

GROWER UPDATE

FOREST ENTERPRISES SCHEMES 1995 to 1999

22 August 2011

FEA PLANTATIONS LIMITED ("FEAP")

(SUBJECT TO A DEED OF COMPANY ARRANGEMENT)(RECEIVERS APPOINTED)

ACN 055 969 429

FOREST ENTERPRISES AUSTRALIA LIMITED ("FEA")

(SUBJECT TO A DEED OF COMPANY ARRANGEMENT)(RECEIVERS AND MANAGERS APPOINTED)

ACN 009 553 548

I refer to the Urgent Grower Update issued on 12 August 2011 and, as foreshadowed, now report to you further on the position regarding your lease.

The Receivers of FEA, Mr Norman and Mr Algeri, have, as noted in Mr Norman's letter to you of 8 August 2011, previously asserted that FEA is entitled to receive rent from Growers in Schemes 1997 to 1999. Mr Norman's letter says that Mr Krejci and I have "ignored" those assertions. That remark is unwarranted and untrue. Mr Norman insinuates that this has exposed your investment to risk; again, I say this is untrue.

To understand why requires me to set out a brief history of the schemes in which you have invested. I will do so as briefly as possible, but, in order to be careful and accurate, am required to do so at some length. Because it will make the position easier to understand, I will use the current names of all the companies involved. Some of the companies have changed their names several times in the past 15 years, and to use the name they had when events occurred would be confusing.

Ferrier (Chairman) | Green | Krejci | Silvia | Hodgson (Consultant)

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THE ORIGINS OF THE SCHEMES

The schemes were first established as "Prescribed Interest Schemes" organised under the then *Corporations Law*. The schemes involved Growers acquiring an interest in the Tasmanian Forest Trusts (variously number 5, 6 or 7 for 1997, 1998 and 1999 respectively); taking a lease of a woodlot and entering into a management agreement. The terms of the schemes were outlined in Prospectuses issued by FEAP in association with FEA.

When established, the parties to the schemes were the Growers (as lessees of woodlots on which trees were to be planted and grown until harvest); FEA as lessor of the woodlots, FEAP as Manager, and Tasmanian Perpetual Trustees, which served as trustee of the Tasmanian Forest Trusts.

Under these initial arrangements, Grower subscriptions were paid FEAP and paid on to Tasmanian Perpetual. FEAP then contracted with FEA for it to establish your trees and allocate you a woodlot which FEA leased from a company (which FEA owned) called Tasmanian Plantation Ltd. Under these arrangements, FEA was entitled to recover rent directly from Growers, although we understand that normally FEAP sought recovery of rent together with its management fees.

These arrangements were common to all of the Tasmanian Forest Trust schemes number 5, 6 and 7.

CHANGES TO THE SCHEMES

In 1998, Commonwealth Parliament changed the law under which schemes 5, 6 and 7 had been established when it enacted the *Managed Investments Act* which amended the *Corporations Law*. The changes to that law radically altered the responsibilities of Trustees and Managers, moving many of the responsibilities of the Trustee to the Manager, which became known as a "Single Responsible Entity", or more commonly, a "Responsible Entity".

The changes to the law applied immediately to new schemes, but allowed older schemes two years or so to amend their arrangements to conform to the changed law. In the case of the Tasmanian Forests Trusts schemes, amendments were made in June 2000 which involved:

- ▲ The replacement of the Scheme Trust Deeds by a separate Scheme Constitution for each Scheme
- ▲ Changing the relationship of lessee/lessor, so that FEAP became the party from whom Growers held a lease, while remaining the Manager of the schemes
- ▲ At the same time, FEAP entered into a direct lease of the land occupied by the schemes with Tasmanian Plantation.

The Scheme Constitution was and is an important document. It describes the relationship between Growers and the other parties to the scheme, and (as it can) in accordance with its own terms overrides any inconsistent documents.

The Scheme Constitutions are, in relevant senses, identical. The parts of them relevant to this note are set out in the attachment. In summary, the Constitutions provide:

Lease Agreement (clause 14.1)

The Constitutions all provide that the Responsible Entity will lease woodlots to Growers. The terms of the new Grower Leases were set out in a schedule to the Constitution. They are the same as the original Grower Leases set up under the Prospectus, except that the Lessor is the Responsible Entity

(FEAP) instead of FEA. The Constitutions provided that FEAP could nominate another Lessor, such as Tasmanian Plantation or FEA, however this did not occur.

The Scheme Constitution also provides that upon acceptance of a Grower's application, the Grower and the Responsible Entity become parties to the Constitution, the Grower Lease and to the Management Agreement under the Constitution.

Constitution is paramount (clause 14.5)

Anticipating that there might be inconsistency between the Constitution and the new Grower Lease and Management Agreements, the new Scheme Constitutions provided that in the event of any conflict between the terms of the Constitutions and the Grower Lease and Grower Management Agreement, the terms of the Constitution prevailed.

Because the Constitution is the governing document of the Schemes under the Corporations Act, the Constitution is able to over-ride inconsistencies in this way.

We don't consider that the Grower Leases and the Constitutions are inconsistent; however so far as it may be suggested that the terms of the Grower Leases appended to the Constitutions indicate that FEA remained the lessor of land to Growers, the terms of the Constitutions providing that FEAP, the Responsible Entity will be the lessor, prevail over that suggestion.

The Responsible Entity is "responsible" for the Scheme

As its name suggests, the purpose of the creation of a Responsible Entity is to ensure there is a single legal entity with responsibility for carrying out all aspects of the Schemes – in this case, setting the scheme up, managing the forests, collecting Grower contributions, harvesting the trees and then realizing the proceeds and distributing them.

The 1998 amendments to the Corporations Law created this position, and imposed extensive duties on both the Responsible Entity and on its directors and officers. These duties and powers are clarified and added to by the Scheme Constitutions, which confer general powers and duties to implement the schemes, and expressly include among those duties making available land for lease to Growers.

Collection of Rent and Management Fees

The Constitutions make the Responsible Entity responsible to collect Rent and Management fees. This is what the Receivers deny, and where their circular to you is misleading. In the attachment you can read for yourself the clauses which not only authorises the Responsible Entity to collect these fees, but also requires it to do so.

The clauses are, unfortunately, somewhat complicated, and the terms used to describe the rent could be confusing. It is also necessary to explain what was the role of a "Custodian" before explaining how the rent and management fee scheme worked.

A Custodian was (and is) an additional party to many Managed Investment Schemes. A Custodian is required when the Responsible Entity has less than \$5 million worth of "Net Tangible Assets". The Custodian is normally either a listed company with Net Tangible Assets of \$5 million, or, very commonly, one of the companies traditionally licensed to administer deceased estates, commonly called "Trustee Companies"; these companies are often bank subsidiaries.

The Custodian is responsible for holding Scheme Assets (such as rent received from Growers) until it is applied for scheme purposes as directed by the Responsible Entity. In this way, it acts as practical brake on any misuse of Scheme Assets. This is part of the role that had been performed by a Scheme Trustee before the 1998 law reforms. In your scheme, the Custodians have, successively, been Tasmanian Perpetual Trustees Ltd; FEA; and then Sandhurst Trustees, a subsidiary of Bendigo and Adelaide Bank.

The Scheme Constitutions require that the Responsible Entity obtain payment of amounts required to be paid under the Scheme, and that those moneys be paid to the Custodian, and thereafter disbursed at the direction of the Responsible Entity. The relevant parts of the Constitution are appended.

Grower Default

When Growers default on any payment due under the Scheme, the Responsible Entity is entitled to sue for the payment, a right consistent with being the lessor of the interest held by Growers.

Conclusion

These provisions, taken together, show that from the date the amendments to the schemes took effect in May/June 2000, FEAP replaced FEA as your lessor; had power (indeed it had a duty) to collect rent and management fees, and that this was to the exclusion of FEA.

Mr Norman had set out arguments similar to those put directly to Growers in correspondence sent to the Deed Administrators in mid 2010. We had told him of our disagreement with those arguments and why we disagreed with him, and had inferred that he accepted our explanation. We are unable to explain why he has sought to make those arguments to Growers.

THREATS TO THE SCHEMES

Mr Norman alludes in his circular to threats to Growers' interests by reference to non-payment, and by reference to breaches of lease covenants not related to payment. The nature of those threats is not altogether clear from Mr Norman's letter; I am therefore required to address what I think he intends by his references. Mr Norman would assist Growers and the Responsible Entity if he clarified the matters to which he is referring.

Non-payment

Mr Norman asserts that Growers who have not paid FEA directly have defaulted. For the reasons set out above, his assertion is wrong. Growers' rent is due to be paid to the Responsible Entity, not FEA.

FEAP has been arranging payment of rent it itself owed to FEA by invoking rights of set-off of amounts FEA owes FEAP. That approach had been upheld by a judge of the Federal Court in 2010, although in recent weeks the Full Federal Court gave reasons allowing part of an appeal by the Receivers of FEA in relation to that single-judge's decision, so that FEAP cannot in practice apply all of the amounts due to it in set-off.

The effect of the appeal was to deny FEAP the immediate ability to invoke one ground of set-off. However, it did not remove or eliminate other rights FEAP has to make payment. For example, FEA has not met insurance and maintenance costs incurred by FEAP in relation to woodlots which FEA itself holds in the schemes, and many Growers pre-paid their rent. In our assessment, the lease arrangements between FEA and FEAP are not currently in breach for non-payment.

The Receivers of FEA have purported to serve notices of default upon FEAP for non-payment of what it says are rental obligations. We do not consider that these notices are effective; and contemplate bringing legal proceedings to determine the point.

Maintenance

Separately, the Receivers of FEA have asserted to FEAP that it is in breach of duties to maintain the woodlots. Until the appointment of Receivers, FEA had carried out this work for FEAP under a Head Management Agreement. The Receivers terminated that Agreement on their appointment.

You will appreciate that FEAP, having to pick up work previously undertaken by another company, has taken some time to resume operation; however, in our view FEAP is now compliant with the requirements for maintenance of woodlots in FEA Schemes 1994 to 2002.

Some of the FEA Forestry Schemes, especially those where FEA had promised to fund the costs of rent and maintenance, are unviable: it has not been possible to obtain external funding or Grower-funding sufficient to meet the costs of carrying out those schemes. These are the "deferred fee" schemes established from 2003. Non-essential maintenance of land occupied by those schemes has been suspended.

Our assessment is that *your* Scheme – a "Grower-Funded" scheme – is viable. However, Mr Norman may be seeking to invoke defaults he says have occurred in relation to land occupied by other schemes. In our view he is not entitled to do so.

Deemed breach

Mr Norman has also, as Receiver and manager of FEA and as Agent for the Secured Creditors in Possession of Tasmanian Plantation, said that FEAP is in breach of a leases through which Growers trace because it is "In Receivership", or has entered into an "arrangement or compromise" with its creditors. Again, I have appended the relevant clause of the arrangements to this letter. The relevant clause reads:

Enters a composition or arrangement with its creditors or shall enter into a Deed of Assignment or become bankrupt or being a company shall go into receivership or liquidation (whether compulsory or voluntary)

Again, we consider Mr Norman's assertions misplaced. FEAP is not, in its capacity as Responsible Entity, in receivership: the instrument under which Mr Norman is appointed expressly says that he is not appointed to Scheme Property or the role of Responsible Entity. Moreover, the company's internal structure has not been displaced in the way contemplated by the phrase "in receivership". Nor is the company in liquidation. The company has entered into a Deed of Company Arrangement, but in our view this is not a "composition or arrangement" of the kind referred to in the clause; rather, these refer to arrangement which individuals may conclude, and which FEAP has not.

In any event, we are exploring means by which FEAP may be removed as Responsible Entity; this will, we hope, put beyond any question the continuation of your Scheme.

In the meantime, we regret the confusion that has been sown by the unnecessary correspondence sent by the Receivers of FEA.

I trust this information is helpful. If you have any further questions, please feel free to contact the FEAP Grower Helpdesk, which can be contacted on 08 8263 2300.

Yours faithfully
FEA Plantations Ltd

A handwritten signature in black ink, appearing to read 'B. Silva', is written over the printed name 'BRIAN SILVA'. The signature is fluid and cursive, with a long horizontal stroke extending to the right.

BRIAN SILVA
Deed Administrator

Attachment: relevant parts of the Scheme Constitutions

14.1 Lease Agreement

- (a) Each Grower will lease from the Responsible Entity (or such other party it nominates) land for the purpose of growing, nurturing and harvesting timber.
- (b) The form of lease to bind the parties is set out as Schedule 2 to this agreement or in such other form as the Responsible Entity may approve.

12.4 Issue of Interests

Upon acceptance of the applicant's application (whether or not before the time that the date of registration of the Trust) the Responsible Entity and the Grower become contractually bound by the Management Agreement and Lease and the Responsible Entity must (if the manager has not previously) issue the interest applied for, and thereupon the applicant has an interest in the project and becomes a Grower.

14.5 Inconsistency

- (a) In the event of any conflict between a lease or a management agreement, and this Constitution, then the terms and provisions of the Constitution shall prevail, and the lease and management agreement shall be void to the extent of that inconsistency without any right to rescind.

16. POWERS AND DUTIES OF RESPONSIBLE ENTITY

16.1 General Responsibility

The general responsibility of the Responsible Entity is to manage and operate the project for all of the Growers taking part in the project, and ensure that all aspects of the project are dealt with honestly, prudently, ethically, and in accordance with the Corporations Law and any other applicable law. In general terms it will do this by its own actions or through agents:

- (a) Making (or causing to be made) available for lease appropriate land
- (h) In addition to all other duties and powers conferred on the Responsible Entity by this Constitution and the Corporations Law, the Responsible Entity must do any act or thing, which in its reasonable opinion, is necessary for the proper and efficient establishment, management and development of the project, and the just and equitable treatment of the Growers, as between themselves, and as between the Responsible Entity and each and every one of them.

APPLICATION MONEY

13.1 Cheques for Application Money

The Responsible Entity must require all payments in respect of an application for interests in the project to be paid in favour of the custodian on account of the project and the applicant.

13.2 Receipt of Application Money

The Responsible Entity must, within a reasonable time of receipt of any payment for application money, remit the payment to the custodian.

13.3 Applications Fund Account

The Responsible Entity must ensure that the custodian deposits into an account designated as being for the Trust - Applications Fund Account no monies other than application monies, or other monies incidental to the making of an application. These funds are Project Assets and are held in trust for the respective Growers contributing them pending the arising of an entitlement to them by the Responsible Entity, whereupon they are held in trust for the Responsible Entity to the extent of its rights, any balance remaining on resulting trust for the Growers.

Application Money

The money paid with the application by applicants

Project Property

The application fund, project trees once severed from land, the proceeds fund, all investments, assets and other any property contributed by growers. Such property does not include:

- (a) the separate and distinct primary production business operated by a grower
- (b) the trees growing on land leased by the grower
- (c) the leasehold interest of the grower in a plantation
- (d) any sale proceeds generated by a grower by virtue of an election under the Constitution to sell his or her own trees

DEFAULT BY GROWERS

22.1 Default

A Grower is in default when any amount due by the Grower with the application remains unpaid, any other sum is due and unpaid pursuant to the Management Agreement and Lease.

22.2 Procedures

If a Grower is in default, the Responsible Entity may:

- (a) Take legal proceedings for the recovery of the amount in default