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FEA
GROUP OF COMPANIES

PARLIAMENTARY JOINT COMMITTEE ON CORPORATIONS AND FINANCIAL SERVICES

INQUIRY INTO AGRIBUSINESS MANAGED INVESTMENT SCHEMES

Forest Enterprises Australia Limited (FEA) welcomes the opportunity to provide a submission to this inquiry.

FEA is a member of the Australian Plantation Products & Paper Industry Council (A3P) and supports the joint submission of A3P and the National Association of Forest Industries to this Inquiry. FEA in this submission focuses on providing additional information drawing on our experience in managed forestry investments so to complement key issues addressed by the joint Industry submission.

About FEA

- FEA is an ASX-listed forestry and forest products company. Formed in 1985, it operates across the timber processing and agribusiness industries. The company's national marketing and corporate administrative functions are based in Launceston, Tasmania FEA's national forestry headquarters and business development division are based in Lismore, New South Wales. FEA owns a state-of-the-art timber mill and woodfibre processing facilities in Bell Bay, Tasmania.

- FEA has around 4,000 shareholders and currently employs around 210 people. In addition FEA currently engages a contract labour force of around 35 people at its Bell Bay Sawmill and approximately 300 contractor trading entities who supply forestry services – all in rural and regional areas.

- FEA Plantations Limited (FEA Plantations), a wholly owned subsidiary of FEA, commenced its first managed forestry investment project in 1993 and has issued 17 consecutive timber investment projects.

- FEA established its own and client hardwood eucalyptus plantations in Tasmania from 1987 and subsequently on mainland Australia, predominantly the northern rivers region of New South Wales.

- In recent years, FEA has expanded its business base to include sawmilling of plantation timber including plantation eucalypt that was originally planted for wood fibre exports. FEA produces the innovative branded sawn timber products, EcoAsh® and BassPine®, as well as exporting wood fibre under the SmartFibre® brand.

Managed Investment Schemes (MIS) are not unique to Agribusiness

- The scope and breadth of MIS as part of Australia's financial services industry goes well beyond just "Agribusiness MIS".

- A managed investment scheme is an entity in which individual investors pool their funds in order to achieve an economy of scale, as well as professional management, diversification and opportunity that would not otherwise be available to an individual investor.

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- There are some 4000 managed funds in Australia covering everything from Superannuation Funds, Life Insurance Offices, Unit Trusts or Managed Investment Schemes, with the latter including cash management trusts, fixed interest trusts, equity trusts, property trusts and agribusiness schemes, for example[1]. At March 2009, total consolidated assets of managed funds institutions was $1,169.0 billion, down from $1,194.7b in the December 2008 quarter, in superannuation funds, public unit trusts, life insurance offices and other managed funds[2].

- The agribusiness managed investment scheme (MIS) sector including horticulture and other agricultural businesses raised $1.1b last financial year with managed forestry investments forming around 63% of total inflows[3].

Recommendation

Investigations by this Joint Committee Inquiry should be undertaken in the context of the entire managed funds Industry, not just the agribusiness MIS sector. Moreover, taking into account experience from the broader managed funds industry may just reveal workable solutions to any specific concerns relating to agribusiness MIS, and managed forestry investments in particular.

The Sound Policy Framework Underlying Forestry MIS

- When considering agribusiness MIS schemes it is important to distinguish between the forestry and non-forestry sectors.

- There is a very sound public policy framework underpinning managed forestry investment arrangements, being the *Plantations for Australia: The 2020 Vision*

- The overarching principle of the *2020 Vision* strategy is to enhance regional wealth creation and international competitiveness through a sustainable increase in Australia's plantation resources, based on a notional target of trebling the area of commercial tree crops by 2020. The strategy was developed in the policy environment established by the Australian and State governments in the National Forest Policy Statement (1992). In July 1996, the Ministerial Council on Forestry, Fisheries and Aquaculture endorsed the plantation industry's target of trebling the plantation estate from 1.1 million hectares to 3 million hectares by the year 2020 [4].

- Demand for timber products continues to increase. Plantation forestry continues to expand to meet the demand for which their products are suited, at the same time as the available production area of public native forest decreases.
    - Australia's plantation estate increased by 4% in 2008 to just under 2 million hectares[5]
    - The total wood harvested in Australia, referred to as roundwood (log) removals, has steadily increased from 20 million cubic metres (m^3) per annum in 1997 to 28 million m^3 in 2008 despite a decline in native forest harvesting[5]

- MIS has proven to be the most effective structure to attract private investment in long-term plantation forestry[6], without the need for special incentives used in other countries or for other sectors. This is particularly so following the increased reservation of public native forests (taken out of production for conservation) and overall decline in state-owned forestry services which support industry development generally. That is, MIS by facilitating private-sector investment and growth in the forestry industry is filling the void left by the departure of public-sector supported

[1] RMIT University, Financial Services Tier1 Compliance Program – Managed Investments, 2008
[2] Australian Bureau of Statistics, 5655.0 Managed Funds, Australia Mar 2009, issued 28/5/09
[3] www.moneymanagement.com.au/article/Agribusiness-MIS-inflows-to-plummet/481709.aspx 18 May 2009
[4] Plantations for Australia: The 2020 Vision. *A Progress Report by the 2020 Vision Partners November 2008*
[5] Australian Bureau Agriculture and Resource Economics (ABARE) *Australian Forest and Wood Products Statistics Sept and Dec 2008*

forest managers. Importantly this is significantly on private property compared to State forest or crown land.

- In 2008 managed forestry investment projects accounted for 81% of all new timber plantations, and a substantial and increasing proportion of replanting, including on land managed by superannuation funds and State Governments. From about 5% in 1997, MIS-funded plantations now account for 34% of the total national plantation estate of 1.97 million hectares[6].

- Plantations from managed forestry investments are providing significant employment in rural and regional Australia[7], particularly important at a time when Australia is facing rising levels of unemployment.

- Plantations from managed forestry investments have so far directed about $6 billion of investment into regional areas (plantation establishment, management, harvesting, haulage, etc) and urban areas (export facilities, processing, transport etc)[8].

- Plantations from managed forestry investments are often portrayed by industry detractors as a threat to agricultural land, but this is unfounded in the national context. Plantations account for 0.25% of land use in Australia, while agriculture accounts for 60% of land use.[5] Cropping and horticulture occupy some 15 times the area established to forest plantations.[6]

- The domestic and export processing industries in regional Australia are increasingly dependent on plantations from managed forestry investments for their consistent long-term wood supplies. These plantations are now creating the scale of resource to maintain future wood supply to existing facilities and to underpin investment in new and upgraded facilities.

- Australia's total log harvest continues to increase consistently. The total native forest harvest is declining and for most of this decade has reduced at an annual rate of 3.7% from over 10 million m^3 to about 8.8 m^3 in 2008. This has been replaced by a large increase in hardwood plantation harvest from less than 1 million m^3 to 4.6 million m^3 in 2008.This significant increase in hardwood plantation harvest is partially the result of the increase in MIS eucalypt plantations starting to reach maturity.[5] The proportion that will be from plantations established under the MIS structure will increase rapidly over the next five years regardless of the final outcome of the Timbercorp and Great Southern administrations.

Recommendation

The full suite of issues that contributed to the demise of Timbercorp and Great Southern should rightly be fully investigated, so that Government, regulatory bodies and the agribusiness sector can work together to minimise a recurrence of the likely losses confronting investors in these companies.

However the focus must be on improvements to the regulatory environment around MIS Governance, including potential for improved co-regulatory measures, rather than this Inquiry being used as a platform for opponents who would seek to bring into question the sound policy basis of managed forestry investments and the plantation forestry industry generally.

Terms of Reference

1) Business models and scheme structures of MIS

FEA's Model

- FEA's business model is based on vertical integration across the entire value-chain to produce branded timber products. It is not driven by producing export woodchips.

[6] Bureau of Rural Sciences (BRS) *National Plantation Inventory 2009 Update*
[7] Bureau of Rural Sciences (BRS) *Socioeconomic Impacts of Plantation Forestry*
[8] Estimated regional economic impact provided by the Australian Plantation Products and Paper Industry Council (A3P) 2009.

- Over 23 years FEA has a proven track record in plantation forestry and processing and value adding of wood products. Managed forestry investments is an important financing pathway that builds economy of scale in a plantation estate that then directly supports downstream processing.

- In 2001-02 FEA further developed its strategic business model towards vertical integration by embarking on a process to diversify income streams, enhance our wood processing capabilities and to progressively rely less on annual woodlot sales from managed forestry investments.

- FEA currently has total freehold landholdings of approximately 94,500ha plus additional leasehold land. By 30 June this year, the total plantations under FEA's management will be approximately 70,000ha spread across approximately 600 properties on both freehold and leasehold land in Tasmania, Northern NSW, and South East Queensland. FEA also recently expanded its estate into the Douglas Daly region of the Northern Territory.

- Most of FEA's approximate 70,000ha of plantations under management constitute a range of native hardwood species with a small amount in Tasmania being softwood radiate pine. The high-value tropical species African Mahogany is now also being established on our Northern Territory operations.

- For FEA, plantations arising from managed forestry investments are not just about producing relatively low-value export woodchips. FEA's model is one where producing value-added timber products are our highest priority.

- Primarily targeting domestic construction markets, FEA currently processes around 350,000 tonnes per annum of plantation logs at its newly completed word class saw mill at Bell Bay, Tasmania; with hardwood timber products marketed under its EcoAsh® brand, and softwood products under the BassPine® brand. Residue wood fibre, and logs not suitable for saw milling, is marketed via FEA's joint venture SmartFibre export woodchip operation, also at Bell Bay.

- FEA's long term plan is to replicate this vertically integrated timber processing model in Northern NSW to complement our plantation estate in that region.

MIS Structures Generally

- MIS forestry is one of the most tightly regulated and scrutinised sectors in the Australian economy. Regulated by Chapter 5C of the *Corporations Act 2001*; various tax laws and the ATO Product Rulings program and financing guidelines; the 'promoter penalties' legislative provisions, Australian Financial Services Licence requirements, ASIC regulations and policy statements. ASX listing rules Privacy law, and Anti Money Laundering and Counter Terrorism Financing.

- A specific condition has been inserted in the AFSL for all Responsible Entity's of managed forestry investments, designed to protect the interests of the investors in the underlying land used in the project.

    - This condition requires that the RE must secure the land within a set time after issuing the interest in the scheme to the investor, or must offer the investor a refund.

    - The condition requires that each investor's interest must be registered beneficially on the land title, as a covenant so that the investor's rights to the trees on that land are protected in the event of any transfer of the ownership of the land.

- Every managed forestry investment company has to be (or has to engage) an ASIC-registered 'Responsible Entity (RE)', which must be issued with an Australian Financial Services Licence (AFSL). In the case of FEA, a wholly owned subsidiary, FEA Plantations Limited (FEA Plantations) (ABN 44 055 969 429) is RE and AFSL holder for all 17 managed forestry investment projects. With minor exceptions this requirement for a RE is common to all managed funds making offers to the general public and is not unique to agribusiness.

FEA's Managed Forestry Investment Project Structure

- An overview of the structure that applies to FEA's managed forestry investment projects are provided in ***Attachment 1***. Further information on the current *FEA Plantations Project 2009*, including Product Disclosure Statements and all supporting materials is available at www.fealtd.com.

- *Structure* - The structure of *FEA Plantations Project 2009* was changed from our previous projects, in light of the outcomes of the 2006 Australian Government review into Forestry MIS which came into effect in July 2008. These new arrangements among other things introduced extra conditions in Div 394 of *ITAA 1997* requiring the MIS company to plant all the trees within 18 months, and to demonstrate to the ATO that at least 70% of the funds collected will be for 'direct forestry expenditure' (DFE) over the life of the project. This DFE excludes expenses such as marketing and commission. In addition the changes introduced as part of the plantation tax review also enable forestry MIS investors to sell their plantation investment after four years, hence creating greater liquidity in the investment.

  These arrangements maintained recognition for the fact that forestry plantations are fundamentally a long term crop, as compared to annual horticultural crops. Forestry has an extended period between outlaying establishment costs and the generation of a return on this investment from thinning and clear fall harvests.

  FEA's project structure ensures that a separate legal entity, and separate public company, being FEA Plantations Limited, is the RE under the Corporations Act for any projects registered under the MIS arrangements.

- *A Focus on Forestry Expertise* - Plantation management expertise is contracted to the parent company, FEA, which is a highly experienced operational forestry company and forest product processor. FEA has been establishing eucalypt plantations since 1987 on its own account and for others. It's highly experienced national forestry team includes over thirty tertiary qualified professionals in Forestry, agricultural science, environmental management, natural resource management, surveyors as well as other administration and field technicians. In addition FEA engages a wide range of contract businesses supplying specialist forestry management skills from mapping, quality control, soil surveys to plantation inventory assessors. FEA does not outsource plantation land acquisition, planning and management services.

- *Management Fees* - Between 1993-2002 FEA Plantations adopted a recurrent fee model. Since 2003 a deferred fee model has been adopted, largely as a necessity to stay competitive in the financial services market and to keep pace with apparent investor preferences. Both fee models have their merits. However on a cash-flow basis from a manager's perspective being able to match operational forestry expenditure with recurrent fee income is a much more logical approach. The DFE model also allows the manager to assess anticipated cashflows to ensure a successful plantation (silvicultural and production) outcome a precursor to achieving returns on investment.

  Our view is that a deferred fee model is sub-optimal and puts significant pressures on managers who do not have diversified revenue streams.

- *Financial Capacity* - FEA appreciates that a key issue for this Joint Inquiry is to examine the issues around the financial capacity of plantation investment managers. By way of example provided as ***Case Study 1*** is an edited excerpt from a statement by FEA to the Australian Securities Exchange of 27 May 2009, repeated in the Supplementary Product Disclosure Statement of the FEA Plantations Project 2009 of 16 June 2009. The full text is available at www.fealtd.com.

Recommendation

When it comes to business models and managed investment scheme structures, two key issues are:

1. *A project structure where management fees align with operational cash-flow requirements and this may need some flexibility depending on the type of Scheme, and*

2. *Managers or parent entities that have diversified revenue stream capacity.*

FEA welcomes further consideration by Government and Corporate Regulators of potential improvements that can be made in each regard.

2) The impact of past and present taxation treatments and rulings related to MIS

- In recent years MIS forestry has been responsible for between 80 - 90% of new plantings in Australia[4,6]. In the last National Plantation Inventory update[6] the proportion of Australia's plantation estate owned by managed investment schemes was 34% and was only second to those owned by Governments (including Joint Ventures) at 37%. With the Queensland public plantations possibly about to be sold the proportion of plantations under public management will reduce to about 26%.

- It is notable that several State Governments, whose plantation development was previously supported by Commonwealth-backed loan funds, have or are now considering the sale of these assets; for example as seen by the recent Queensland Government 2009 budget announcement and ongoing speculation regarding the NSW Government's intentions for its plantation estates. The main prospective buyers are presumably large international institutions with funding from sources that is "patient" capital.

- Because it is so capital intensive direct investment by corporate entities in planting trees is generally an unattractive proposition and generally lacks shareholder support. The difficulty most processors have in owning their own plantation forests is the dilemma Company Boards have in investing today's shareholders funds for returns that possibly different shareholders will receive at a future date some 10 – 30 years hence.

- The MIS forestry sector has demonstrated its success at mobilising a small proportion of Australia's total investment pool of largely urban funds into regional Australia for funding a wide range of enterprises. The large MIS plantation companies have professional forestry teams and contractors that are efficient and competent at establishing plantations on a large scale.

- Considered use of the tax system, as has occurred with the prepayment timing provisions and the DFE model, have been a successful mechanism to give tax revenue neutrality and also achieve desirable levels of new plantings. This recognises the long-term nature of forestry compared with virtually any other rural investment, its highly illiquid nature and its heavy taxation levels at harvest due to its once only harvest nature.

- The provisions under ITAA (division 394) recognise that companies need to be able to plan land, seedlings and contractor requirements without gambling on what investments may be made before they happen. There would be a disastrous impact on planting levels if the deductibility of establishment costs in year of expenditure was removed. Evidence of this can be seen by the disastrous effects on planting levels that occurred in Australia in the period 2002 -2003 as a result of the "Ralph Report" changes and the Treasurer's announcement in November 1999.

- Due to transition arrangements post the "Ralph Report" and the introduction of the GST, the impact on new plantation establishment levels was not fully expressed until 2002 – 2003. This is evidenced by the relatively low planting levels across the Industry in 2002-2004 of between 42,320 and 54,378 hectares for these years compared with a figure of about 80,000 ha per year to reach the notional 2020 Vision target[9]

- For optimal wood marketing, and to run an efficient and profitable timber processing business, it is vital FEA can enact strategies that ensure a smooth wood flow (or consistency in throughput) to processing facilities from the plantation resource. This all starts with the amount (area) and timing of plantation establishment. Provided in ***Case Study 2*** is an overview of the impact of what changing the MIS structure in 1999 meant for FEA's plantation resource and future wood marketing and timber processing.

[9] Taken from the Bureau of Resource Sciences (BRS) *National Plantation Inventory 2007*

- The change of view by the Commissioner of Taxation in 2007 in relation to whether agribusiness investors were "carrying on a business" of forestry or other agriculture, created uncertainty that has contributed to the current situation with two companies in administration.

- The uncertainty and the delays in the test case coming to Court plus inadequate transition arrangements have caused a falling off in investment activity, primarily in non-forestry MIS. For MIS forestry the inclusion of a separate division within ITAA 1997 created some certainty of tax treatment but with no consultation prior to the introduction of the 70% defined forestry expenditure concept there were difficulties in making this last minute concept operational.

- The changes also caused administrative delays within the ATO and obtaining necessary Product Rulings took very much longer than the 90 day target benchmark that has been suggested as reasonable. This meant that Product Rulings for new projects in 2009 were unreasonably overdue.

- The trade off for reintroduction of the prepayment provision in 2002 was that the manager is taxed on their gross receipts in the year in which the investor claims the deduction. This means that the receipt of income is returned as tax in an income year before the expenditure is incurred, which would have otherwise have been deductible to the manager. This so called tax symmetry has a potentially severe impact on cash flow and has probably also contributed to the current demise of MIS companies with less funds available to establish and manage their projects.

- This needs to be borne in mind in any proposals that might arise from this Joint Inquiry to increase investor security for their plantation investments. The current tax timing impacts critically on cash flows for the manager and further restriction on availability of funds will make this situation more severe. The timing of taxation of income to the manager should revert to the same imposed on most if not all other Australian businesses.

Recommendation

This Joint Inquiry in exploring improved Governance arrangements should note and take into account the fact that any changes in MIS structure have severe implications for future plantation resource and wood flows 12 -20 years into the future. This then impacts on investment into infrastructure and also into decisions about whether the wood is exported or the wood processed within Australia. Without continuity of wood flows, then investment in further processing, higher value products and therefore potential investor returns may be adversely affected.

3) Any conflicts of interest for the board members and other directors

- A transparent Governance structure is critical and the logical response for adequately addressing real or perceived concerns regarding conflict of interest and for fostering confidence in MIS arrangements more generally. FEA believes it has a robust model in this regard.

- The managed forestry investment project structure ensures that a separate legal entity, in our case being FEA Plantations Limited (FEA Plantations), is required under the Corporations Act to be the Responsible Entity (RE) and to issue the offer for investment or the Product Disclosure Statement. The RE must act in the best interests of grower investors and where a conflict arises, must give priority to the interests of growers over the interests of the RE (Sect 601FC, Corporations Act 2001).

- To ensure the RE and the growers interests are separated from the parent company, FEA Plantations (RE) has two external Directors, and two Directors drawn from the Parent Company FEA. As there is not a majority of external Directors on the FEA Plantations Board, there is also a separate Compliance Committee, which in FEA Plantation's example, has an external Chairman and two other external members.

- The Compliance Committee has the role of monitoring FEA Plantation's compliance plan, which has been lodged with ASIC. The compliance committee has the function of reporting to the RE on any breach of the Law involving any MIS project and any breach of the scheme's constitution. The compliance committee can report direct to ASIC if it is not satisfied with the RE's actions with regard to any matter reported by the compliance committee to the RE. (Sect 601JC) Compliance with the compliance plan is audited by registered company auditor within 3 months of the end of each financial year. (Sect 601HG)

- The FEA Group has both a *Corporate Governance Policy* and a *Conflicts of Interest and Related Party Transactions Policy*, which has been approved by both the FEA and FEA Plantations Boards and annually reviewed. The objectives of this policy framework is to:

  - Ensure the rights and interests of MIS investors and shareholders are treated fairly.

  - To provide a framework and systematic approach to adequately identify, manage and resolve situations where conflicts of interest may arise, or might be perceived to arise, in accordance with ASIC policy and the relevant provisions of the Corporations Act.

  - To provide a framework for related party transactions to ensure compliance with the Corporations Act and best practice.

  - To communicate FEA Group's position on conflicts of interest and related party transactions to investors, prospective investors and the public and to provide a defensible position if subject to external review.

- A register of significant transactions affecting investors woodlots is maintained and reviewed at FEA Plantations Board and Compliance Plan meetings as another mechanism to monitor this policy. This is audited annually.

Recommendation

The current structure of MIS arrangements is sound as long as,

1) *There are truly independent and external Directors on the Board of the Responsible Entity and the Compliance Committee;*
2) *Directors have sufficiently broad and practical experience and a range of skills in the product being promoted.*
3) *The RE has sufficient oversight of the financial resources available for the projects to ensure financial capacity for the projects and proper delivery of services to the projects.*

Any moves to establish a dual structure of RE and separate Trustee, as has been suggested by some commentators, would not necessarily achieve any better outcome or increased security for investors. This would only serve to delegate control to separate trustee companies and research houses, significantly add to costs of administering each Scheme, and avoid the real issue of ensuring that project structures adequately secure investor assets from the manager's (or Parent Entities) company assets, and hence separate liabilities in the unfortunate event of a corporate collapse.

4) Commissions, fees and other remuneration paid to marketers, distributors related entities and sellers of MIS to investors

- We note recent calls by the Investment and Financial Services Association to ban financial products that pay upfront and trail commissions to financial planners, which follow similar calls by the Financial Planners Association and consumer group Choice. FEA welcomes these statements and consequential examination of potential improvements, but considers that this is not just a matter for agribusiness MIS, but should be a considered for all financial products.

- Commentators often state that agribusiness commissions and marketing costs are high without comparing the costs for the marketing of other products. In the case of MIS forestry there is only one payment at the commencement of the investment. Many of the products that compete for the same investment dollar have trailing commissions back to the financial planner, who first introduced the financial planner to the particular investment. These multiplied over a similar period to a forestry crop rotation plus the starting commission are often comparable or greater than the once only commissions paid for MIS forestry.

- It should be noted that most financial planners and accountants selling agribusiness MIS and a wide range of other financial products are members of financial planning groups. These groups provide marketing, training and product advice to their network. As part of this service, they develop Approved Product Lists (APL). The financial planners and other advisers within the Group generally can only sell financial products listed on these APL's. Different groups undertake due diligence differently to come up with their APL's.

- In FEA's case all remuneration is negotiated with the dealer group and not with individual advisers.

Recommendation

Recognising that this issue is broader than agribusiness MIS, it would be appropriate for this Joint Inquiry in reviewing commissions, fees and other remuneration to "marketers" to do so in the context of all financial products so to achieve greater transparency and objectivity in the manner in which the investing public are advised about the fees and charges that apply when making any investment.

FEA is supportive of appropriate reforms that would facilitate greater consistency in approach and where commissions are spread over a period that reflects the long term nature of the plantation forestry investment. If all projects had a similar fee structure then the investor is investing in the expertise of the RE and its service providers and the size or timing of commissions is not a factor weighing on the investment decision.

5) The accuracy of promotional material for MIS, particularly information relating to claimed benefits and returns (including carbon offsets); 8) The performance of the schemes; and 10) Project returns and supporting information, including assumptions on product price and demand

- A considerable compliance and disclosure regime already regulates promotional material, and communication of scheme performance and returns. There are a number of ASIC guidelines to be complied with and any non-compliance or difference in interpretation could lead to ASIC questioning the promotional material or the PDS and changes being made.

- This current regime appears sufficient if fully complied with and enforced.

- FEA Plantations (as the RE) makes every effort to ensure all published statements are properly verified and maintains records recording the sources of material or statements made. Through an internal compliance protocol, overseen by the Compliance Officer, which is reported to the FEA Plantations Board every piece of marketing material is recorded and procedures signed off.

- Notwithstanding the limitations imposed by ASIC Regulatory Guide PS170 "Prospective Financial Information", FEA Plantations Limited is acutely aware that any disclosure of expectations about growth rates, yields, production costs and product prices must be reasonable, adequate and reliable.

- FEA Plantations discloses to grower investors and the market generally, actual or expected yields and returns for mature projects, and progressive growth rate and performance of current projects, through
    - Dedicated updates in its quarterly "Canopy" newsletter distributed to all investors and shareholders;
    - Annual Project (Progress) Reports to grower investors which comprise two reports, one by FEA's Manager, Forestry Services and the other by an expert Independent Forester; and

- Relevant information is also provided to Research Houses and disseminated through their particular reports.

This information is available on our web-site as well as in printed form. In addition disclosures are made in annual project materials, for example, provided in **Case Study 3** is an edited excerpt from the Supplementary Product Disclosure Statement of the FEA Plantations Project 2009.

- Of note is that FEA Plantations is tightly restricted in making forecasts under ASIC policy and all disclosure of performance comes with the proviso that past performance does not guarantee future performance.

- As a potential means to fostering improve investor education it is worth further Government and Corporate Regulators consideration towards a regime that encourages greater disclosure of past performance, as it directly reflects of the manager's capacity to achieve a successful plantation (silvicultural and production) outcome.

Recommendation

Promotional material and communications relating to MIS Projects are tightly controlled by ASIC and resulting project compliance regimes. Provided that the risks of investment in managed forestry investments are clearly disclosed, backed up by compliance and enforcement by regulators, this should lead to greater investor awareness and confidence.

9) The factors underlying the recent scheme collapses

- In examining the recent demise of Timbercorp and Great Southern it is vital for all involved to separate out any issues associated with the solvency of the manager (or parent entity) and solvency of the Schemes themselves. Whilst not mutually exclusive the underlying issues and hence any responses or improvements required, will most likely be quite different. It would appear that Forestry MIS projects of both Companies could still continue as going concerns, but this is highly dependent upon an alternate RE being willing to take on this role.

- An important consideration is the financial capacity and viability of the RE, revenue streams and related disclosure to the investor market. The question of deferred and recurrent fee models (discussed under Term of Reference 1) is particularly relevant here too.

- Another critical issue arising is the need to secure the assets of grower investors in the Scheme, and in particular the protection of investors land use tenure in light of the collapse or change in RE. Where land is leased for the establishment of plantations it should not be possible for a lessor to be able to terminate a Forestry Right or Lease immediately a RE or parent entity enters receivership. An area for improved regulation would be around ensuring lease instruments are unable to be terminated or otherwise removed prior to the terms of the scheme.

12) The need for any legislative or regulatory change

- FEA supports the commitment of the plantation forestry industry to work constructively with Government, Corporate Regulators and the financial planning sector to make any necessary improvements to the regulatory framework and Governance around the managed forestry investment sector.

Recommendation

An important issue for discussion will be clearly defining the actual outcomes required from improved compliance and disclosure, but in a way that provides for some flexibility in how it is achieved by individual promoters. A useful example in this regard is that of the ASX Principles of Corporate

Governance, which all listed Companies are required by the Exchange and market generally to verify their compliance with as part of their annual reporting. Importantly though there is some flexibility in what arrangements each Company puts in place to meet this "code" in practice.

FEA supports further discussion and development of a set of "principles" that if then applied under an appropriate co-regulatory regime would provide greater investor confidence in and industry governance of, managed forestry investment. For example principles that encompass the following:

- *Ensuring that client monies are appropriately administered by the RE in order to carry out the contracted plantation services of the project.*
- *Ensuring that the plantation investment company has a demonstrated financial capacity.*
- *Increased transparency and demonstrated reliability in information provided about specific managed forestry investments.*
- *More prominent disclosure of the risks inherent in agricultural enterprises and managed forestry investments.*
- *A consistent and transparent remuneration system for fees and commissions.*
- *Improved socio-economic and environmental information for investors about the forestry and forest products industry.*
- *Adoption of an enforceable code of conduct for the managed forestry investment industry, and mandatory reporting compliance with the code.*

In Conclusion

- This Inquiry is vitally important in the wake of the recent demise of two major agribusiness MIS companies, to minimise a recurrence of the likely losses confronting investors in those companies.
- Improving the governance arrangements around the administration of agribusiness MIS should rightly be the focus of Joint Inquiry, including potential improved co-regulatory measures, rather than this Inquiry being used as a platform for opponents who would seek to bring into question the sound policy basis of the *Plantations 2020 Vision*, Forestry MIS, and the plantation forestry industry generally.
- Given the relatively small scale of agribusiness MIS as compared to the substantial managed funds industry it is important that this Inquiry is undertaken in the context of, and drawing on the experience of, this broader financial services industry. In principle, further regulatory measures unique to Forestry MIS should be avoided as many of the matters under consideration have application across the whole financial services sector.
- Plantation forestry and downstream timber processing contributes significantly to regional employment and economic viability. The outcomes of this Joint Inquiry will play an important role in ensuring that significant private investment in plantations and downstream processing continues based on a consistent and reliable wood flow from a future plantation resource.
- FEA supports the joint submission to this Inquiry by Australian Plantation Products & Paper Industry Council and the National Association of Forest Industry. By providing examples of FEA's experience in managed forestry investments we reiterate that as a way forward, we support further discussion and development by Government, Regulators and the plantation forestry industry of a set of "principles" that if then applied under an appropriate co-regulatory regime, would provide greater investor confidence in and industry governance of, managed forestry investment arrangements.

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Appendices

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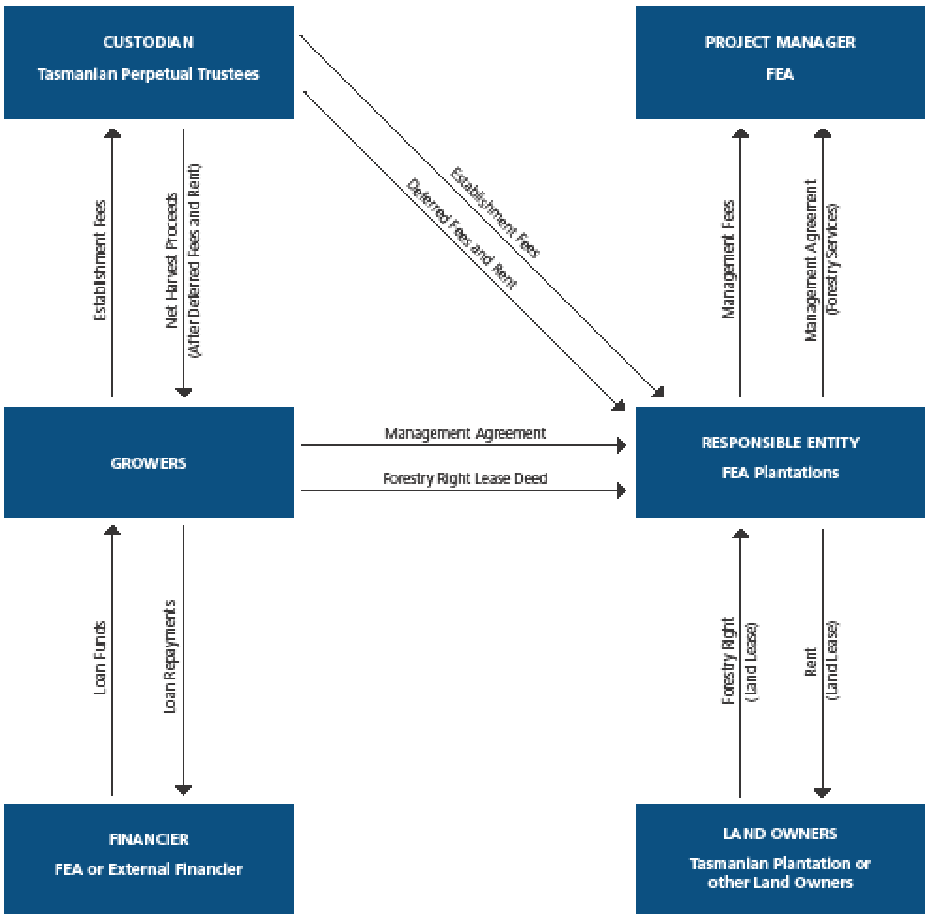
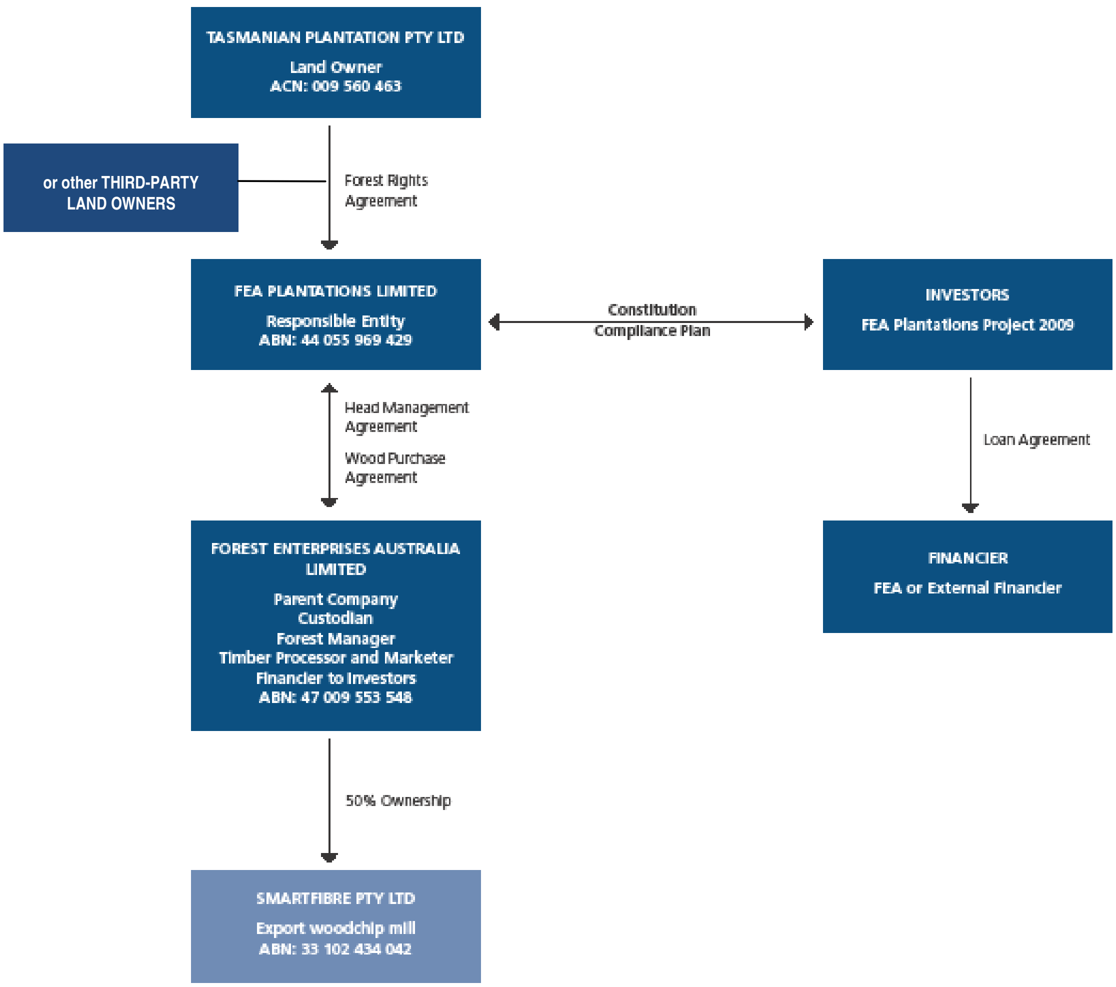
ATTACHMENT 1 - FEA MANAGED FORESTRY INVESTMENT PROJECT STRUCTURE

PROJECT STRUCTURE: FEA PLANTATIONS PROJECT 2008 AND PREVIOUS



This diagram is a simplified description only. Applicants should read the PDS and the underlying legal documents completely to fully understand the relationships.

PROJECT STRUCTURE: FEA PLANTATIONS PROJECT 2009



This diagram is a simplified description only. Applicants should read the PDS and the underlying legal documents completely to fully understand the relationships.

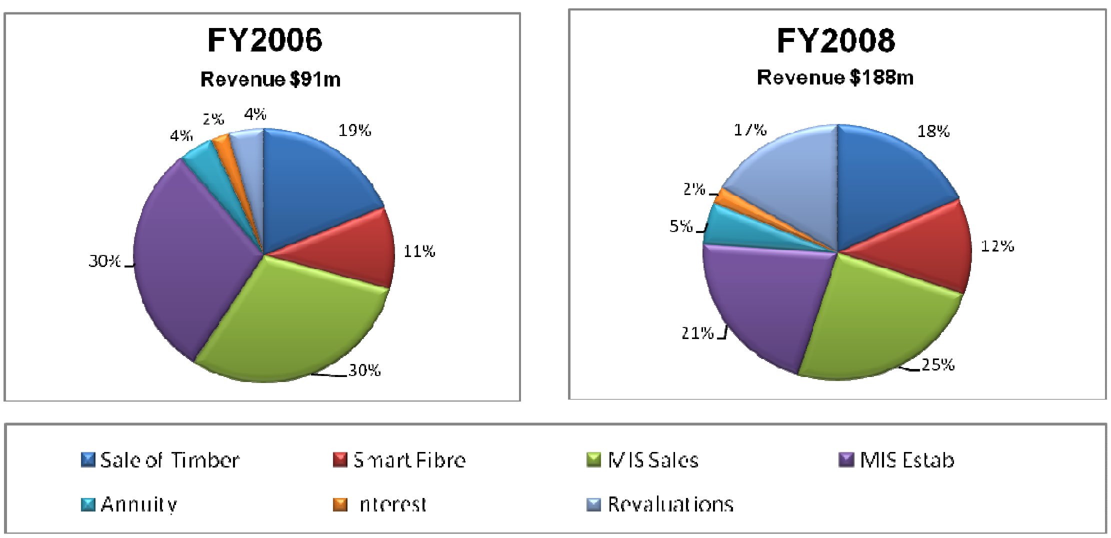
CASE STUDY 1 – A DEMONSTRATION OF FINANCIAL CAPACITY

The following is an edited excerpt from a statement by FEA to the Australian Securities Exchange of 27 May 2009, repeated in the Supplementary Product Disclosure Statement of the FEA Plantations Project 2009 of 16 June 2009. The full text is available at www.fealtd.com. It provides a recent example of how FEA and FEA Plantations Limited disclose issues around demonstrating financial capacity.

- As is the case for all agricultural managed investment schemes, the ongoing viability of a particular Project is dependent upon numerous factors, including the management ability of the Responsible Entity. The ability of FEA Plantations to manage the Project is dependent on its financial position, which in turn is dependent on the financial position of its parent company, FEA.

- FEA is a public company listed on the ASX and, as such, is subject to a continuous disclosure regime. In order to monitor the financial position of FEA, potential investors are advised by FEA Plantations Limited to monitor FEA's website and ASX's respective website for up-to-date information on FEA's financial position as relevant announcements are made.

- The pie charts below are evidence of FEA shifting its reliance away from a single revenue source of managed forestry investment sales and moving further towards a fully integrated model with diversified revenue streams. In FY2008, sales of managed forestry investments accounted for approximately 50% of FEA's total revenue, as compared with approximately 64% in FY2006. This figure should continue to improve as FEA grows its Bell Bay saw mill timber processing output.



Note: The above charts include FEA's 50% share of SmartFibre revenue, not separately recognised in FEA's accounts, as SmartFibre is equity accounted Since 30 June 2008, the company has reassessed its revenue recognition policy relating to deferred lease and management fees. The charts above have been adjusted to take this into account. Please see note 1(e) of FEA's FY2009 half year accounts for further details. Please refer to Page 12 FEA's 2008 Annual Report for a description on the way that MIS revenue is recognised.

CASE STUDY 2 – IMPACTS ON FEA FROM 1999 CHANGE IN TAXATION TREATMENTS

- Any structural changes to the current taxation arrangements of the MIS plantation sector would have the potential for huge unintended consequences. The changes made as a result of the Treasurer's statement on the Ralph Report in November 1999 are only just being overcome.

- It took 4-5 years for the impact of these changes to be factored out of the sector and for confidence and pre-Ralph Report planting levels to be restored.

- This can be illustrated in FEA's case in the graph below (Figure 1), which shows FEA's annual planted areas. The drag between investments received and planting means there is a delayed impact in planting levels.

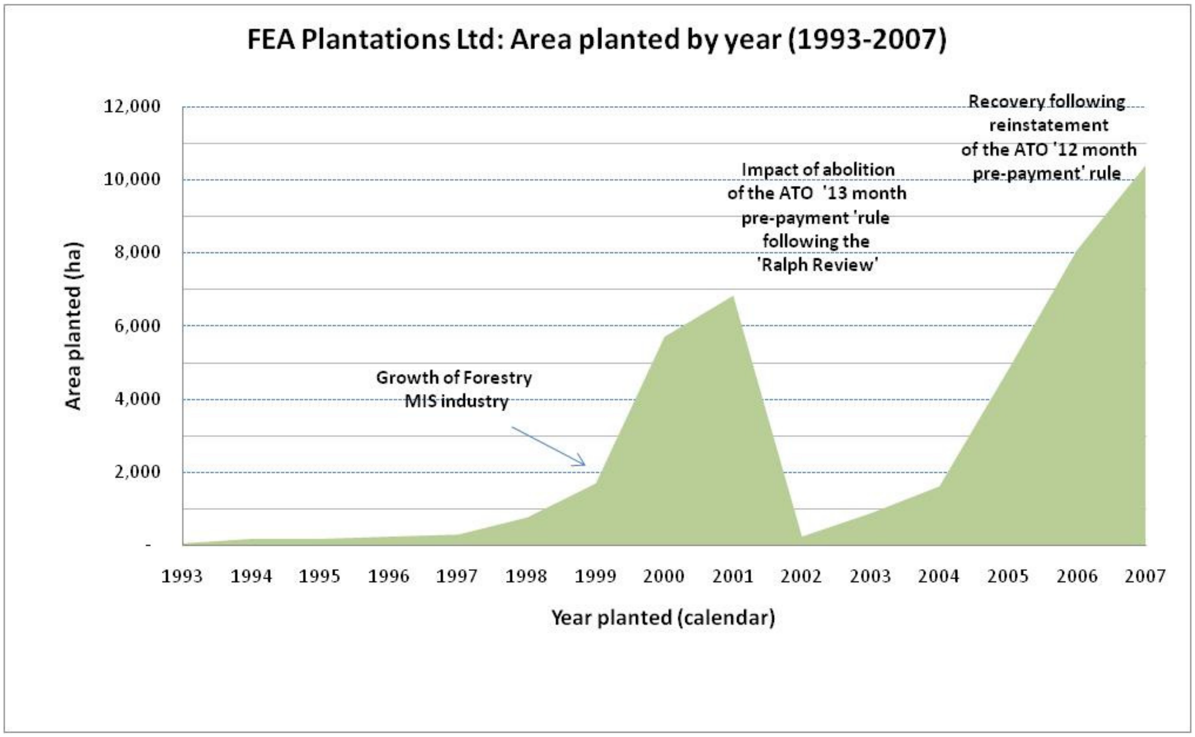


Figure 1– FEA - Area Planted by Year (1995 –2007)

- More importantly, (Figure 2) shows the impact of an unsmoothed wood flow. This demonstrates that with FEA's 13- 15 year regime there are wild gyrations in future wood flows, particularly between 2012 and 2020, which are impacted by unintended decisions made many years previously.

- Without smoothing of these woodflows using optimisation models, this would be an impossible woodflow to manage from a wood marketing and processing point of view.

- This illustrates that any changes in structure needs a considerable lead time from a practical perspective and all parties need to be confident about the impact on planting levels if there is going to be optimal returns to growers, and investment in future processing to add as much value as possible to the Australian economy.

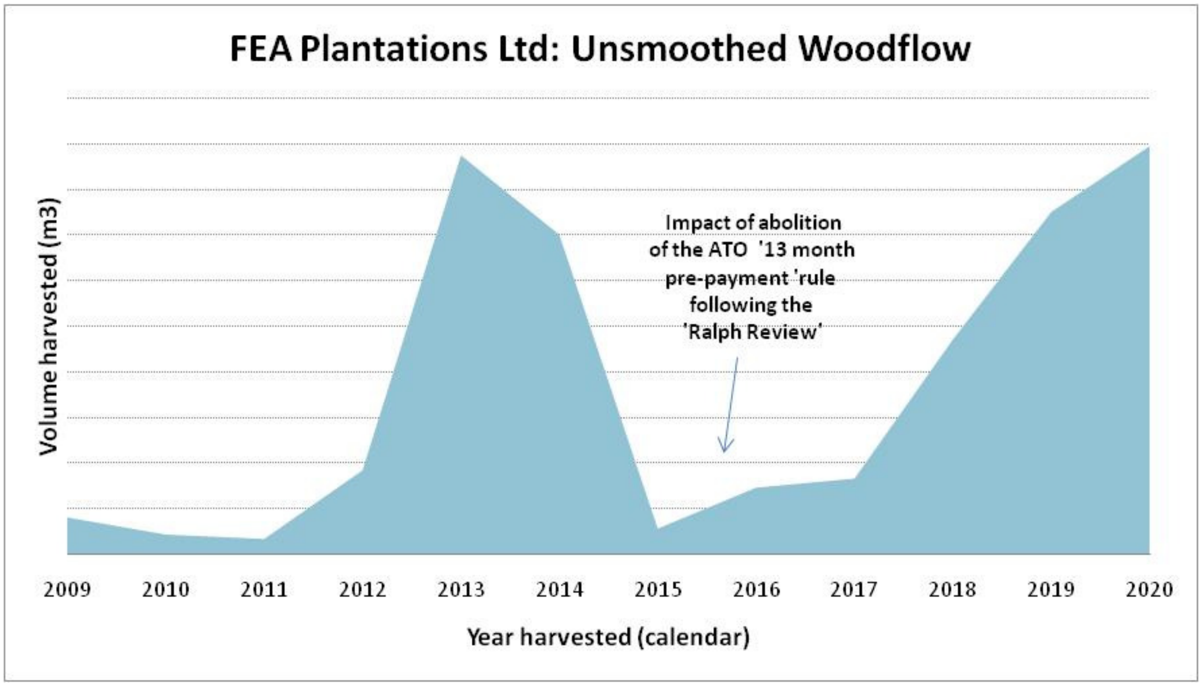


Figure 2 – FEA – Unsmoothed Woodflows and effect of severe fluctuations of planting levels on future wood supplies.

CASE STUDY 3 – AN FEA EXAMPLE OF DISCLOSING PROJECT RETURNS AND RELATED INFORMATION

The following is an edited excerpt from the Supplementary Product Disclosure Statement of the FEA Plantations Project 2009, full text is available at www.fealtd.com. It provides a clear example of how FEA addresses issues around disclosing project returns.

- In the PDS on pages 6-7 and page 17, FEA Plantations has provided details of returns from the first managed forestry investment project planted in 1993 (Tasmanian Forests Trust No 1 ARSN 093 165 210). The harvest of this project was completed in June 2008 and investors received a total harvest return of $16,920 per hectare from Thinning and Clearfall (which is in excess of prospectus projections) with an after-tax IRR of 7.3% per annum. The 1993 project raised approximately $140,000 in investors' subscription funds with total investments for 44 hectares with ongoing Lease and Management fees. The project site was established on two properties in north-east Tasmania which form part of a significantly larger land and plantation holding managed by FEA. FEA is now in the position to release pre-harvest inventory data from its second managed forestry investment project planted in 1994 (Tasmanian Forests Trust No 2 ARSN 093 165 505) disclosed in FEA's *Canopy* Autumn 2009 newsletter. This project was planted on 158 ha over two properties in north-east Tasmania. Again, these plantations managed on behalf of investors form part of significantly larger land and plantation holdings managed by FEA.

- The Clearfall harvest of plantations in the 1994 project are scheduled to commence in October 2009 and the net harvest proceeds received by the investors are expected to exceed $17,000 per hectare with an expected post-tax IRR of 6.6% per annum. Clearfall sawlog recovery is estimated at 77% of sawlogs suitable for delivery to FEA's Bell Bay sawmill for processing into EcoAsh® branded timber. FEA Plantations is satisfied that its pre-harvest data is sound and accurate and that the expected yields are based on reasonable grounds.

- The Before-tax return takes into account 100% tax-deductibility of investor's costs but does not include any tax payable on the Harvest Proceeds. The After-tax return takes into account 100% tax-deductibility of investor's costs and includes all tax payable on Harvest Proceeds. Both calculations are based on top marginal tax rates.

- It should be noted that both the first (1993) and second (1994) projects were originally scheduled to be 15 year projects. The first project was harvested at approximately 14.5 years of age and the second is scheduled to be harvested at 15 years of age.

- FEA Plantations has provided thinning harvest incomes to its investors in its next five (1995 – 1999) projects. However, these do not provide a meaningful indication of total yield and Clearfall harvest incomes because the full area of each plantation could not be thinned for various reasons. It is also difficult for FEA Plantations to make forecasts on the total harvest incomes to be received by investors in these projects with a reasonable basis given that the period to final harvest and the number of factors and circumstances beyond FEA Plantations' control that can intervene and impact on actual net harvest income results. Whilst FEA has an ongoing inventory program and employs highly trained specialists in the forestry sector, the longer the period from harvest that is required to estimate final returns results in less statistical confidence.

- As the plantations mature and reach a growth stage where useful measurements can be relied upon by using the latest available growth modelling, details are provided in Manager's Reports to Growers produced on an annual basis.

- As also stated in the PDS on pages 7 and 17, any reference to past or current performance referred to in the PDS and, therefore, this SPDS must be qualified by noting that past performance is not indicative of future performance and FEA Plantations is not able to guarantee the performance of the plantations established for the Project nor any financial returns to Investors.

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