2009. Effective December 8, 2009, we entered into an Amendment No. 4 to the Fifth Supplement to our master loan agreement to extend the maturity date of the revolving line of credit to February 1, 2010. As of October 31, 2009, we had drawn $5.0 million on the line of credit.

We are not currently in compliance with all covenants of the master loan agreement and there is no assurance that we will be able to comply in the future with all covenants and obligations of the master loan agreement or that any waiver or amendment to the master loan agreement will be provided by AgStar. Further, there can be no assurance that AgStar will not demand immediate repayment of all $59.5 million in indebtedness outstanding under the master loan agreement at October 31, 2009 or exercise any of its rights as a secured party with respect to the Company's assets now or in the future should we fail to comply with any covenants in the future. We do not have adequate capital to repay all of the amounts that would become due if AgStar accelerates our obligations under the master loan agreement. Further, we do not have adequate cash to repay the $5.0 million outstanding on the line of credit at October 31, 2009 and intend to request an additional extension of the maturity date of this line of credit beyond February 1, 2010. There can be no assurance that such an extension will be granted on terms advantageous to us, if at all. Further, while an event of default exists, the Company is not permitted to borrow additional funds under its line of credit or revolving term note unless AgStar consents to the advance. While AgStar has consented to make advances in the past, our potential inability to borrow additional funds under the master loan agreement may result in a working capital shortfall.

The Company's plan to address the expected shortfall of working capital is to conserve funds by utilizing and reducing corn inventory as well as reducing operating expenses through cost controls. The Company believes it has sufficient funding for its business in the short-term if it is not required to repay the outstanding indebtedness to AgStar or the outstanding indebtedness on the line of credit, based on converting and selling inventory, and reducing expenses. If the current industry conditions continue and the Company is not able to maintain sufficient funding in the short-term, the Company may be forced to raise subordinated debt, if available, sell additional equity, restructure or significantly curtail its operations, file for bankruptcy or cease operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be forced to take any such actions. However, there can be no assurance, that we will not require additional financing in the future or that any additional financing will be available to us on satisfactory terms, if at all.

During fiscal 2008, we were not in compliance with a covenant of our loan agreements with AgStar requiring the submission of quarterly financial statements within 30 days of the end of each quarter. However, AgStar waived these events of non-compliance with this covenant. Other than this covenant relating to delivery of financial statements, we were in compliance with the covenants of our loan agreements with AgStar during fiscal year 2008.

Year Ended October 31, 2008 Compared to Year Ended October 31, 2007

Operating Activities — We generated approximately $23 million from operating activities in fiscal year 2008 compared to fiscal year 2007 during which we used approximately $13 million for operating activities. This increase of approximately $36 million was due to a number of factors. Contributing to the net increase were the following:

(1) Net income was $8.6 million for the year ended October 31, 2008 compared to a net loss of $5.4 million for year ended October 31, 2007.

(2) Depreciation and amortization expense for the year ended October 31, 2008 as compared to the year ended October 31, 2007 increased $ 4.4 million to $5.7 million.

(3) As of October 31, 2007, we had used cash to purchase inventory in the amount of $19 million compared to October 31, 2008 at which time inventory levels were reduced to $9.6 million.

(4) Cash was used during the year ended October 31, 2008 to reduce accounts payable by $3.6 million compared to an increase of accounts payable for the year ended October 31, 2007 of $7.7 million.

Investing Activities—During the year ended October 31, 2008, we used $1.4 million for investing activities compared to $4.2 million used during the year ended October 31, 2007. This difference is due, primarily, to a reduction of capital expenditures after we began producing ethanol at our plant and the construction had stopped.

Financing Activities—We used $13.5 for financing activities for the year ended October 31, 2008 as compared to the year ended October 31, 2007 during which we raised $17.4 million in cash through financing activities. Contributing to the change were the following:

(1) We repaid $7.0 million on our line of credit with AgStar in fiscal year 2008 compared to advances on the line of credit of $6.1 million in fiscal year 2007.

(2) We received loan proceeds of $4.2 million in 2007 from a related party for our purchase of corn inventory and retention of previously purchased corn inventory until our plant was operating. That note was paid in full in fiscal year 2008.

(3) We paid down a net of $1.8 million on long term debt in fiscal year 2008 compared to repayment of $0.3 million in fiscal year 2007.

(4) We received $7.5 million in proceeds from the sale of equity in 2007. There were no such proceeds in fiscal year 2008.

At October 31, 2008, we had cash balances of approximately $11.4 million. In addition, we had approximately $3.8 million of long-term borrowing capacity and $7.1 million of short term borrowing capacity, net of outstanding letters of credit.

Off Balance-Sheet Arrangements

We have no off balance-sheet arrangements.

Credit Arrangements

Credit Arrangements with AgStar

On September 29, 2005, we entered into a credit agreement with AgStar Financial Services, PCA ("AgStar") establishing a senior credit facility for construction of the plant in the amount of $59,583,000. Simultaneously, we and AgStar entered into a Second Supplement that provided for a revolving loan in the amount of $2,000,000 to provide for general, corporate and operating expenses. In December 2006, the construction loan was amended to increase the amounts available up to $64,583,000. The construction loan converted to a $59,583,000 term note and a $5,000,000 revolving term note in October 2007. The amount available under the revolving term note is reduced each year by $500,000. As of October 31, 2009, the maximum amount of the revolving term note was $4,000,000.

The term note required interest only payments from November 2007 to April 2008 at the one-month LIBOR plus 3.25%, which totaled 3.49%, 5.74% and 9.07% at October 31, 2009, 2008 and 2007, respectively. In May 2008, we locked in an interest rate of 3.58% plus 3.00%, which totals 6.58%, on $45,000,000 of the note, for three years ending April 30, 2011. The remainder of the amounts outstanding on the term note is subject to the variable rate based on LIBOR. We will make equal monthly payments of principal and interest of approximately $640,000 to amortize the note over a period not to exceed ten years, with a final balloon payment due in October 2012. In addition, we are required to make additional payments on the term note of excess cash flow, as defined in the agreement, up to $2,000,000 per year to the lending institution until we need a specified financial ratio. As part of the debt financing, the premium above LIBOR may be reduced based on the ratio of members' equity to assets.

As of October 31, 2009, we have used approximately $1.1 million of AgStar's commitment under the revolving term note. The term note and revolving term note will mature on October 1, 2012.

We also have a line of credit with AgStar that is subject to certain borrowing base requirements. On June 12, 2009, the Company and AgStar agreed upon the terms of the renewal of the Company's line of credit effective May 29, 2009. Therefore, effective May 29, 2009, the Company entered into an Amendment No. 3 to the Fifth Supplement (the "Amendment") to its master loan agreement, as previously amended and supplemented, with AgStar. Among other things, the effect of this amendment was to renew the Company's revolving line of credit loan at a maximum commitment of $6,750,000 and a maturity date of November 1, 2009. Effective December 8, 2009, the Company and AgStar agreed upon the terms of Amendment No 4 to the Fifth Supplement ("Amendment 4") to its master loan agreement as previously amended and supplemented. The effect of this Amendment 4 was to extend the maturity date of the revolving line of credit to February 1, 2010.

Amounts available under the line of credit are reduced by outstanding standby letters of credit. Interest accrues on borrowings at the one month LIBOR plus 3.25%, which totaled 3.49%, 5.74% and 9.07% at October 31, 2009, 2008 and 2007, respectively. We must pay a 0.25% commitment fee on the average daily unused portion of the line of credit. At October 31, 2009, 2008 and 2007, outstanding borrowings on the line of credit were $5,000,000, none and $6,974,235, respectively. We had an outstanding standby letters of credit of $400,000 at October 31, 2008, which expired in November 2008. We had no outstanding standby letters of credit at October 31, 2009.

AgStar has been granted a security interest in substantially all of the assets of Heron Lake BioEnergy and its subsidiary, Lakefield Farmers Elevator, LLC. We also assigned to AgStar our interest in our agreements for the sale of ethanol and distillers grains, and for the purchases of coal, corn and electricity, as well as our design-build agreement with Fagen, Inc. AgStar also received a mortgage relating to our real property and that of Lakefield Farmers Elevator. Roland J. (Ron) Fagen personally guarantees our obligations under the credit agreement with AgStar, up to a maximum of $3,740,000, through a personal guaranty. Mr. Fagen did not, and has not, received any consideration from us for acting as guarantor. Fagen, Inc. also guaranteed a portion of our indebtedness to AgStar, but this guarantee was eliminated effective October 1, 2007. The guaranty agreements specify certain events of default, including: material breaches of representations and warranties; failure to perform or comply with any covenant or agreement in the guaranty agreement; or the occurrence of an event of default under the master loan agreement or other loan documents.

During the term of the loans, we are subject to certain financial loan covenants consisting of minimum working capital, minimum debt coverage, and minimum tangible net worth. We are only allowed to make annual capital expenditures up to $500,000 annually without prior approval. The loan agreements also impose restrictions on our ability to make cash distributions to our members.

Upon an occurrence of an event of default or an event that will lead to our default, AgStar may upon notice terminate its commitment to loan funds and declare the entire unpaid principal balance of the loans, plus accrued interest, immediately due and payable. An event of default includes, but is not limited to, our failure to make payments when due, insolvency, any material adverse change in our financial condition or our breach of any of the covenants, representations or warranties we have given in connection with the transaction.

At October 31, 2009 as at July 31, 2009, April 30, 2009 and January 31, 2009, the Company was out of compliance with the minimum working capital requirement provision of its master loan agreement with AgStar Financial Services, PCA (AgStar). In addition, the Company anticipates that the minimum net worth and fixed charge coverage ratio covenants will not be met through or as of fiscal year end 2010 unless amended. At January 31, 2009, the Company reclassified the long-term debt related to this agreement to current liabilities because the Company was not in compliance with the minimum working capital requirement. That reclassification remains as of October 31, 2009 because of the actual and anticipated covenant default stated above. Additionally, the Company expensed the remaining unamortized loan costs totaling approximately $445,000 associated with this debt during the quarter ended January 31, 2009.

In connection with the renewal of the line of credit effective May 29, 2009, AgStar waived the Company's noncompliance with the working capital covenant of the master loan agreement as of and for the periods ending January 31, 2009 and April 30, 2009. AgStar also waived excess cash flow payment provisions for the year ended October 31, 2008 in consideration of an excess cash flow payment by the Company of $94,700 on June 12, 2009. The balance due of the October 31, 2008 excess cash flow payment in the amount of $1,799,300 is deferred until such time as the Company makes a request to the Lender for certain distributions to its members. On September 9, 2009, AgStar waived the Company's noncompliance with the working capital covenant of the master loan agreement for the period ended July 31, 2009. As of October 31, 2009, the unwaived covenant defaults relate to the Company's default of covenants requiring us to maintain at least $5.0 million minimum working capital; at least $39.5 million of tangible net worth; and a fixed charge ratio of 1.20 to 1.00 or greater.

If AgStar exercises its right to accelerate the maturity of the debt outstanding under the master loan agreement or the line of credit, the Company will not have adequate available cash to repay the amounts currently outstanding at October 31, 2009. Further, while an event of default exists, the Company is not permitted to borrow additional funds under its line of credit or revolving term note without AgStar's consent.

The Company believes it has sufficient capital resources through October 31, 2010 based upon its current cash reserves, inventory sales, anticipated revenues and the available borrowing under the master loan agreement, as well as the effect of expense reduction measures, provided that AgStar extends the maturity date of the revolving line of credit, does not exercise its right to accelerate the maturity of the long term debt, and the Company is not otherwise required to repay its indebtedness to AgStar under the master loan agreement on an accelerated basis. The Company's expense reduction measures and cash conservation measures include utilizing and reducing corn inventory as well as reducing operating expenses through cost controls. If the current industry conditions continue and the Company is not able to maintain sufficient funding in the short-term, the Company may be forced to raise additional capital through subordinated debt, if available, sell additional equity, restructure or significantly curtail its operations, file for bankruptcy or cease operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be forced to take any such actions .

As of October 31, 2009, we estimate the fair value of our credit arrangements with AgStar to approximate $59.8 million, based on contractual terms, which is approximately $229,000 more than its carrying value of $59.5 based on the variable interest rate debt. The fair value of the debt fluctuates to the extent that interest rates are fixed and the current fair value rates are more or less than the fixed rate. While the debt markets have experienced significant volatility recently, the fixed rate portion of our long-term debt with AgStar reprices in April 2011 and all of the AgStar debt matures in October 2012 and we do not believe we are exposed to any unusual liquidity risks given the long-term nature of our debt. The market conditions for credit at the time of maturity of our debt in 2012 will determine our ability to refinance our debt and the terms associated with refinancing.

Other Credit Arrangements

In addition to our primary credit arrangement with AgStar, we have other material credit arrangements and debt obligations.

In October 2003, we entered into an industrial water supply development and distribution agreement with the City of Heron Lake, Jackson County, and Minnesota Soybean Processors. In consideration of this agreement, we and Minnesota Soybean Processors are allocated equally the debt service on $735,000 in water revenue bonds that were issued by the City to support this project that mature in February 2019. The parties have agreed that prior to the scheduled expiration of the agreement; they will negotiate in good faith to replace the agreement with a further agreement regarding the wells and related facilities. In May 2006, we entered into an industrial water supply treatment agreement with the City of Heron Lake and Jackson County. Under this agreement, we pay monthly installments over 24 months starting January 1, 2007 equal to one years' debt service on approximately $3.6 million in water revenue bonds, which will be returned to us if any funds remain after final payment in full on the bonds and assuming we comply with all payment obligations under the agreement. As of October 31, 2009, there was a total of $3.7 million in outstanding water revenue bonds and we classify our obligations under these bonds as assessments payable. The interest rates on the bonds range from 0.50% to 8.73%.

In November 2007, we entered into a shared savings contract with Interstate Power and Light Company ("IPL"), our electrical service provider. Under the agreement, IPL is required to pay $1,850,000 to fund project costs for the purchase and installation of electrical equipment. In exchange, we are required to share a portion of the energy savings with IPL that may be derived from the decreased energy consumption from the new equipment. We are required to pay IPL approximately $30,000 for the first thirteen billing cycles, $140,000 at the end of the thirteenth billing cycle, and thereafter, approximately $30,000 for the remainder of the billing cycles. These amounts represent IPL's portion of the shared savings. We also granted IPL a security interest in the electrical equipment to be installed on our site. The shared savings contract expires December 31, 2012.

In connection with the shared savings contract, IPL deposited $1,710,000 of the $1,850,000 in an escrow account on our behalf and we received the remaining $140,000 as cash proceeds. The escrow account expires at the same time as the shared savings contract or a termination by IPL of the escrow arrangement, at which time any remaining funds will be distributed to IPL. We earn interest at a rate of 4.2% on the funds escrowed and we pay a rate of interest of 1.5% on the funds deposited into escrow. Each month, a distribution from the escrow account is made to IPL to pay its portion of the shared savings under the shared savings contract.

To fund the purchase of the distribution system and substation for the plant, we entered into a loan agreement with Federated Rural Electric Association pursuant to which we borrowed $600,000 by a secured promissory note. Under the note we are required to make monthly payments to Federated Rural Electric Association of $6,250 consisting of principal and an annual fee of 1% beginning on October 10, 2009. In exchange for this loan, Federated Rural Electric Association was granted a security interest in the distribution system and substation for the plant. The balance of this loan at October 31, 2009 was $593,750.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We are a smaller reporting company, as defined by Rule 12b-2 of the Exchange Act, and therefore are not required to provide the information under this Item.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The following financial statements are included in this Annual Report on Form 10-K beginning at the "F" page noted:

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9A.T . CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

We maintain a system of "disclosure controls and procedures," as defined by Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, as amended.

Our Chief Executive Officer, Robert J. Ferguson, and Interim Chief Financial Officer, Brett L. Frevert, have evaluated our disclosure controls and procedures as of the end of the period covered by this report. Based upon their review, they have concluded that these controls and procedures are effective.

Changes in Internal Controls over Financial Reporting

In connection with the audit of our financial statements for our fiscal year ended October 31, 2008, we identified material weaknesses in our internal control over financial reporting relating to lack of segregation of duties, period-end closing procedures, and inadequate number of accounting department personnel. No material weaknesses will be considered remediated until the remedial procedures have operated for an appropriate period, have been tested and management has concluded that they are operating effectively. During fiscal year 2009, we completed a plan to address these material weaknesses including:

- Implementing policies with regards to the segregation of duties specifically as they relate to cash transactions;

- Improving period-end closing procedures that resulted in a more timely close; and

- Improving the review process to evaluate the accuracy of the financial statements and supplemental reports.

As a small business, the Company does not have the resources to fund sufficient staff to ensure a complete segregation of responsibilities within the accounting function. However, Company management reviews financial statements and bank reconciliations on a monthly basis, along with the adoption of a monthly financial closing process. These actions, in addition to the improvements identified above, will minimize any risk of a potential material misstatement occurring.

There have been no changes in internal control over financial reporting other than those identified above that occurred during the fourth fiscal quarter that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

The Company's internal control report is included in this Annual Report on Form 10-K under Item 8, "Financial Statements and Supplementary Data" under the caption "Management's Report on Internal Control Over Financial Reporting."

ITEM 9B. OTHER INFORMATION

Effective December 8, 2009, HLBE and AgStar agreed upon the terms of Amendment No. 4 to the Fifth Supplement to its master loan agreement as previously amended and supplemented. The effect of this Amendment No. 4 was to extend the maturity date of the revolving line of credit to February 1, 2010. The line of credit has a maximum commitment of $6,750,000. A copy of the Amendment No. 4 is attached to this Form 10-K as Exhibit 10.32.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

The information required by this item is incorporated herein by reference to the following sections of the Company's Proxy Statement for its 2010 Annual Meeting of Shareholders, which will be filed with the Securities and Exchange Commission pursuant to Regulation 14A within 120 days after the close of the fiscal year for which this report is filed (the "Proxy Statement"):

- Ownership of Units by Principal Holders and Management;
- Proposal 1: Election of Governors;
- Corporate Governance;
- Executive Officers and Executive Compensation;
- Certain Relationships and Related Person Transactions;
- Section 16(a) Beneficial Ownership Reporting Compliance; and
- Code of Ethics.

ITEM 11. EXECUTIVE COMPENSATION

The information required by this item is incorporated herein by reference to the sections of the Company's Proxy Statement entitled "Executive Officers and Executive Compensation" and "Governor Compensation."

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

The information required by this item is incorporated herein by reference to the section of the Company's Proxy Statement entitled "Ownership of Units by Principal Holders and Management," and is incorporated herein by reference to Part II, Item 5 entitled "Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities" of this Annual Report on Form 10-K.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

The information required by this item is incorporated by reference to the sections of the Company's Proxy Statement entitled "Certain Relationships and Related Person Transactions" and "Corporate Governance."

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

The information required by this item is incorporated herein by reference to the section of the Company's Proxy Statement entitled "Relationship with Independent Accountants."

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENTS SCHEDULES

(a) Financial Statements

(b) Exhibits

See "Exhibit Index" on the page following the Signature Page.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

Dated: January 29, 2010

HERON LAKE BIOENERGY, LLC

By: /s/ Robert J. Ferguson
Robert J. Ferguson, Chief Executive Officer
(principal executive officer)

Each person whose signature appears below hereby constitutes and appoints Robert J. Ferguson and Brett L. Frevert, and each of them, as his true and lawful attorney-in-fact and agent, with full power of substitution, to sign on his behalf, individually and in each capacity stated below, all amendments to this Form 10-K and to file the same, with all exhibits thereto and any other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents full power and authority to do and perform each and every act and thing requisite and necessary to be done in and about the premises, as fully and to all intents and purposes as each might or could do in person, hereby ratifying and confirming each act that said attorneys-in-fact and agents may lawfully do or cause to be done by virtue thereof.

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below on behalf of the registrant by the following persons in the capacities indicated on January29, 2010.

/s/ Robert J. Ferguson Robert J. Ferguson	Chief Executive Officer and President (principal executive officer), Governor
/s/ Brett L. Frevert Brett L. Frevert	Interim Chief Financial Officer (principal financial and accounting officer)
/s/ Doug Schmitz Doug Schmitz	Governor
/s/ Michael S. Kunerth Michael S. Kunerth	Governor
/s/ David J. Woestehoff David J. Woestehoff	Governor
/s/ David J. Bach David J. Bach	Governor
/s/ Timothy O. Helgemoe Timothy O. Helgemoe	Governor
/s/ Milton J. McKeown Milton J. McKeown	Governor
/s/ David M. Reinhart David M. Reinhart	Governor
/s/ Chad Core Chad Core	Governor
/s/ Robert J. Wolf Robert J. Wolf	Governor

Management's Report on Internal Control over Financial Reporting

The Board of Directors and Members of Heron Lake BioEnergy, LLC:

Management is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a15-(f) and 15d-15(f) under the Securities Exchange Act of 1934. The Company's internal control over financial reporting is a process designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles. A company's internal control over financial reporting includes those policies and procedures that:

(i) pertain to the maintenance of records that, in reasonable detail, accurately and fairly reflect the transactions and dispositions of the assets of the Company;

(ii) provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with generally accepted accounting principles, and that receipts and expenditures of the Company are being made only in accordance with authorizations of management and directors of the Company; and

(iii) provide reasonable assurance regarding prevention or timely detection of unauthorized acquisition, use or disposition of the Company's assets that could have a material effect on the financial statements.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Under the supervision of our Chief Executive Officer and our Interim Chief Financial Officer, we conducted an evaluation of the effectiveness of our internal control over financial reporting based on the framework in *Internal Control— Integrated Framework* issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO).

A material weakness (within the meaning of PCAOB Auditing Standard No. 2) is a control deficiency, or a combination of control deficiencies, that results in more than a remote likelihood that a material misstatement of the annual or interim financial statements will not be prevented or detected.

In conducting the aforementioned evaluation, management concluded that the Company's internal control over financial reporting was effective as of October 31, 2009.

Boulay, Heutmaker, Zibell & Co. P.L.L.P.
CERTIFIED PUBLIC ACCOUNTANTS & CONSULTANTS

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Governors
Heron Lake BioEnergy, LLC and Subsidiary
Heron Lake, Minnesota

We have audited the accompanying consolidated balance sheets of Heron Lake BioEnergy, LLC and Subsidiary as of October 31, 2009 and 2008, and the related consolidated statements of operations, changes in members' equity, and cash flows for each of the fiscal years in the three-year period ended October 31, 2009. Heron Lake BioEnergy, LLC and Subsidiary's management is responsible for these financial statements. Our responsibility is to express an opinion on these financial statements based on our audits.

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

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Heron Lake BioEnergy, LLC and Subsidiary as of October 31, 2009 and 2008, and the results of its operations and its cash flows for each of the fiscal years in the three-year period ended October 31, 2009 in conformity with accounting principles generally accepted in the United States of America.

The accompanying financial statements have been prepared assuming that the Company will continue as a going concern. As discussed in Note 2 to the financial statements, the Company has incurred a loss of approximately $11.3 million for the fiscal year ending October 31, 2009. The Company was also out of compliance of its master loan agreement and reclassified the long term debt related to this agreement to current liabilities. If the right to accelerate the maturity of the debt outstanding under the master loan agreement or the line of credit were to be exercised, the Company will not have adequate available cash to repay the amounts currently outstanding. These conditions raise substantial doubt about the Company's ability to continue as a going concern. Management's plans regarding those matters also are described in Note 2. The financial statements do not include any adjustments that might result from the outcome of this uncertainty.

/s/ Boulay, Heutmaker, Zibell & Co. P.L.L.P.

Certified Public Accountants

Minneapolis, Minnesota
January 29, 2010

HERON LAKE BIOENERGY, LLC AND SUBSIDIARY

Consolidated Balance Sheets

	October 31, 2009	October 31, 2008
ASSETS		
Current Assets		
Cash and equivalents	$ 3,184,074	$ 11,355,075
Restricted cash	340,644	1,499,472
Accounts receivable	4,439,701	3,368,076
Inventory	4,752,117	9,633,749
Derivative instruments	—	750,172
Prepaid expenses	210,136	616,641
Total current assets	12,926,672	27,223,185
Property and Equipment		
Land and improvements	12,574,760	12,552,721
Plant buildings and equipment	97,332,591	97,159,759
Vehicles and other equipment	604,783	597,921
Office buildings and equipment	618,437	597,508
	111,130,571	110,907,909
Accumulated depreciation	(12,569,966)	(7,025,870)
	98,560,605	103,882,039
Other Assets		
Deferred loan costs, net	—	467,128
Restricted cash	718,790	995,804
Other intangibles	488,010	464,304
Debt service deposits and other	395,200	368,350
Total other assets	1,602,000	2,295,586
Total Assets	$ 113,089,277	$ 133,400,810

Notes to Consolidated Financial Statements are an integral part of this Statement.

HERON LAKE BIOENERGY, LLC AND SUBSIDIARY

Consolidated Balance Sheets

		October 31, 2009		October 31, 2008
LIABILITIES AND MEMBERS' EQUITY				
Current Liabilities				
Line of credit	$	5,000,000	$	—
Current maturities of long-term debt		55,224,183		5,649,354
Accounts payable:				
Trade accounts payable		2,466,040		5,635,204
Trade accounts payable - related party		714,115		792,450
Construction payable - related party		3,839,413		3,839,413
Accrued expenses		566,481		512,709
Lower of cost or market adjustment		1,249,495		7,122,966
Total current liabilities		69,059,727		23,552,096
Long-Term Debt, net of current maturities		4,775,804		59,265,534
Commitments and Contingencies				
Members' Equity, 27,104,625 Class A units outstanding		39,253,746		50,583,180
Total Liabilities and Members' Equity	$	113,089,277	$	133,400,810

Notes to Consolidated Financial Statements are an integral part of this Statement.

HERON LAKE BIOENERGY, LLC AND SUBSIDIARY

Consolidated Statements of Operations

	Year Ended October 31, 2009	Year Ended October 31, 2008	Year Ended October 31, 2007
Revenues	$ 88,304,596	$ 131,070,642	$ 23,560,498
Cost of Goods Sold			
Cost of goods sold	85,448,407	105,660,541	24,313,695
Lower of cost or market adjustment	5,408,840	8,751,000	—
Total Cost of Goods Sold	90,857,247	114,411,541	24,313,695
Gross Profit (Loss)	(2,552,651)	16,659,101	(753,197)
Operating Expenses	4,515,476	3,351,252	3,527,199
Operating Income (Loss)	(7,068,127)	13,307,849	(4,280,396)
Other Income (Expense)			
Interest income	78,320	84,078	9,166
Interest expense	(4,014,448)	(4,807,965)	(1,181,442)
Write off of loan costs	(444,985)	—	—
Other income	119,806	34,077	4,386
Total other expense	(4,261,307)	(4,689,810)	(1,167,890)
Net Income (Loss)	$ (11,329,434)	$ 8,618,039	$ (5,448,286)
Weighted Average Units Outstanding - Basic and Diluted	27,104,625	27,104,625	26,361,406
Net Income (Loss) Per Unit - Basic and Diluted	$ (0.42)	$ 0.32	$ (0.21)

Notes to Consolidated Financial Statements are an integral part of this Statement.

HERON LAKE BIOENERGY, LLC AND SUBSIDIARY

Consolidated Statements of Changes in Members' Equity

Balance - October 31, 2006	39,733,427
Capital Contribution - 3,750,000 Class A units, $2.00 per unit, December 2006	7,500,000
Capital Contribution - exercise of warrants for 225,000 Class A units, $.80 per unit, August 2007	180,000
Net loss for the year ended October 31, 2007	(5,448,286)
Balance - October 31, 2007	41,965,141
Net income for the year ended October 31, 2008	8,618,039
Balance - October 31, 2008	50,583,180
Net loss for the year ended October 31, 2009	(11,329,434)
Balance - October 31, 2009	$ 39,253,746

Notes to Consolidated Financial Statements are an integral part of this Statement.

HERON LAKE BIOENERGY, LLC AND SUBSIDIARY

Consolidated Statements of Cash Flows

	Year Ended October 31, 2009	Year Ended October 31, 2008	Year Ended October 31, 2007
Cash Flow From Operating Activities			
Net income (loss)	$ (11,329,434)	$ 8,618,039	$ (5,448,286)
Adjustments to reconcile net income (loss) to net cash provided by (used in) operating activities:			
Depreciation and amortization	5,645,311	5,688,300	1,269,117
Amortization of loan costs included with interest expense	22,143	—	—
Write off of loan costs	444,985	—	—
Lower of cost or market adjustment	5,408,840	8,751,000	—
Unrealized (gains) losses on derivative instruments	—	(678,713)	150,088
(Gain)/loss on disposal of assets	(38,301)	3,317	(4,396)
Change in operating assets and liabilities:			
Restricted cash	1,021,767	(803,383)	291,500
Accounts receivable	(1,071,625)	(1,413,950)	(1,550,443)
Inventory	4,529,174	7,729,607	(14,861,633)
Derivative instruments	750,172	(257,695)	(879,384)
Prepaid expenses	406,505	(491,783)	(51,784)
Accounts payable	(3,247,499)	(3,611,106)	7,718,778
Accrued expenses	53,771	(341,041)	645,577
Accrued lower of cost or market adjustments	(10,929,853)	—	—
Net cash provided by (used in) operating activities	(8,334,044)	23,192,592	(12,720,866)
Cash Flows from Investing Activities			
Proceeds from sale of assets	177,516	224,498	29,421
Capital expenditures	(349,521)	(1,186,148)	(4,204,339)
Payment for other intangibles	(59,835)	(474,183)	—
Net cash used in investing activities	(231,840)	(1,435,833)	(4,174,918)
Cash Flows from Financing Activities			
Checks written in excess of bank balance	—	(514,633)	(8,972)
Proceeds from (payments on) line of credit, net	5,000,000	(6,974,235)	6,126,175
Proceeds from (payments on) note payable - related party	—	(4,202,930)	4,202,930
Proceeds from long-term debt	—	3,289,177	—
Payments on long-term debt	(4,992,343)	(5,113,249)	(307,168)
Payments for loan costs	—	—	(179,166)
Debt service deposits	(26,850)	(215,600)	(151,750)
Release of restricted cash	414,076	239,457	—
Member contributions	—	—	7,500,000
Member contributions related to warrants exercised	—	—	180,000
Net cash provided by (used in) financing activities	394,883	(13,492,013)	17,362,049
Net Increase (Decrease) in cash and equivalents	(8,171,001)	8,264,746	466,265
Cash and Equivalents - Beginning of period	11,355,075	3,090,329	2,624,064
Cash and Equivalents - End of period	$ 3,184,074	$ 11,355,075	$ 3,090,329

Notes to Consolidated Financial Statements are an integral part of this Statement.

HERON LAKE BIOENERGY, LLC AND SUBSIDIARY

Consolidated Statements of Cash Flows

	Year Ended October 31, 2009	Year Ended October 31, 2008	Year Ended October 31, 2007
Supplemental Disclosure of Cash Flow Information			
Interest expense paid	$ 4,040,240	$ 5,100,895	$ 589,118
Interest capitalized paid	—	—	2,802,010
Total interest paid	$ 4,040,240	$ 5,100,895	$ 3,391,128
Supplemental Disclosure of Non-Cash Activities			
Restricted cash from long-term debt proceeds	$ —	$ 1,710,000	$ —
Property and equipment in construction payables	$ —	$ 3,839,413	$ 4,188,455
Property and equipment financed by long-term debt	$ —	$ —	$ 40,245,680
Assessment payable related to property and equipment	$ —	$ —	$ 867,500
Loan costs capitalized with property and equipment	$ —	$ —	$ 99,387
Construction payables refinanced with long-term debt	$ —	$ —	$ 14,882,948

Notes to Consolidated Financial Statements are an integral part of this Statement.

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Nature of Business

The Company owns and operates a 50 million gallon ethanol plant near Heron Lake, Minnesota with ethanol distribution to upper Midwest states. In addition, the Company produces and sells distillers grains with solubles as co-products of ethanol production. The Company was formed on April 12, 2001 to have an indefinite life. The Company began its ethanol plant operations in September 2007. Prior to September 2007, the Company was in the development stage.

Principles of Consolidation

The financial statements include the accounts of Heron Lake BioEnergy, LLC and its wholly owned subsidiary, Lakefield Farmers Elevator, LLC, collectively, the "Company." All significant intercompany balances and transactions are eliminated in consolidation.

Fiscal Reporting Period

The Company's fiscal year end for reporting financial operations is October 31.

Accounting Estimates

Management uses estimates and assumptions in preparing these financial statements in accordance with generally accepted accounting principles. Those estimates and assumptions affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported revenues and expenses. The Company uses estimates and assumptions in accounting for significant matters including, among others, the carrying value and useful lives of property and equipment, analysis of impairment on long-lived assets, and valuation of forward purchase contract commitments and inventory. The Company periodically reviews estimates and assumptions, and the effects of revisions are reflected in the period in which the revision is made. Actual results could differ from those estimates.

Revenue Recognition

Revenue from sales is recorded when title transfers to the customer, collection of the relevant receivable is probable, persuasive evidence of an arrangement exists, and the sales price is fixed and determinable. The title transfers when the product is loaded into the railcar or truck, the customer takes ownership and assumes risk of loss.

Cash and Equivalents

The Company considers all highly liquid debt instruments purchased with a maturity of three months or less to be cash and equivalents.

The Company maintains its accounts at five financial institutions. At times throughout the year, the Company's cash balances may exceed amounts insured by the Federal Deposit Insurance Corporation and the Securities Investor Protection Corporation. The Company does not believe it is exposed to any significant credit risk on cash and equivalents.

Restricted Cash

The Company is periodically required to maintain cash balances at its broker related to derivative instrument positions. In addition, at October 31, 2009 the Company maintained restricted cash of approximately $341,000 related to a loan agreement as described in Note 10.

Accounts Receivable

Credit terms are extended to customers in the normal course of business. The Company performs ongoing credit evaluations of its customers' financial condition and, generally, requires no collateral.

Accounts receivable are recorded at estimated net realizable value. Accounts are considered past due if payment is not made on a timely basis in accordance with the Company's credit terms. Accounts considered uncollectible are written off. The Company's estimate of the allowance for doubtful accounts is based on historical experience, its evaluation of the current status of receivables, and unusual circumstances, if any. At October 31, 2009 and 2008, the Company was of the belief that such accounts would be collectable and thus an allowance was not considered necessary.

Inventory

Inventory consists of raw materials, work in process, finished goods, supplies, and other grain inventory. Corn is the primary raw material and, along with other raw materials and supplies, is stated at the lower of cost or market on a first-in, first-out (FIFO) basis. Work in process and finished goods, which consists of ethanol and distillers grains produced, is stated at the lower of average cost or market. Other grain inventory, which consists of agricultural commodities, is valued at market value (net realizable value). Other grain inventory is readily convertible to cash because of its commodity characteristics, widely available markets and international pricing mechanisms. Other grain inventory is also freely traded, has quoted market prices, may be sold without significant further processing, and has predictable and insignificant disposal costs. Merchandise inventory is valued at lower of cost or market on a first-in, first-out (FIFO) basis.

Costs of sales also include expenses directly attributable to the repair and maintenance of the plant. During the fiscal year ended October 31, 2009, we incurred costs of approximately $300,000 as part of a five day planned annual shutdown and maintenance procedure. Upon shutdown, portions of the refractory section of the boiler collapsed. While there were no injuries sustained, significant additional time and costs were incurred to secure the refractory, ensure the safety of the workers completing repairs and to complete the repairs. This added eleven days to the shutdown for a total of sixteen days shutdown during May. Costs associated with the unusual repairs were approximately $700,000 and are included in operating expenses

Derivative Instruments

From time to time, the Company enters into derivative transactions to protect gross margins from potentially adverse effects of market and price volatility in future periods. In order to reduce the risks caused by market fluctuations, the Company hedges a portion of its anticipated corn and natural gas purchases, and ethanol sales by entering into options and futures contracts. These contracts are used with the intention to fix the purchase price of anticipated requirements for corn and natural gas in the Company's ethanol production activities and the related sales price of ethanol produced. The fair value of these contracts is based on quoted prices in active exchange-traded or over-the-counter market conditions.

The Company generally does not designate these derivative instruments as hedges for accounting purposes and derivative positions are recorded on the balance sheet at their fair market value, with changes in fair value caused from marking these instruments to market, recognized in current period earnings or losses on a monthly basis. While the Company does not designate the derivative instruments that it enters into as hedging instruments because of the administrative costs associated with the related accounting, the Company believes that the derivative instruments represent an economic hedge.

In order for a derivative to qualify as a hedge, specific criteria must be met and appropriate documentation maintained. If the derivative does qualify as a hedge, depending on the nature of the hedge, changes in the fair value of the derivative will be either offset against the change in fair value of the hedged assets, liabilities, or firm commitments through earnings or recognized in other comprehensive income until the hedged item is recognized in earnings. Gains and losses from derivatives that do not qualify as hedges, or are undesignated, must be recognized immediately in earnings.

The Company evaluates its contracts to determine whether the contracts are derivatives. Certain contracts that literally meet the definition of a derivative may be exempted as "normal purchases or normal sales." Normal purchases and normal sales are contracts that provide for the purchase or sale of something other than a financial instrument or derivative instrument that will be delivered in quantities expected to be used or sold over a reasonable period in the normal course of business. Certain corn, ethanol and distillers grains contracts that meet the requirement of normal purchases or sales are documented as normal and exempted from the accounting and reporting requirements, and therefore, are not marked to market in our financial statements.

Other Intangibles

Other intangibles are stated at cost and include road improvements located near the plant in which the Company has a beneficial interest in but does not own the road. The Company amortizes the assets over the economic useful life of 15 years.

Property and Equipment

Property and equipment are recorded at cost. Depreciation is provided over an estimated useful life by use of the straight-line deprecation method. Maintenance and repairs are expensed as incurred; major improvements and betterments are capitalized. Construction in progress is comprised of costs related to the construction of the ethanol plant facilities. Interest is capitalized during the construction period. Depreciable useful lives are as follows:

Land improvements	15 Years
Plant building and equipment	7 - 40 Years
Vehicles and equipment	5 - 7 Years
Office buildings and equipment	3 - 40 Years

Long-Lived Assets

The Company reviews property and equipment and other long-lived assets for impairment whenever events or changes in circumstances indicate that the carrying amount may not be recoverable. Circumstances which could trigger a review include, but are not limited to: significant decreases in the market price of the asset; significant adverse changes in the business climate or legal factors; accumulation of costs significantly in excess of the amount originally expected for the acquisition of construction of the asset; current period cash flow or operating losses combined with a history of losses or a forecast of continuing losses associated with the use of the assets; and current expectation that the asset will more likely than not be sold or disposed significantly before the end of its estimated useful life. If circumstances require a long-lived asset be tested for possible impairment, the Company first compares undiscounted cash flows expected to be generated by an asset to the carrying value of the asset. If the carrying value of the long-lived asset is not recoverable on an undiscounted cash flow basis, an impairment is recognized to the extent that the carrying value exceeds its fair value. Fair value is determined through various valuation techniques including discounted cash flow models, quoted market values and third-party independent appraisals, as considered necessary.

The Company's ethanol production facilities, has an installed capacity of 50 million gallons per year. The carrying value of these facilities at October 31, 2009 was approximately $98.5 million. In accordance with the Company's policy for evaluating impairment of long-lived assets described above, management has evaluated the recoverability of the facilities based on projected future cash flows from operations over the facilities' estimated useful lives. Management has determined that the projected future undiscounted cash flows from operations of these facilities exceed their carrying value at October 31, 2009; therefore, no impairment loss was indicated or recognized. In determining the projected future undiscounted cash flows, the Company has made significant assumptions concerning the future viability of the ethanol industry, the future price of corn in relation to the future price of ethanol and the overall demand in relation to production and supply capacity. Given the uncertainties in the ethanol industry, should management be required to adjust the carrying value of the facilities at some future point in time, the adjustment could be significant and could significantly impact the Company's financial position and results of operations. No adjustment has been made to these financial statements for this uncertainty.

Deferred Loan Costs

Costs associated with the issuance of the debt discussed in Note 9 and 10 are recorded as deferred loan costs, net of accumulated amortization. Loan costs are amortized to operations over the term of the related debt using the effective interest method. Prior to the commencement of operations in September 2007, the Company capitalized loan costs with interest costs during the construction of the plant. Once operations commenced, loan cost amortization was expensed. As explained in Note 10, the Company has reclassified the long term portion of certain debt to current. At that time, the Company expensed the remaining unamortized loan costs totaling approximately $445,000 associated with this debt.

Grants

The Company recognizes grant proceeds for reimbursement of expenditures incurred upon complying with the conditions of the grant. For reimbursements of incremental expenses (expenses the Company otherwise would not have incurred had it not been for the grant), the grant proceeds are recognized as a reduction of the related expense. For reimbursements of capital expenditures, the grants are recognized as a reduction of the basis of the asset upon complying with the conditions of the grant.

Financial Instruments

The Company believes the carrying value of cash and equivalents and restricted cash approximate fair value.

The Company believes the carrying amount of derivative instruments approximates fair value based on quoted prices in active exchange-traded or over-the-counter markets.

The Company believes the carrying amount of the line of credit and note payable approximates the fair value due to market interest rates and short-term nature of the debt.

Due to declining interest rates during 2009 and 2008 and having fixed the interest rate on a portion of the debt as noted in Note 10, the carrying amount of the long-term debt, based on contractual terms, was less than the fair value at October 31, 2009 and 2008. The carrying amount and the fair value of long-term debt are as follows:

	Carrying Amount	Fair Value
Long-term debt at October 31, 2009	$ 59,999,987	$ 60,228,760
Long-term debt at October 31, 2008	$ 64,914,888	$ 66,043,522

Income Taxes

The Company is treated as a partnership for federal and state income tax purposes and generally does not incur income taxes. Instead, its earnings and losses are included in the income tax returns of the members. Therefore, no provision or liability for federal or state income taxes has been included in these financial statements. Differences between financial statement basis of assets and tax basis of assets is related to capitalization and amortization of organization and start-up costs for tax purposes, whereas these costs are expensed for financial statement purposes. In addition, the Company uses the alternative depreciation system (ADS) for tax depreciation instead of the straight-line method that is used for book depreciation, which also causes temporary differences. The Company's tax year end is December 31. Primarily due to the partnership tax status, the Company does not have any significant tax uncertainties that would require disclosure.

Net Income (Loss) per Unit

Basic net income (loss) per unit is computed by dividing net income (loss) by the weighted average number of members' units outstanding during the period. Diluted net income or loss per unit is computed by dividing net income (loss) by the weighted average number of members' units and members' unit equivalents outstanding during the period.

Environmental Liabilities

The Company's operations are subject to environmental laws and regulations adopted by various governmental entities in the jurisdiction in which it operates. These laws require the Company to investigate and remediate the effects of the release or disposal of materials at its location. Accordingly, the Company has adopted policies, practices, and procedures in the areas of pollution control, occupational health, and the production, handling, storage and use of hazardous materials to prevent material environmental or other damage, and to limit the financial liability, which could result from such events. Environmental liabilities are recorded when the liability is probable and the costs can be reasonably estimated.

Subsequent Events

The Company has evaluated subsequent events through January 29, 2010 the date which the financial statements were issued.

2. GOING CONCERN

The financial statements have been prepared on a going-concern basis, which contemplates the recoverability of assets and the satisfaction of liabilities in the normal course of business. Significant volatility in the commodity markets have caused margins in the ethanol industry to be negative. For fiscal 2009 the Company incurred a loss of approximately $11.3 million and used cash of approximately $8.3 million for operating activities during the twelve months ended October 31, 2009. At October 31, 2009, the Company was out of compliance with the minimum working capital, the minimum tangible net worth and the minimum fixed charge ratio provisions of its master loan agreement with AgStar Financial Services, PCA ("AgStar"). In addition, the Company anticipates that one or more of the covenants will not be met as of fiscal year end 2010 unless amended. At January 31, 2009, the Company reclassified the long-term debt related to this agreement to current liabilities because the Company was not in compliance with the minimum working capital requirement. That reclassification remains as of October 31, 2009 because of the actual and anticipated covenant defaults stated above. As a result, the Company expensed the remaining unamortized loan costs totaling approximately $445,000 associated with this debt during the quarter ended January 31, 2009. If AgStar exercises its right to accelerate the maturity of the debt outstanding under the master loan agreement or the line of credit, the Company will not have adequate available cash to repay the amounts currently outstanding at October 31, 2009. Further, while an event of default exists, the Company is not permitted to borrow additional funds under its line of credit or revolving term note without AgStar's consent. These factors raise substantial doubt about the Company's ability to continue as a going concern.

On June 12, 2009, the Company and AgStar agreed upon the terms of the renewal of the Company's line of credit effective May 29, 2009. Therefore, effective May 29, 2009, the Company entered into an Amendment No. 3 to the Fifth Supplement (the "Amendment") to its master loan agreement, as previously amended and supplemented, with AgStar. Among other things, the effect of this amendment was to renew the Company's revolving line of credit loan at a maximum commitment of $6,750,000 and a maturity date of November 1, 2009. In connection with the renewal, AgStar also waived the Company's noncompliance with the working capital covenant of the master loan agreement as of and for the periods ending January 31, 2009 and April 30, 2009. AgStar also waived excess cash flow payment provisions for the year ended October 31, 2008 in consideration of an excess cash flow payment by the Company of $94,700 on June 12, 2009. The balance due of the October 31, 2008 excess cash flow payment in the amount of $1,799,300 is deferred until such time as the Company makes a request to the Lender for certain distributions to its members. On September 9, 2009, AgStar waived the Company's noncompliance with the working capital covenant of the master loan agreement for the period ended July 31, 2009. Effective December 8, 2009, the Company and AgStar agreed upon the terms of Amendment No 4 to the Fifth Supplement ("Amendment 4") to its master loan agreement as previously amended and supplemented. The effect of this Amendment 4 was to extend the maturity date of the revolving line of credit to February 1, 2010. The Company is actively negotiating the extension of this with the bank.

The Company believes it has sufficient capital resources through October 31, 2010 based upon its current cash reserves, inventory sales, anticipated revenues and the available borrowing under the master loan agreement, as well as the effect of expense reduction measures, provided that AgStar extends the maturity date of the revolving line of credit, does not exercise its right to accelerate the maturity of the long term debt, and the Company is not otherwise required to repay its indebtedness to AgStar under the master loan agreement on an accelerated basis. The Company's expense reduction measures and cash conservation measures include utilizing and reducing corn inventory as well as reducing operating expenses through cost controls. If the current industry conditions continue and the Company is not able to maintain sufficient funding in the short-term, the Company may be forced to raise additional capital through subordinated debt, if available, sell additional equity, restructure or significantly curtail its operations, file for bankruptcy or cease operations. The financial statements do not include any adjustments relating to the recoverability and classification of recorded asset amounts or amounts and classification of liabilities that might be necessary should the Company be forced to take any such actions .

3. UNCERTAINTIES

The Company has certain risks and uncertainties that it experienced during volatile market conditions such as what the Company experienced during fiscal 2008 and 2009. These volatilities can have a severe impact on operations. The Company's revenues are derived from the sale and distribution of ethanol and distillers grains to customers primarily located in the U.S. Corn for the production process is supplied to the plant primarily from local agricultural producers. Ethanol sales average 75% - 80% of total revenues and corn costs average 65% - 70% of cost of goods sold.

The Company's operating and financial performance is largely driven by the prices at which it sells ethanol and the net expense of corn. The price of ethanol is influenced by factors such as supply and demand, the weather, government policies and programs, unleaded gasoline prices and the petroleum markets as a whole, although since 2005 the prices of ethanol and gasoline began a divergence with ethanol selling for less than gasoline at the wholesale level. Excess ethanol supply in the market, in particular, puts downward pressure on the price of ethanol. The largest cost of production is corn. The cost of corn is generally impacted by factors such as supply and demand, the weather, government policies and programs, and a risk management program used to protect against the price volatility of these commodities. Market fluctuations in the price of and demand for these products may have a significant adverse effect on the Company's operations, profitability and the availability and adequacy of cash flow to meet the Company's working capital requirements.

4. FAIR VALUE MEASUREMENTS

The Company measures certain financial instruments at fair value in our balance sheets. The fair value of these instruments is based on valuations that include inputs that can be classified within one of the three levels of a hierarchy. Level 1 inputs include quoted market prices in an active market for identical assets or liabilities. Level 2 inputs are market data, other than Level 1, that are observable either directly or indirectly. Level 2 inputs include quoted market prices for similar assets or liabilities, quoted market prices in an inactive market, and other observable information that can be corroborated by market data. Level 3 inputs are unobservable and corroborated by little or no market data. Except for those assets and liabilities which are required by authoritative accounting guidance to be recorded at fair value in our balance sheets, the Company has elected not to record any other assets or liabilities at fair value. The fair value of certain long-lived assets is based on recoverability through utilization in operations. Except for those assets and liabilities which are required by authoritative accounting guidance to be recorded at fair value in our balance sheets, the Company has elected not to record any other assets or liabilities at fair value.

The following table provides information on those assets measured at fair value on a recurring basis.

	Fair Value as of October 31, 2009	Fair Value Measurement Using Level 1	Fair Value Measurement Using Level 2	Fair Value Measurement Using Level 3
Restricted cash — current	$ 340,644	$ 340,644	$ —	$ —
Restricted cash — long-term	$ 718,790	$ 718,790	$ —	$ —

The fair value of the money market funds included in restricted cash is based on quoted market prices in an active market.

5. CONCENTRATIONS

The Company sells all of the ethanol and distiller grains produced to two customers under marketing agreements as described in Note 15. At October 31, 2009 and 2008, these two customers comprised 96% and 93% of accounts receivable, respectively.

6. INVENTORY

Inventory consists of the following at October 31:

	2009	2008
Raw materials	$ 1,551,255	$ 5,830,477
Work in process	776,801	1,200,242
Finished goods	800,915	725,365
Supplies	847,289	683,007
Other grains	775,857	1,194,658
Totals	$ 4,752,117	$ 9,633,749

The Company recorded losses of approximately $352,000 and $1,628,000 for the fiscal years ended October 31, 2009 and 2008 respectively, related to inventory, in addition to losses recorded on forward purchase contracts as noted in Note 15, where the market value was less than the cost basis, attributable primarily to decreases in market prices of corn and ethanol. The loss was recorded with the lower of cost or market adjustment in the statement of operations. In addition, the Company stored grain inventory for farmers. The value of these inventories owned by others is approximately $283,000 and $658,000 based on market prices at October 31, 2009 and 2008, respectively, and is not included in the amounts above..

7. DERIVATIVE INSTRUMENTS

As of October 31, 2009, the Company held no positions in corn or ethanol derivative instruments. As of October 31, 2008, the Company recorded an asset for derivative instruments of approximately $750,000 at fair value in the Consolidated Balance Sheet.

The following tables provide details regarding the gains and (losses) from the Company's derivative instruments in statements of operations, none of which are designated as hedging instruments:

	Statement of Operations location	Twelve Months Ended October 31, 2009	2008	2007
Corn contracts	Cost of goods sold	$ 1,207,000	$ 6,287,000	$ (2,654,000)
Ethanol contracts	Revenues	373,000	3,600,000	—
Totals		$ 1,580,000	$ 9,887,000	$ (2,654,000)

8. CONSTRUCTION IN PROGRESS

The Company capitalizes construction costs and construction period interest until the assets are placed in service. During fiscal 2007, the Company capitalized interest during the construction period of approximately $2,901,000.

9. LINE OF CREDIT

The Company has a line of credit with AgStar subject to certain borrowing base requirements. On June 12, 2009 and effective May 29, 2009, the Company entered into an Amendment No. 3 to the Fifth Supplement (the "Amendment") to its master loan agreement, as previously amended and supplemented, with AgStar. Among other things, the effect of this amendment was to renew the Company's revolving line of credit loan at a maximum commitment of $6,750,000 and a maturity date of November 1, 2009. AgStar waived the Company's noncompliance with the working capital covenant of the master loan agreement as of and for the periods ending January 31, 2009, April 30, 2009, and July 31, 2009. Effective December 8, 2009, the Company and AgStar agreed upon the terms of Amendment No 4 to the Fifth Supplement ("Amendment 4") to its master loan agreement as previously amended and supplemented. The effect of this Amendment 4 was to extend the maturity date of the revolving line of credit to February 1, 2010. Interest accrues on borrowings at the one-month LIBOR plus 3.25%, which totaled 3.49% at October 31, 2009 and 5.74% at October 31, 2008. From May 1, 2009 through May 29, 2009, AgStar added a 2.0% surcharge to the interest rate on the outstanding amounts under the Company's master loan agreement. The Company has a .25% commitment fee on the unused portion of the line of credit. Amounts available under the line of credit are reduced by outstanding standby letters of credit. As of October 31, 2009, the Company had drawn $5,000,000 on the line. There was no balance outstanding on the line of credit at October 31, 2008. The Company had outstanding standby letters of credit of $400,000 at October 31, 2008, which expired in November 2008. As of October 31, 2009, the Company was not in compliance with the minimum working capital, minimum tangible net worth and minimum fixed charge ratio provisions of the master loan agreement. If AgStar exercises its right to accelerate the maturity of the debt outstanding under the master loan agreement or the line of credit, the Company will not have adequate available cash to repay the amounts currently outstanding at October 31, 2009. Further, while an event of default exists, the Company is not permitted to borrow additional funds under its line of credit or revolving term note without AgStar's consent.

The line of credit and the term note and revolving term note discussed in Note 10 are subject to a general security agreement with the lending institution bank. The terms of this agreement require the Company to maintain certain financial ratios and covenants such as working capital and net worth requirements, minimum debt to equity and debt service coverage, and restrictions on distributions. Borrowings under the agreement are secured by substantially all corporate assets. During fiscal 2008, the Company was not in compliance with the debt covenant related to the submission of quarterly financial statements within 30 days during fiscal 2008. The lender waived compliance for these violations.

10. LONG-TERM DEBT

Long-term debt consists of the following:

	October 31 2009	October 31 2008
Term note payable to lending institution, see terms below.	$ 53,381,697	$ 57,508,968
Revolving term note payable to lending institution, see terms below.	1,155,872	1,155,872
Note payable to Jackson County with interest at 4.00%, forgiven during fiscal 2009 based upon job creation thresholds at specified wages as part of the plant development.	—	100,000
Balance forward	$ 54,537,569	$ 58,764,840

	October 31 2009	October 31 2008
Balance from previous page	$ 54,537,569	$ 58,764,840
Assessment payable as part of water treatment agreement, due in semi-annual installments of $189,393 with interest at 6.55%, enforceable by statutory lien, with the final payment due in 2021. The Company is required to make deposits over 24 months, which began in January 2007, for one years' worth of debt service payments that are held on deposit to be applied with the final payments of the assessment.	3,010,998	3,173,624
Assessment payable as part of water treatment agreement, due in semi-annual installments of $25,692 with interest at 0.50%, enforceable by statutory lien, with the final payment due in 2016.	352,610	401,985
Assessment payable as part of water supply agreement, due in monthly installments of $4,126 with interest at 8.73%, enforceable by statutory lien, with the final payment due in 2019.	313,520	334,657
Note payable for equipment, with monthly payments of $2,371 including effective interest of 6.345%, due in April 2012, secured by equipment.	65,517	65,956
Note payable to electrical provider, with monthly payments of $29,775 including implicit interest of 1.50%, due in December 2013, secured by equipment and restricted cash.	1,126,023	1,573,826
Note payable to electrical company with monthly payments beginning in October 2009 of $6,250 with a 1% maintenance fee due each October, due September 2017. The electrical company is a member of the Company.	593,750	600,000
Totals	59,999,987	64,914,888
Less amounts due within one year	55,224,183	5,649,354
Net long-term debt	$ 4,775,804	$ 59,265,534

Term Note Payable

The term note requires monthly payments of approximately $640,000 of principal and interest. Interest accrues at the one-month LIBOR plus 3.25%, which totaled 3.49% and 5.74% at October 31, 2009 and 2008, respectively. In May 2008, the Company locked in an interest rate of 3.58% plus 3.00%, which totals 6.58% on $45,000,000 of the note, for three years ending April 30, 2011. As described in Notes 2 and 9, as of October 31, 2009, July 31, 2009, April 30, 2009 and January 31, 2009 the Company was not in compliance with the covenants of the master loan agreement. The Company received a waiver from AgStar as of and for the periods ended January 31, 2009, April 30, 2009 and July 31, 2009. However, the Company was not in compliance as of October 31, 2009 and does not expect to be in compliance with one or more covenants of the master loan agreement as of October 31, 2010 unless the covenants are amended. Therefore, the term note and the revolving term note described below have been classified as current liabilities. The term note originally had a ten year amortization, with a final balloon payment due in October 2012. In addition, the Company is required to make additional payments on the term note of excess cash flow, as defined in the agreement, up to $2,000,000 per year to AgStar until the Company meets a specified financial ratio. As part of the debt financing, the premium above LIBOR may be reduced based on the ratio of members' equity to assets. The owner of the general contractor, who is a member, has personally guaranteed up to $3,740,000 of the Company's obligations under the master loan agreement. From May 1, 2009 through May 29, 2009, AgStar added a 2.0% surcharge to the interest rate on the outstanding amounts under the Company's master loan agreement. If AgStar exercises its right to accelerate the maturity of the debt outstanding under the master loan agreement or the line of credit, the Company will not have adequate available cash to repay the amounts currently outstanding at October 31, 2009. Further, while an event of default exists, the Company is not permitted to borrow additional funds under its line of credit or revolving term note without AgStar's consent.

Revolving Term Note

The Company has a revolving term note with AgStar for up to $5,000,000 for cash and inventory management purposes. The maximum amount available under the revolving term note decreases $500,000 each year and was $4,000,000 as of October 31, 2009. The Company pays interest on principal advances monthly at the one-month LIBOR rate plus 3.25%, which totaled 3.49% and 5.74% at October 31, 2009 and 2008 respectively. The Company pays a commitment fee of 0.35% per annum on the unused portion of the revolving term note. As described above and in Note 2 and 9, as of and for the period ending October 31, 2009, the Company was out of compliance with the master loan agreement and does not anticipate being in compliance as of and for the period ending October 31, 2010. As such, amounts due under the revolving term note have been classified as current liabilities. From May 1, 2009 through May 29, 2009, AgStar added a 2.0% surcharge to the interest rate on the outstanding amounts under the Company's master loan agreement. During fiscal 2008, the Company was not in compliance with the debt covenant related to the submission of quarterly financial statements within 30 days. The lender waived compliance for this violation.

Estimated maturities of long-term debt at October 31, 2009 are as follows:

2010	$ 55,224,183
2011	707,088
2012	714,147
2013	453,477
2014	381,599
After 2014	2,519,493
Total long-term debt	$ 59,999,987

11. MEMBERS' EQUITY

The Company is authorized to issue 50,000,000 capital units, of which 28,750,000 have been designated Class A units, 11,250,000 have been designated as Class B units, and 10,000,000 have not yet been designated. Members of the Company are holders of units who have been admitted as members upon their investment in our units and who are admitted as members by our board of governors. The minimum number of units required to retain membership is 2,500 units. Any holder of units who is not a member will not have voting rights. Transferees of units must be approved by our board of governors to become members. Members who are holders of our present units are entitled to one vote for each unit held. Subject to the Member Control Agreement, all units share equally in the profits and losses, distributions of assets, and voting rights on a per unit basis.

At October 31, 2009 and 2008, the Company had 27,104,625 Class A units issued and outstanding.

Warrants

The Company authorized warrants in fiscal 2004 for 25,000 Class A units to the existing nine members of the Board of Governors. The warrants granted to each member of the Board of Governors the right to purchase 25,000 Class A units at an exercise price of $.80 per unit. The warrants vested October 31, 2005 and were exercisable for a period of five years thereafter. These units were not used in the computation of net loss per unit for fiscal 2007 as they would have been anti-dilutive. All of the warrants were exercised in August 2007 whereby the Company received $180,000.

12. LEASES

The Company leases equipment, primarily rail cars, under operating leases through 2017. Equipment under operating lease primarily represents rail cars for which the rentals began in August 2007. Rent expense for fiscal 2009, 2008, and 2007 was approximately $844,000, $853,000, and $225,000 respectively.

At October 31, 2009, the Company had the following minimum future lease payments, which at inception had non-cancelable terms of more than one year:

2010	$	1,660,560
2011		1,660,560
2012		1,642,705
2013		1,556,100
2014		1,211,725
Thereafter		2,356,200
Total lease commitments	$	10,087,850

13. INCOME TAXES

The differences between consolidated financial statement basis and tax basis of assets are as follows at October 31:

		2009		2008
Consolidated financial statement basis of assets	$	113,089,277	$	133,400,810
Plus: Organization and start-up costs capitalized		2,037,334		2,195,063
Less: Unrealized gains on derivatives		—		(678,713)
Less: Accumulated tax depreciation and amortization greater than financial statement basis		(12,978,756)		(7,614,210)
Income tax basis of assets	$	102,147,855	$	127,302,950

		2009		2008
Consolidated financial statement basis of liabilities	$	73,835,531	$	82,817,630
Less: Accrued expenses		(1,815,975)		(7,635,675)
Income tax basis of liabilities	$	72,019,556	$	75,181,955

14. RELATED PARTY TRANSACTIONS

In December 2006, an affiliate of the plant design-builder invested an additional $7,500,000 in exchange for 3,750,000 Class A units. In July 2007, the Company was advanced approximately $4,203,000 from the owner of the general contractor for the purchase of inventory, which was repaid in November 2007.

In December 2006, the Company entered into an agreement with a member to construct an electrical substation for approximately $1,020,000. In November 2007, the Company obtained a loan from this member as described in Note 10.

The Company purchased approximately $45,266,000, $47,569,000 and $8,836,000 of corn from members in fiscal 2009, 2008 and 2007, respectively.

Please refer to the section titled "Legal Proceedings" following for information on arbitration proceedings between the Company and Fagen, Inc., a related party.

15. COMMITMENTS AND CONTINGENCIES

Water Agreements

In October 2003, the Company entered into an industrial water supply development and distribution agreement with the City of Heron Lake for 15 years. The Company has the exclusive rights to the first 600 gallons per minute of capacity that is available from the well, and provides for the Company, combined with Minnesota Soybean Processors (MnSP), to approve any other supply contracts that the City may enter into. In consideration, the Company will pay one half of the City's water well bond payments of $735,000, plus a 5% administrative fee, totaling approximately $594,000, and operating costs, relative to the Company's water usage, plus a 10% profit. These costs will be paid as water usage fees. The Company recorded an assessment of approximately $367,000 with long-term debt as described in Note 10. The Company pays operating and administrative expenses of approximately $12,000 per year.

In May 2006, the Company entered into a water treatment agreement with the City of Heron Lake and Jackson County for 30 years. The Company will pay for operating and maintenance costs of the plant in exchange for receiving treated water. In addition, the Company agreed to an assessment for a portion of the capital costs of the water treatment plant. The Company recorded assessments with long-term debt of $500,000 and $3,550,000 in fiscal 2007 and 2006, respectively, as described in Note 10. The Company paid operating and maintenance expenses of approximately $370,000 and $307,000 in fiscal 2009 and 2008, respectively.

Marketing Agreements

Effective September 30, 2009, the Company entered into an ethanol marketing agreement with an unrelated party under which the marketer will purchase, market and re-sell all of the ethanol produced at the Company's plant for the three year term of the agreement. Following the three year term, the agreement will automatically renew for subsequent year terms unless either party terminates the agreement 60 days before the end of the term. The Company pays certain expenses and a 1% marketing fee after expenses. The Company assumed leases on 125 rail cars for approximately $980,000 per year until May 2014 as part of the termination of the prior marketing agreement.

The Company has a distiller's grain marketing agreement with an unrelated party to purchase all of the Company's distiller's grains. The agreement provides for predetermined formulas for the sale of distiller's grains and solubles. The initial term was for one year after operations commenced and was automatically renewed on a monthly basis. The contract is terminable with 90 days written notice.

Legal Proceedings

Permit Matters

Our business subjects us to various federal, state and local environmental laws and regulations, including those relating to discharges into the air, water and ground; the generation, storage, handling, use, transportation and disposal of hazardous materials; and the health and safety of our employees.

The costs associated with obtaining these permits and meeting the demands of regulators reflected in the permits have increased our costs of construction and production. In particular, we have incurred additional costs relating to an air-emission permit from the Minnesota Pollution Control Agency ("MPCA"). We applied for a synthetic minor air-emissions source permit in July 2004 that was granted by the MPCA in May 2005. In June 2005, a coalition of two environmental groups and one energy group challenged the grant of this air emissions permit by an appeal to the Minnesota Court of Appeals. In July 2006, the Minnesota Court of Appeals affirmed the MPCA's issuance of the permit. In conjunction with the permit and the permit dispute and to prevent further appeals by the coalition, we entered into a compliance agreement with the MPCA on January 23, 2007 that currently governs the air emissions from our plant. Under the compliance agreement, we agreed to submit an amendment to our air permit to qualify our facility as a "major emissions source". The compliance agreement also allowed us to continue the construction of our facility. Under the compliance agreement, we agreed to operate our facility in a manner such that the emissions of each of the criteria pollutants generated by our ethanol plant, as determined on a 12 month rolling sum, do not exceed 95 tons per year and agreed to comply in all other respects with the air emissions permit previously issued by the MPCA. Accordingly, we submitted a major amendment to our existing air-emissions permit in December 2008, and, following air pollution control device testing, we submitted a second major amendment in September 2009, both seeking amendments to our air permit, including amendments to permit conditions and adjustments to other components of plant operations and production. However, we are continuing discussions with the MPCA regarding the necessity for qualifying our facility as a major emissions source, particularly in light of changes in federal law that increased the limit of certain emissions allowed as a synthetic minor source. On March 13, 2008, MPCA issued a notice of violation to us for violations of certain rules, statutes, and permit conditions (as modified by the compliance agreement), including emission violations and reporting violations. As part of our continuing discussions with MPCA, we are seeking to resolve these violations by agreement with MPCA. A violation of environmental laws, regulations or permit conditions can result in substantial civil fines or criminal sanctions, or permit revocations or plant shutdown. Pending the resolution of this air permit issue, we continue to operate subject to the compliance agreement.

Fagen Design-Build Litigation

On September 28, 2005, the Company executed a Design-Build Agreement with Fagen, Inc. by which Fagen, Inc. agreed to design and build a 50 million gallon per year coal-fired ethanol plant in Heron Lake, Minnesota, for a contract price of approximately $76,000,000. The agreement contained numerous warranty and guarantee provisions as well as a liquidated damages provision. Construction began in late 2005, and after several delays the first corn grind took place on September 21, 2007. The plant, however, has not been able to meet the air emissions warranties or operate as a “synthetic minor source” as warranted and intended under the design-build agreement.

By the terms of the Design-Build Agreement, claims or controversies between the Company and Fagen, Inc. arising out of or relating to the Design-Build Agreement, or the breach thereof, are ultimately to be decided by Arbitration in accordance with the Construction Industry Arbitration Rules of the American Arbitration Association. On September 18, 2009 the Company served and filed its Demand for Arbitration and Request for Mediation. A Revised Demand for Arbitration was served and filed on December 23, 2009 following an unsuccessful attempt to mediate the dispute. In these Demands for Arbitration, the Company alleges that Fagen, Inc. breached the terms and conditions of the Design-Build Agreement including its warranties and guarantees, was negligent in its efforts to correct various performance and emissions problems, had not completed the plant on a timely basis in accordance with the Design-Build Agreement, and prior to the execution of the Agreement had made certain negligent misrepresentations with respect to coal-fired ethanol plants. In the Demand for Arbitration, the Company seeks damages for breach of contract and breach of the warranties and guarantees, damages resulting from the negligent efforts to correct the problems, damages for the negligent misrepresentations, as well as liquidated damages for delays in the plant construction. The Company seeks damages in the amount of $22,800,000.

Fagen, Inc. responded to the Demand for Arbitration by denying liability and asserting various affirmative defenses. In addition, Fagen, Inc. brought a Counterclaim alleging that it is entitled to payment of a retainage held by the Company in the amount of approximately $3.8 million. In addition, Fagen, Inc. alleges that it performed additional work and provided additional labor and materials to the plant in the amount of approximately $2.2 million; it alleges that this did not constitute warranty or guarantee work and therefore it claims it is entitled to payment of this additional amount. The Company responded to the Counterclaim by denying the allegations and asserting various affirmative defenses. On January 4, 2010, Fagen, Inc. requested to join ICM, Inc. as a party to the arbitration action, claiming that joinder was necessary for proper resolution of the claims and defenses in the arbitration action. On January 27, 2010, ICM, Inc. responded to the request, agreeing to be joined provided certain procedures are established. In its response, ICM also indicated that it intends to assert claims against us under the license agreement we entered into with ICM as part of the design build agreement with Fagen. On January 27, 2010, we filed our response and objections to Fagen’s request to join ICM as a party, and requested that a special arbitrator be appointed to resolve the joinder issues. We intend to defend against the Fagen counterclaims and any claims brought by ICM, Inc. and assert our defenses vigorously.

The arbitration proceeding is in its early phase, and arbitrators have not yet been selected.

Contractual Obligations

The following table provides information regarding the consolidated contractual obligations of the Company as of October 31, 2009:

	Total	Less than One Year	One to Three Years	Three to Five Years	Greater Than Five Years
Long-term debt obligations (1)	$ 70,748,224	$ 64,521,802	$ 1,844,976	$ 1,198,130	$ 3,183,316
Operating lease obligations	10,087,850	1,660,560	3,303,265	2,767,825	2,356,200
Purchase obligations (2)	20,083,737	12,246,237	7,837,500	—	—
Total contractual obligations	$ 100,919,811	$ 78,428,599	12,985,741	$ 3,965,955	$ 5,539,516

(1) Long-term debt obligations include estimated interest and interest on unused debt.
(2) Purchase obligations primarily include forward contracts for corn and coal.

The Company also has agreements to pay for the operating costs and maintenance expenses associated with the water agreement of approximately $12,000 and $205,000 per year with term lengths of approximately 15 and 30 years, respectively.

The Company has coal supply agreements with a minimum commitment of approximately $4,950,000 per year until May 2012, including transportation, with provisions for fuel surcharges and adjustments for inflation. The amounts related to these agreements are included with purchase obligations in the table above.

Forward Contracts

The Company has forward contracts in place for corn purchases of approximately $7.3 million through May 2010, which represents approximately 9% of the Company's anticipated purchases in fiscal 2010.

Currently, some of these corn contract prices are above current market prices for corn. Given the recent changing price of corn upon taking delivery under these contracts, the Company would incur a loss. Accordingly, the Company recorded a loss on purchase commitments of approximately $5,056,000 and $7,123,000 for the twelve months ended October 31, 2009 and 2008 respectively. The loss was recorded as a lower of cost or market adjustment on the statement of operations. The amount of the loss was determined by applying a methodology similar to that used in the lower of cost or market evaluation with respect to inventory. Given the uncertainty of future ethanol prices, this loss may or may not be recovered, and further losses on the outstanding purchase commitments could be recorded in future periods.

HERON LAKE BIOENERGY, LLC

INDEX TO EXHIBITS TO FORM 10-K FOR FISCAL YEAR ENDED OCTOBER 31, 2008

Exhibit Number	Exhibit Title	Incorporated by Reference To:
3.1	First Amended and Restated Articles of Organization of Heron Lake BioEnergy, LLC	Exhibit 3.1 of the Company's Registration Statement on Form 10 (SEC Accession No. 0001104659-08-054557) filed on August 22, 2008 (the "2008 Registration Statement").
3.2	Member Control Agreement of Heron Lake BioEnergy, LLC, as amended through March 29, 2008	Exhibit 3.2 of the Company's 2008 Registration Statement.
4.1	Form of Class A Unit Certificate	Exhibit 4.1 of the Company's 2008 Registration Statement.
4.2	Unit Transfer Policy adopted November 5, 2008	Exhibit 4.1 of the Company's Current Report on Form 8-K dated November 5, 2008.
10.1	Fourth Amended and Restated Loan Agreement dated October 1, 2007 by and between AgStar Financial Services, PCA and Heron Lake BioEnergy, LLC	Exhibit 10.1 of the Company's 2008 Registration Statement.
10.2	Third Supplement dated October 1, 2007 to Fourth Amended and Restated Loan Agreement by and between AgStar Financial Services, PCA and Heron Lake BioEnergy, LLC	Exhibit 10.2 of the Company's 2008 Registration Statement.
10.3	Fourth Supplement dated October 1, 2007 to Fourth Amended and Restated Loan Agreement by and between AgStar Financial Services, PCA and Heron Lake BioEnergy, LLC	Exhibit 10.3 of the Company's 2008 Registration Statement.
10.4	Term Note dated October 1, 2007 in principal amount of $59,583,000 by Heron Lake BioEnergy, LLC to AgStar Financial Services, PCA as lender	Exhibit 10.4 of the Company's 2008 Registration Statement.
10.5	Term Revolving Note dated October 1, 2007 in principal amount of $5,000,000 by Heron Lake BioEnergy, LLC to AgStar Financial Services, PCA as lender	Exhibit 10.5 of the Company's 2008 Registration Statement.
10.6	Personal Guaranty dated October 1, 2007 by Roland Fagen, guarantor, in favor of AgStar Financial Services, PCA	Exhibit 10.6 of the Company's 2008 Registration Statement.
10.7	Fourth Amended and Restated Guaranty dated October 1, 2007 by Lakefield Farmers Elevator, LLC in favor of AgStar Financial Services, PCA	Exhibit 10.7 of the Company's 2008 Registration Statement.
10.8	Fifth Supplement dated November 19, 2007 to Fourth Amended and Restated Loan Agreement by and between AgStar Financial Services, PCA and Heron Lake BioEnergy, LLC	Exhibit 10.8 of the Company's 2008 Registration Statement.
10.9	Revolving Line of Credit Note dated November 19, 2007 in principal amount of $7,500,000 by Heron Lake BioEnergy, LLC to AgStar Financial Services, PCA as lender	Exhibit 10.9 of the Company's 2008 Registration Statement.
10.10	Industrial Water Supply Development and Distribution Agreement dated October 27, 2003 among Heron Lake BioEnergy, LLC (f/k/a Generation II Ethanol, LLC), City of Heron Lake, Jackson County, and Minnesota Soybean Processors	Exhibit 10.10 of the Company's 2008 Registration Statement.
10.11	Industrial Water Supply Treatment Agreement dated May 23, 2006 among Heron Lake BioEnergy, LLC, City of Heron Lake and County of Jackson	Exhibit 10.11 of the Company's 2008 Registration Statement.

Exhibit Number	Exhibit Title	Incorporated by Reference To:
10.12	Standard Form of Agreement between Owner and Designer — Lump Sum dated September 28, 2005 by and between Fagen, Inc. and Heron Lake BioEnergy, LLC†	Exhibit 10.12 of the Company’s 2008 Registration Statement.
10.13	Distiller’s Grain Marketing Agreement dated October 5, 2005 by and between Heron Lake BioEnergy, LLC and Commodity Specialist Company as assigned to CHS Inc. as of August 17, 2007	Exhibit 10.13 of the Company’s 2008 Registration Statement.
10.14	Ethanol Fuel Marketing Agreement dated August 7, 2006 by and between RPGM, Inc. and Heron Lake BioEnergy, LLC	Exhibit 10.14 of the Company’s 2008 Registration Statement.
10.15	Letter Agreement re: Environmental Compliance Support dated March 12, 2007 by and between Fagen Engineering, LLC Heron Lake BioEnergy, LLC	Exhibit 10. 15 of the Company’s 2008 Registration Statement.
10.16	Coal Loading, Transport, and Delivery Agreement effective as of April 1, 2007 by and between Tersteeg Transport Inc. and Heron Lake BioEnergy, LLC	Exhibit 10.16 of the Company’s 2008 Registration Statement.
10.17	Coal Transloading Agreement dated June 1, 2007 by and between Southern Minnesota Beet Sugar Cooperative and Heron Lake BioEnergy, LLC†	Exhibit 10.17 of the Company’s 2008 Registration Statement.
10.18	Master Coal Purchase and Sale Agreement dated June 1, 2007 by and between Northern Coal Transport Company and Heron Lake BioEnergy, LLC, including confirmation letter dated July 13, 2007†	Exhibit 10.18 of the Company’s 2008 Registration Statement.
10.19	Loan Agreement dated December 28, 2007 by and between Federated Rural Electric Association and Heron Lake BioEnergy, LLC	Exhibit 10.19 of the Company’s 2008 Registration Statement.
10.20	Secured Promissory Note issued December 28, 2007 by Heron Lake BioEnergy, LLC as borrower to Federated Rural Electric Association as lender in principal amount of $600,000	Exhibit 10.20 of the Company’s 2008 Registration Statement.
10.21	Security Agreement dated December 28, 2007 by Heron Lake BioEnergy, LLC in favor of Federated Rural Electric Association	Exhibit 10.21 of the Company’s 2008 Registration Statement.
10.22	Electric Service Agreement dated October 17, 2007 by and between Interstate Power and Light Company and Heron Lake BioEnergy, LLC	Exhibit 10.22 of the Company’s 2008 Registration Statement.
10.23	Shared Savings Contract dated November 16, 2007 by and between Interstate Power and Light Company and Heron Lake BioEnergy, LLC	Exhibit 10.23 of the Company’s 2008 Registration Statement.
10.24	Escrow Agreement dated November 16, 2007 by and between Heron Lake BioEnergy, LLC , Farmers State Bank of Hartland for the benefit of Interstate Power and Light Company	Exhibit 10.24 of the Company’s 2008 Registration Statement.
10.25	Employment Agreement dated February 1, 2008 by and between Heron Lake BioEnergy, LLC and Robert J. Ferguson *	Exhibit 10.25 of the Company’s 2008 Registration Statement.
10.26	Services Contract dated March 1, 2007 by and between Heron Lake BioEnergy, LLC and Gerber & Haugen, P.L.L.P. relating to the services of James A. Gerber *	Exhibit 10.26 of the Company’s 2008 Registration Statement.
10.27	Letter Agreement dated February 28, 2008 by and between Heron Lake BioEnergy, LLC and Gerber & Haugen, P.L.L.P. relating to the services of James A. Gerber *	Exhibit 10.27 of the Company’s 2008 Registration Statement.

Exhibit Number	Exhibit Title	Incorporated by Reference To:
10.28	Compliance Agreement effective January 23, 2007 by and between Heron Lake BioEnergy, LLC and the Minnesota Pollution Control Agency	Exhibit 10.28 of the Company's 2008 Registration Statement.
10.29	Unit Transfer Policy of Heron Lake BioEnergy, LLC dated November 2008	Exhibit 4.1 to Current Report on Form 8-K dated November 5, 2008.
10.30	Letter Agreement dated November 25, 2008 by and between Heron Lake BioEnergy, LLC, CFO Systems, LLC and Brett L. Frevert relating to the services of Brett L. Frevert *	Exhibit 10.1 to Current Report on Form 8-K dated November 26, 2008.
10.31	Ethanol Purchase and Marketing Agreement dated September 2, 2009 by and between Heron Lake BioEnergy, LLC and C&N Ethanol Marketing Corporation.	Exhibit 10.1 to Current Report on Form 8-K dated September 2, 2009.
10.32	Amendment No. 4 to Fifth Supplement dated December 8, 2009 by and between Heron Lake BioEnergy, LLC and AgStar Financial Services, PCA	Attached hereto.
21.1	Subsidiaries of the Registrant	Exhibit 21.2 of the Company's 2008 Registration Statement.
31.1	Certification of Chief Executive Officer (principal executive officer) pursuant to Rules 13a-14(a) and 15d-14(a) of the Exchange Act.	Attached hereto.
31.2	Certifications of Chief Financial Officer (principal financial officer) pursuant to Rules 13a-14(a) and 15d-14(a) of the Exchange Act.	Attached hereto.
32	Certification pursuant to 18 U.S.C. § 1350.	Attached hereto.

* Indicates compensatory agreement.

† Certain portions of this exhibit have been redacted and filed on a confidential basis with the Commission pursuant to a request for confidential treatment under Rule 24b-2 of under the Exchange Act. Spaces corresponding to the deleted portions are represented by brackets with asterisks [* * *].

AMENDMENT NO. 4 TO
FIFTH SUPPLEMENT
TO THE MASTER LOAN AGREEMENT
(REVOLVING LINE OF CREDIT LOAN)

This Amendment No. 4 to the Master Loan Agreement (Revolving Line of Credit Loan) (this " **Amendment** ") is effective as of December 8, 2009, by and between **HERON LAKE BIOENERGY, LLC** , a Minnesota limited liability company (" **Borrower** ") and **AGSTAR FINANCIAL SERVICES, PCA** (" **Lender** ").

RECITALS

A. Lender has extended various credit facilities to Borrower for the purposes of acquiring, constructing, equipping, furnishing and operating an ethanol production facility in Jackson County, Minnesota, pursuant to that certain Fourth Amended and Restated Master Loan Agreement dated as of October 1, 2007, as the same may be amended, supplemented, modified, extended or restated from time to time (the " **MLA** "); that certain Third Supplement to the Master Loan Agreement (Term Loan) dated as of October 1, 2007, as the same may be amended, supplemented, modified, extended or restated from time to time (the " **Third Supplement** "); that certain Fourth Supplement to the Master Loan Agreement (Term Revolving Loan) dated as of October 1, 2007, as the same may be amended, supplemented, modified, extended or restated from time to time (the " **Fourth Supplement** "); and that certain Fifth Supplement to the Master Loan Agreement (Revolving Line of Credit Loan) dated as of November 19, 2007, as amended by that certain Amendment No. 1 to Fifth Supplement to the Master Loan Agreement dated November 17, 2008, as further amended by that certain Amendment No. 2 to Fifth Supplement to the Master Loan Agreement dated February 1, 2009, and as further amended by that certain Amendment No. 3 to Fifth Supplement to the Master Loan Agreement dated May 29, 2009, as the same may be amended, supplemented, modified, extended or restated from time to time (collectively, the " **Fifth Supplement** "). The MLA, Third Supplement, Fourth Supplement and Fifth Supplement are referred to collectively hereinafter as the " **Loan Agreement** ").

B. Borrower has requested that Lender extend the maturity date of the Revolving Line of Credit Loan, and Lender has agreed to such extension upon the terms and conditions set forth herein.

C. Unless otherwise expressly defined herein, capitalized terms used herein shall have the same meaning ascribed to them in the MLA or the Fifth Supplement, as applicable.

AGREEMENT

NOW, THEREFORE, in consideration of the premises herein contained, and for other good and valuable consideration, the receipt and sufficiency of which are hereby acknowledged, the parties hereto herby agree as follows:

1. **Amendment to Fifth Supplement .** Section 1: The following defined term in the Fifth Supplement is hereby amended and restated to read as follows:

" Revolving Line of Credit Loan Maturity Date " shall mean February 1, 2010.

2. **Representations and Warranties .** Borrower hereby represents to Lender that, after giving effect to this Amendment:

(a) All of the representations and warranties of Borrower contained in the MLA and in each other Loan Document are true and correct in all material respects as though made on and as of the date hereof.

(b) As the date hereof, except as otherwise specifically stated herein, no Event of Default has occurred and is continuing.

3. **Miscellaneous .**

(a) Effect; Ratification . The amendments set forth herein are effective solely for the purposes set forth herein and shall be limited precisely as written, and shall not be deemed to (i) be a consent to, or an acknowledgment of, any amendment, waiver or modification of any other term or condition of the Loan Agreement or (ii) prejudice any right or remedy which Lender may now have or may have in the future under or in connection with the Loan Agreement, as amended hereby, or any other instrument or agreement referred to therein. It is further understood and agreed by and between the Borrower and the Lender that all other terms and provisions of the Loan Agreement shall remain in full force and effect, enforceable by the Lender against the Borrower as fully as though no amendments had been made hereby, and this Amendment shall not be deemed to hinder, compromise or lessen the enforceability of the Loan Agreement, the Notes, or any mortgage, security interest, or guaranty securing repayment of the Loans, in any way. Each reference in the Loan Agreement and in any other Loan Document to the "Fifth Supplement" shall mean the Fifth Supplement, as amended hereby.

(b) Loan Documents . This Amendment is a Loan Document executed pursuant to the MLA and shall be construed, administered and applied in accordance with the terms and provisions thereof.

(c) Defined Terms . All terms used and not otherwise defined herein shall have the meanings assigned to them in the MLA or the Fifth Supplement, as applicable.

(d) Counterparts . This Amendment may be executed in any number of counterparts, each such counterpart constituting an original and all of which when taken together shall constitute one and the same instrument.

(e) Severability . Any provision contained in this Amendment which is held to be inoperative, unenforceable or invalid in any jurisdiction shall, as to that jurisdiction, be inoperative, unenforceable or invalid without affecting the remaining provisions of this Amendment in that jurisdiction or the operation, enforceability or validity of such provision in any other jurisdiction.

(f) GOVERNING LAW . THIS AMENDMENT SHALL BE GOVERNED AND CONSTRUED IN ACCORDANCE WITH THE LAWS OF THE STATE OF MINNESOTA.

(g) WAIVER OF JURY TRIAL . THE BORROWER AND THE LENDER HEREBY IRREVOCABLY WAIVE ALL RIGHTS TO TRIAL BY JURY IN ANY ACTION, PROCEEDING OR COUNTERCLAIM ARISING OUT OF OR RELATING TO ANY LOAN DOCUMENT TO WHICH IT IS A PARTY OR ANY INSTRUMENT OR DOCUMENT DELIVERED THEREUNDER.

{SIGNATURE PAGE FOLLOWS}

**SIGNATURE PAGE TO
AMENDMENT NO. 4 TO
FIFTH SUPPLEMENT TO THE MASTER LOAN AGREEMENT
(REVOLVING LINE OF CREDIT LOAN)
BY AND BETWEEN
HERON LAKE BIOENERGY, LLC
AND
AGSTAR FINANCIAL SERVICES, PCA
DATED AS OF: December 8, 2009**

IN WITNESS WHEREOF, the parties hereto have caused this Amendment to be executed and delivered by their respective duly authorized officers as of the date first written above.

BORROWER:

HERON LAKE BIOENERGY, LLC,
a Minnesota limited liability company

By: /s/ Robert J. Ferguson
Robert J. Ferguson
Its: President

LENDER:

AGSTAR FINANCIAL SERVICES, PCA,
a United States corporation

By: /s/ Mark Schmidt
Mark Schmidt
Its: Vice President

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EXHIBIT 31.1

CERTIFICATIONS

I, Robert J. Ferguson, certify that:

1. I have reviewed this Form 10-K of Heron Lake BioEnergy, LLC.

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation;

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: January 29, 2010

/s/ Robert J. Ferguson
Robert J. Ferguson
Chief Executive Officer
(principal executive officer)

CERTIFICATIONS

I, Brett L. Frevert, certify that:

1. I have reviewed this Form 10-K of Heron Lake BioEnergy, LLC.

2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;

3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;

4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:

   (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;

   (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;

   (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and

   (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting.

5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):

   (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

   (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: January 29, 2010

/s/ Brett L. Frevert
Brett L. Frevert
Interim Chief Financial Officer
(principal financial officer and principal accounting officer)

CERTIFICATION

The undersigned certifies pursuant to 18 U.S.C. §1350, that:

(1) The accompanying Annual Report on Form 10-K for the period ended October 31, 2009 fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and

(2) The information contained in the accompanying Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: January 29, 2010

/s/ Robert J. Ferguson
Robert J. Ferguson
Chief Executive Officer
(Principal executive officer)

/s/ Brett L. Frevert
Brett L. Frevert
Interim Chief Financial Officer
(Principal financial officer and principal accounting officer)