



## **Submission to the Senate Standing References Committee on Rural Affairs & Transport in Relation to an Inquiry into an Examination of the Foreign Investment Review Board National Interest Test**

This submission is made by TFS Corporation (TFS) with particular reference to paragraphs (i) (ii) (v) (vi) and (vii) of the terms of reference of this Inquiry. In addition some comment is made on ways of improving the transparency of decisions made by the FIRB under the National Interest Test.

### **TFS Corporation (TFS)**

TFS is a publicly-listed company that has sandalwood plantations in the East Kimberley region and a processing plant at Mount Romance in Albany in Western Australia's South West. The plantation in the North is Indian sandalwood (*Santalum Album*) whilst the sandalwood processed in the South West is native Australian Sandalwood (*Santalum Spicatum*).

TFS is the major grower of plantation Sandalwood in the Ord River Irrigation Area (ORIA). We estimate that approximately 80% of the Sandalwood under plantation in the ORIA is managed by TFS. The most mature of the trees will be harvested in 2012/13 in the East Kimberley. These are the world's largest Indian Sandalwood plantations.

Through Mt Romance, TFS operates tourist attractions and retail outlets in Albany, Kununurra and Broome. These venues play an important role in educating visitors on the significance of the Sandalwood industry to Western Australia.

Sandalwood and its oil are in great demand in both Asia and the Middle East, because of a lack of established domestic supply which has caused significant export opportunities for Australia. Indian sandalwood oil retails for up to \$3m a tonne making it a very valuable but compact export product. On average a sandalwood tree takes 15 years to harvest. As it requires mutation from adjacent host trees it is very different to annual monoculture crops.

TFS has experienced continual growth and in 2009 TFS entered the Forbes Asia Pacific's "Best Under a Billion" which recognizes the top 200 companies in the region with revenue under \$1-billion. It is the second largest private employer in Kununurra after Argyle Diamonds and is also one of the largest employers in Albany through Mt Romance.

Whilst it started as a Managed Investment Scheme (MIS) TFS has substantially moved away from this model. The TFS Group has broadened its income base to include non-MIS sources.

In fact, revenues from MIS sources made up approximately 40% in the 2010 financial year and were less than 10% of revenues for 2011. Whilst revenue from MIS sources made up approximately 40% of total revenue in FY 2010, the figure was less than 10% in FY 2011.

TFS has recently received foreign investment of over \$65-million from a Middle Eastern Sovereign fund and a AAA rated US based institution. Five year options are in place with both institutions and could amount to a further \$270-million of investment if exercised. Unfortunately such sources of funding are not readily available in Australia and as a result to ensure a continuity of funding companies such as TFS have and will continue to rely on opportunities off shore.

### **Community Involvement**

Since 2005 Mt Romance and global cosmetic brand AVEDA have worked with Indigenous members of the Songman Circle of Wisdom to create an indigenous plant certification protocol. Under the program sustainable business partnerships are formed with Aboriginal harvesters who obtain from the Government licences to collect sandalwood. A royalty from the product is then paid to them on the oil sold from their wood. TFS is a proud foundation sponsor of the Clontarf East Kimberley Football Academy which is part of the Gerard Neesham program in Perth. This is a nationally recognized initiative dealing with indigenous education.

TFS has recently funded a feasibility study by Notre Dame University for tertiary and vocational education for on-country management. This would be available for the broader community but particularly indigenous students. The University is considering this initiative and TFS is looking to partner this. Importantly this would improve management of the natural resources relating to the Kimberley.

TFS has also signed a MOU with Mirriwung Gajerrong (MG) Corporation to create of a Joint Venture company to jointly own and manage 1,000 hectares in the ORIA. TFS will assist MG Corporation in creating opportunities and benefits for the Miriuwung and Gajerrong people by providing expertise in land selection and technical support in the areas of agronomy, forestry and land preparation.

As part of its engagement with India TFS recently established the Natural Origin Recognition Protocol (NORP), a program designed to recognize the link between the Indian Sandalwood species that we grow in Australia and its traditional owners in India. NORP aims to promote energy independence, education and economic development in rural India. A combination of initiatives including the promotion of education, democratic process and access to clean water will be undertaken, with the aim of stimulating cottage industries like soap-making in these villages. Former Australian test cricketer and TFS Global Ambassador, Adam Gilchrist together with the Australian High Commissioner to India Peter Varghese launched the project in Rajasthan last year. This project enjoys the support of the Australian Government.

## **The Indian Market for Sandalwood**

Trade in Sandalwood began thousands of years ago. Historically India supplied over 90% of the world's Indian Sandalwood (*Santalum album*), with volumes estimated to be more than 20,000 tonnes of heartwood production per annum. Indian Sandalwood oil was exported internationally for use in the global fragrance market and has wide use in India's domestic industries such as toiletries, pan masala, attar and medicines. The wood also has both cultural and religious applications, being an important ingredient for worship (puja) and for cremation where it is used to lift the spirits to heaven.

Over-harvesting and disease have resulted in dwindling wild supplies in India. Since 1994 Indian Sandalwood (*Santalum album*) has been recognized as vulnerable by the World Conservation Union's Threatened Species Redlist. This has impacted upon many parts of India where local industries attached to the Sandalwood trade have suffered. Artisans (who create carvings and deities using Sandalwood), Sandalwood processors and attar manufacturers have been most severely impacted.

Australia is potentially a critical source of supply for the large Indian and Chinese markets where rising standards of living are increasing demand for a wide range of sandalwood products from Australia. Economic opportunities could be created for these industries by supplementing dwindling domestic supply with plantation-grown material imported from Australia.

TFS is currently in discussions with both the Indian and Australian Governments on how this trade can be accommodated in the current Free Trade talks between the two countries.

## **The Market for Australian Sandalwood**

Apart from some export overseas Australian Sandalwood (*Santalum spicatum*) is processed by MRA and used for cosmetic and lifestyle products which are sold through retail outlets in Australia. In particular TFS has outlets in Kununurra, Broome and Albany.

Australian Sandalwood in WA is harvested both privately and by the Forest Products Commission. Private harvesters involve a significant percentage of Aboriginal Communities who have had extensive experience in this area. The harvesting of Australian Sandalwood in WA goes back to around 1838 and is one of the State's oldest industries.

In both cases the annual harvest is regulated by the WA Department of Environment and Conservation and is capped annually.

(i) **How the test was applied to purchases of Australian agricultural land by foreign companies, foreign sovereign funds and other entities in the past 12 months;**

The FIRB has consistently taken the view that TFS's agribusiness operations have been in the national interest and there have been a number of relevant transactions involving TFS.

Since May 2010, (which is 12 months prior to the referral of the Inquiry) TFS has made a number of announcements relating to foreign investment.

- a) On 26<sup>th</sup> May 2010 TFS announced that a AAA rated US based institution entered into an investment Management Agreement involving the acquisition of 182 hectares in the East Kimberley. This initial investment was valued at \$20M. With the exercise of all of the options the total investment would amount to around \$100M. A copy of the ASX Release is at Annexure 1. On the 7 June 2010 TFS issued a further ASX Release which announced FIRB approval (See Annexure 2). This transaction was settled on the 16<sup>th</sup> September 2010 (see Annexure 3).

Subsequently the same investor exercised a further option in relation to another 182 hectares. This is valued at around \$20M (see Annexure 4).

- b) On the 23 December 2010, TFS issued a Market Update announcing that there had not only been settlement with the US investor mentioned in (a) but it further announced other measures to attract foreign investment and overseas financing (see Annexure 5).
- c) On 19 January 2011, TFS announced a \$47M investment from a Middle Eastern Sovereign Wealth Fund with proceeds of \$27M being received. With the exercise of all options the total investment could amount to \$240M (see Annexure 6). The first option was exercised by this investor in June 2011 with proceeds of \$21M (see Annexure 7).
- d) Further to the foreign investment mentioned above TFS raised around \$150M in June 2011 in overseas finance. This will facilitate growth for TFS by providing for further land holdings and plantations (see Annexure 8).

In all the transactions there were numerous benefits to the company, its shareholders, the community and its investors.

In the current financial climate it is very difficult for any agribusiness to receive bank financing. Only last year TFS found itself in a critical situation because Australian banks would not fund its plans for growth. Overseas investment and financing will allow this, helping the company to execute its strategic plan with significant ongoing benefits for Australian employment and trade.

In its dealings with the FIRB, TFS has found the process to be thorough and professional.

iii) **The role of the Government, regulators and receivers, including their obligations under the Corporations Act 2001 and/or the Foreign Acquisitions and Takeovers Act 1975, including the role of the Australian Securities and Investments Commission, in upholding the test;**

TFS has found in all its dealing with the FIRB that careful consideration has been given by the FIRB during the processing of applications for approval. This has also extended to the Minister's office where Ministerial approval was required.

TFS's experience has demonstrated that the role of the FIRB and the Minister is an appropriate one and effective. It is necessary that the application of the national interest test should have flexibility to reflect the changing commercial and political landscape and therefore the changing national interest.

What is in the nation's interest today might not be so tomorrow. Commercial realities change as does the political landscape.

(iv) **The role of the foreign sovereign funds in acquiring Australian sovereign Assets;**

In the case of TFS any acquisition of land by overseas funds is the subject of an agreement with TFS to manage the investment. This includes plantation of trees, management of the plantation and harvesting. To this extent there is not only local content with labour and management but also a degree of control retained by an Australian company. TFS is a major employer in regional WA. It is the second largest employer in Kununurra and in Albany is one of the largest employers in the district. Another benefit that could flow from growth is the increased opportunity for Aboriginal communities in those regions.

The role of the overseas investor therefore does not involve any:

- control of TFS
- direction of management and;
- choice of market

TFS essentially has a duty to maximize a return to the investor and has autonomy on how this is done.

**(vi) How similar national interest tests are applied to the purchase of agricultural land and agri-businesses in countries comparable to Australia; and**

In New Zealand, foreign investment is screened by New Zealand's Overseas Investment Office (OIO) under the auspices of the Overseas Investment Act 2005. Government approval is required for purchases of land larger than 5 hectares (12.35 acres) and land in certain sensitive or protected areas, or fishing quotas. If the land or fishing quota to be purchased is owned by a company or other entity, approval will be required if the investor will be acquiring a 25% or more equity or controlling interest.

In 2011 the OIO introduced several factors designed to complement the existing factors and good character test. These factors are designed to evaluate the benefit to New Zealand.

The new factors include the Economic Interests factor to ensure New Zealand's economic interests are adequately safeguarded and promoted. A Mitigating factor has also been added to consider opportunities for New Zealand involvement such as local company Directors or the establishment of a local head office.

Whilst the transactions undertaken by TFS would comfortably meet the provisions in NZ, TFS believes that the system is too prescribed and cumbersome. This in turn would not create an attractive environment for foreign investment.

**(vii) Any other related matters; and**

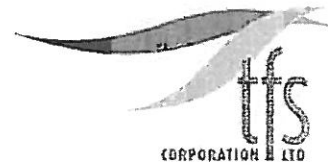
**Transparency of Decisions**

Whilst TFS would not support publication of applications for approval of foreign investment, it has no objection to a public register of land (particularly agricultural land) which is the subject of foreign investment.

Publicising an application for approval of foreign investment would deter investors and could have detrimental commercial consequences. The situation is quite different however once approval has been granted.

**Summary**

In summary foreign investment has had a positive result for investors and shareholders in TFS. This extends to the wider community, particularly so in regional WA. Without foreign investment TFS could not meet its strategy for growth. This in turn could deny future benefits for investors, shareholders and the regions in which it operates.



### ASX RELEASE

## AAA RATED US BASED INSTITUTION COMMITS TO TFS SANDALWOOD PLANTATIONS

26 May 2010

### Highlights

- AAA rated US based Institution enters into an Investment Management Agreement pursuant to which TFS will manage a 180 hectare Indian sandalwood plantation to be planted in FY10 .
- Investment by the Institution over the life of the plantation excluding performance bonuses to TFS anticipated to be circa \$20m.
- Secures option to plant an additional 180ha per annum for next 5 years to 2015 with this investment anticipated to be, approximately, \$100m if all options are exercised.

Australian agribusiness TFS Corporation (ASX: TFC) has signed a confidential Investment Management Agreement (IMA) with a US based institutional investor potentially worth \$120 million over six years. The IMA is subject to and conditional upon the settlement of a related land acquisition agreement with TFS. The land acquisition agreement is conditional on, amongst other things, the Investor obtaining Foreign Investment Board approval. Under the IMA TFS is paid an upfront payment for the purchase of land and establishment of the plantation, annual payments for plantation management, and a performance bonus upon a hurdle rate of return being achieved by the investor.

This investment is in addition to the recently announced (May 4) forecast of 500 hectares of Non-MIS sales, and puts TFS on track to sell over 500 hectares of Non-MIS in FY10 up over 40% on FY09 Non-MIS sales.

"This institutional investment continues the rapid and fundamental transformation of TFS from a company heavily reliant on yearly MIS sales and its associated income to one that will receive its investment and income from predominantly more stable institutional and private sector sources," TFS Executive Chairman Frank Wilson said.

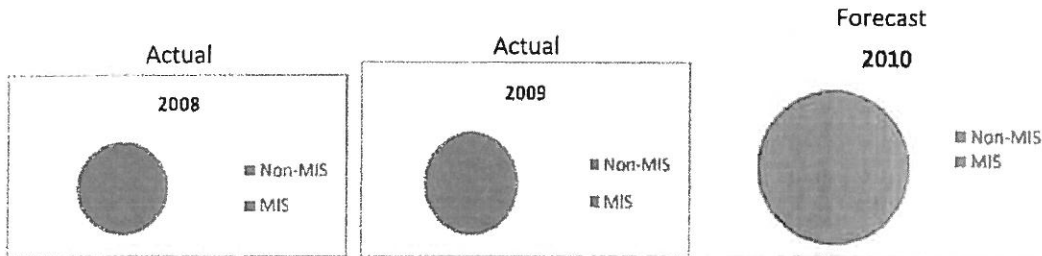
"Even in a tumultuous economic environment, TFS's forestry products continue to attract the support of leading global institutions and private investors by entering longer term investment agreements. This gives TFS the revenue stability to deliver on its strategy of becoming the world's leading integrated Sandalwood supplier."

"Our strategy to restructure our products to attract institutional investors has proven to be the right one in the wake of the MIS market fallout. Together with the continuing increase in profitability of our sandalwood processing arm Mt Romance, TFS is well positioned as our first Indian Sandalwood plantations are harvested in the next three years," Mr Wilson said.

Indian Sandalwood sits in the high return category compared to traditional hardwood and softwood products. The heartwood trades for in excess of \$110,000 per tonne on average, having risen at a compounding rate of over 18 per cent per annum over the past 18 years.

**Successful transition of business model**

The strategy put in place by the TFS Board and Management team in 2008 to transition the sales model to capture the global institutional forestry investment flows and reduce reliance on retail MIS investors is taking shape.



**Figure 1: Growth in TFS plantation sales since 2008 have been driven by Non-MIS investment.**

Global Institutional Forestry Investment accounts for annual investment flows of \$2.5 billion and Indian Sandalwood will now take its place as a high return category within this asset class. Following fluctuations across global markets, interest rates and currencies there is a growing institutional demand for investment into hard assets, and the TFS plantation investment fits neatly into that thematic.

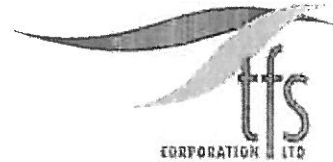
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**ASX RELEASE**

**FIRB APPROVAL OBTAINED**

07 June 2010

In a release dated 26 May 2010 TFS advised that it had entered into an Investment Management Agreement ("IMA") with a AAA rated US based Institution whereby TFS will manage a 180 hectare Indian sandalwood plantation to be planted in FY10.

The IMA is subject to and conditional upon the settlement of a related land acquisition agreement with TFS. The land acquisition agreement is conditional on, amongst other things, the Investor obtaining Foreign Investment Review Board approval.

TFS wishes to advise that Foreign Investment Review Board approval has been obtained.

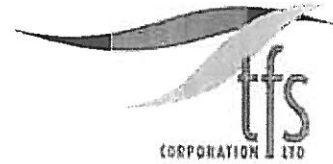
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**ASX RELEASE**

**US INSTITUTIONAL TRANSACTION SETTLES**

20 September 2010

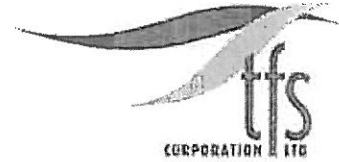
TFS is pleased to advise that the transaction announced on the 26 May 2010 with a AAA rated US based Institution settled on 16 September 2010.

A copy of the 26 May release is attached.

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**ASX RELEASE**

**US INSTITUTION EXERCISES FIRST OPTION**

06 December 2010

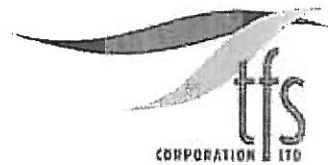
TFS is pleased to advise the AAA rated US investor which settled its initial plantation investment of 182 ha on 16 September 2010 has exercised its first option and will plant a further 182 ha in FY 2011.

Investment by the institution for the additional 182 ha over the life of the plantation excluding performance bonuses to TFS is anticipated to be circa \$20m.

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**ASX RELEASE****MARKET UPDATE**

23 December 2010

TFS advises that final agreements for a 376 hectare plantation investment with an institutional foreign investor were executed on 22<sup>nd</sup> December 2010. Settlement of the investment is subject only to the investor obtaining Foreign Investment Review Board (FIRB) approval, and will occur within 2 business days of FIRB approval being granted. The investment is being made via a passive investment in a unit trust. At settlement TFS will receive initial proceeds of approximately \$26m (including GST) and over the life of the project a further \$13m in annual management and investment service fees. In addition TFS is entitled to receive performance fees upon certain hurdle rates of return being achieved by the investor. The investor will also be placing \$9.6m with TFS for investment in the secondary market for MIS Indian sandalwood grower woodlots.

On the back of this transaction TFS is pleased to announce that Clarkson Investment Services (DIFC) Ltd (Clarksons) regulated by the Dubai Financial Services Authority has accepted a mandate from TFS to raise \$75m for TFS through the issuance of new debt. Clarksons are highly confident they will complete this transaction in the 1Q, 2011 after having undertaken due diligence on TFS for the past two months.

Clarksons is a boutique natural resources focused investment bank based in Dubai. Its team members have raised total capital in excess of \$40bn. Clarksons is the wholly owned subsidiary of Clarkson, PLC, the world's premier integrated maritime services provider that is listed on the London Stock Exchange.

Part of the funds raised will be applied to retire all existing bank debt with the Commonwealth Bank of Australia (CBA) which will stand at circa \$30m after the settlement with the foreign investor.

TFS expects to use the balance of the funds from the new Debt issue (circa \$45m) for potential land acquisitions and other expansion opportunities.

After the settlement total cash proceeds year to date from institutional plantation investors and gross cash inflows from existing Mt Romance processing operations and other operations will be circa \$50m. Based on expected institutional plantations settlements in the 2H of FY2011 TFS expects its total net after tax positive operating cash flow to be circa \$70m in FY11.

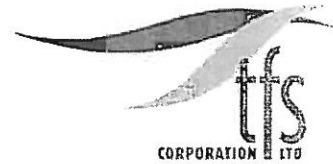
Given the size and significance and imminent timing of the settlement, the TFS board believes it is prudent to defer the payment of the final year dividend to coincide with this settlement. Accordingly the final year dividend will now be paid shortly after settlement and is therefore expected to be paid no later than 31 January 2011. The dividend record date will remain the same.

In addition TFS is pleased to note that it continues to receive significant demand from international institutional investors for its Indian sandalwood plantation investment. This includes a AAA rated USA investor who has recently exercised its option for a second investment in FY11. TFS has a number of other significant institutional transactions that will be announced in 2H FY11 that are nearing their final stages of due diligence and completion.

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**ASX RELEASE****MARKET UPDATE**

19 January 2011

TFS is pleased to advise that a \$47m plantation investment by a middle eastern sovereign wealth fund, referred to in ASX release 23 December 2010 has settled with initial proceeds of approximately \$27m (inclusive of GST) received. A further \$13m in annual management and investment service fees will be received by TFS over the life of the investment, plus an additional \$9.6m has been allocated to the purchase of MIS grower woodlots in the secondary market.

The settlement occurred post the receipt of formal approval from the Foreign Investment Review Board (FIRB) as referred to in the December update.

The settlement of this transaction concludes a key transaction for TFS and reinforces the success of TFS' initiative to develop an institutional investment product for the wholesale market. It is worth noting that arrangements with this investor also include a 5 year option and, if all options are exercised the total investment by the sovereign wealth fund over the life of the project, excluding performance fees and the direct investment into secondary market purchases of MIS Indian Sandalwood grower woodlots will be approximately \$240m.

The settlement of this transaction along with two rounds of investment from a AAA rated US investor, provide a strong foundation for the continued success of this new business segment and global recognition of the sound fundamentals underpinning TFS' Indian Sandalwood business.

The settlement of this transaction also reflects the conclusion of all structural issues enabling ease of foreign investment into plantations managed and owned by TFS. Subsequently, the timing of the receipt of funds should in general now be aligned with the sales and planting cycle, such that the strong underlying cash flows of TFS will become transparent for the investment community.

TFS has a very strong pipeline of institutional investor interest which forms the back drop to TFS' recent FY11 forecast of circa \$70m at the operating cash flow line.

As referred to in the December update, part of the proceeds from this settlement will be applied to paying down bank debt to circa \$33m.

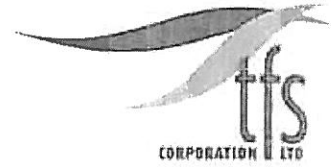
As the MIS market continues to be subdued, the wisdom of the TFS board and management to diversify its sources of investment flows to a more reliable and stable customer base becomes even clearer. In FY11, investment flows from the institutional market should again increase their prominence. TFS is exceptionally pleased that it has been able to grow its earnings through the GFC and the decline in the MIS sector. As noted in the AGM, TFS expects to increase its FY11 cash earnings again by at least 10%.

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**ASX RELEASE**

**MIDDLE EASTERN SOVEREIGN WEALTH FUND  
EXERCISES FIRST OPTION**

16 June 2011

TFS Corporation Ltd ("TFS") (ASX Code – TFC) is pleased to advise that a middle eastern sovereign wealth fund which settled its initial plantation investment of 376 ha in January 2011 has exercised its first option and signed an unconditional contract to plant a further 322 ha in FY 2011.

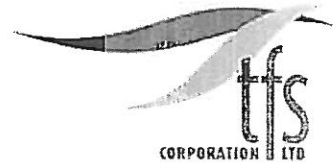
Approval has been received from the Foreign Investment Review Board (FIRB) and the initial proceeds of approximately \$21m (inclusive of GST) are expected to be received within 2 business days. A further \$12m in annual management and investment service fees will be received by TFS over the life of the investment, plus an additional \$10m has been allocated to the purchase of MIS grower woodlots in the secondary market.

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**ASX RELEASE**

**TFS COMPLETES RAISING OF US\$150 MILLION IN SENIOR SECURED NOTES**

23 June 2011

TFS Corporation Ltd ("TFS") (ASX code – TFC) today announced that its raising of US\$150 million of 11% Senior Secured Notes due 2018 (the "Notes") and Warrants ("Options") to purchase ordinary shares has been successfully completed.

TFS Executive Chairman Frank Wilson said the issuance of Senior Secured Notes and Warrants ("Options") to purchase ordinary shares at \$1.28 per share had been well supported by a number of major US, European and Asian investors who had identified TFS' strong position in the lucrative Indian Sandalwood market.

"The institutional support we have received is a great endorsement of TFS as the investors are participating in the future equity of the company at a substantial premium to the current market price," Mr Wilson said.

"Although the interest rate applied to the Notes is nominally higher than our previous facility with the CBA, the Notes provide more operating flexibility and certainty", Mr Wilson said.

Mr Wilson said the completion of the raising has secured funding for the company's long-term land pipeline which will provide the capacity to increase plantings for institutional investors and TFS itself.

"This will allow us to continue our track record of consistent earnings growth as we approach our first harvest when production based revenues are expected to be highly value accretive to shareholders," Mr Wilson said.

TFS is moving towards a business model where it will increase company plantation ownership over the next five years. This is the next step towards TFS' plan for vertical integration, where shareholders will benefit directly from the growing, processing and selling of sandalwood products.

With the company moving closer to its first harvest in 2013, TFS will have 5000 ha planted in the Ord River Irrigation Area, by the close of this years planting.

Currently about 50 per cent of the plantation trees are owned by MIS investors, with institutions owning 25 percent and TFS the remaining 25 per cent.

Mr Wilson said the company was confident of an increased level of plantation investment from overseas institutions, therefore it was important for TFS to boost its land holdings to ensure it was able to meet the anticipated investor demand.

Historically, TFS has relied on MIS investors to fund its growth, but over the last two years the Company has attracted new investment from a number of large international institutions. Only ten percent of its revenue is now derived from new MIS sales.

Mr Wilson said the growing number of global investors in TFS was due to the strong demand underpinning the Indian Sandalwood market, and the expectation that TFS will emerge as a major global supplier of oil and wood.

“We are receiving increased interest from the Middle East, the United States, and Europe with the TFS Beyond Carbon institutional investment product having already sold out for FY11 and now being distributed by a major European bank in FY12. ”

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