

**THE PARLIAMENTARY STANDING COMMITTEE ON ENVIRONMENT,
RESOURCES AND DEVELOPMENT MET IN THE RECEPTION ROOM, TOWN
HALL, LAUNCESTON, ON MONDAY 19 MARCH 2007.**

Mr BOB GORDON, MANAGING DIRECTOR, FORESTRY TASMANIA, AND **Mr IAN JOLLY**, GMO RENEWABLE RESOURCES REPRESENTING TASWOOD GROWERS, WERE CALLED, MADE THE STATUTORY DECLARATION AND WERE EXAMINED.

CHAIR (Mr Hall) - Thank you, gentlemen, for appearing today. I invite both of you, or the spokesperson, as I did with Auspine and Rayonier, to make an introductory statement, if you would like, and talk about the terms of reference as you see them, and the log supply deal, and then I will open it up to the members for questions.

Mr JOLLY - I am happy to make a few opening comments. I do not think my partner, Mr Gordon, needs any introduction so I will assume that you all know him very well. For my part, I am a forester. I am been with GMO since 2000. GMO Renewable Resources is an affiliate of a bigger investment company. The renewable resources team specialises in investing in timberlands. We advise on investments in New Zealand totalling in the vicinity of 230 000 hectares. One of the first investments we made was here in Tasmania, and we are very enthusiastic about the 48 000 hectares that we have invested in here. There is a further 30 000 hectares in South America. My colleagues in the US manage about 1.5 million hectares.

We are a little surprised to be here today, to be frank. It is not clear to me exactly why we are here, but we are happy to be open and as honest as you would expect us to be about this process. We appreciate the amount of interest that this has created and your concerns around it. We are happy to answer your questions as they arise, with the caveat of course that we are a private commercial business and so are a number of the other parties involved in this decision-making process and we do not wish to make comments on provide information that could cause damage either to our business or to theirs. With that caveat, I am happy to answer your questions.

CHAIR - Bob, would you like to add to that?

Mr GORDON - A little bit like Ian, I am wondering why we are here, but obviously am happy to be here and answer questions. On several occasions, Forestry Tasmania had advice that section 12 of the Forestry Act did not apply to this transaction, but we are more than happy to have a discussion about what the softwood joint venture is and what its objectives are. Those of you who were at the recent GBE hearing would know I provided a bit of background about why it came here in the first place.

CHAIR - It might be useful, if you would not mind, to give us a synopsis of that.

Mr GORDON - In the mid-1970s, forestry in Australia became a controversial issue when a book written by the Routleys, supported by a conservation movement, suggested, amongst other things, that pine plantations were undesirable, they were exotic weed and we should basically stop planting them. This happened to coincide with a

Commonwealth-State agreement in which the Commonwealth encouraged the States to put softwood plantations in the ground as a way of generating an industry a bit down the track. The Forestry Commission participated in that Commonwealth Softwood Agreement program and, for a variety of reasons stretching back 50 or 60 years, softwoods were planted in Tasmanian locations that at the time were linked to government employment priorities. For instance, a whole lot were planted in the Fingal Valley because of a downturn in the mining industry; those at Strahan were planted partly because of a downturn in the mining and wharf in Queenstown and Strahan; some in the north-west were originally planted as some soldier settlements did not do very well and it was thought the land could be better put into some sort of forestry use.

It was probably not until the mid-1980s that there was a much more consolidated approach to the State-owned softwood plantations in Tasmania. That happened to correspond with severe financial restrictions imposed by governments at a time when Tasmania was in a difficult financial position; firstly the Government of Premier Gray, then Premier Field, and Mr Groom and Mr Rundle. Basically, the old Forestry Commission and then Forestry Tasmania did not have the money to continue to expand the softwood plantations in the State.

In about 1993, Premier Groom, in his state of the State address to the Parliament, said that he was going to change the old Forestry Commission. He planned to corporatise it, and he was also looking at whether the pine estate would be better off in private hands, or some other ownership. Forestry Tasmania was eventually formed out of the Forestry Commission through an act of parliament which predated the GBE act. It was the first GBE, although we did not call them that then. The new board of Forestry Tasmania was asked to look at an appropriate ownership structure for the softwood plantation estate, whether they should be kept in government ownership and, if so, the capital requirement to expand the estate. A study by Judy Clark from ANU on behalf of the Greens and the Wilderness Society at the time questioned whether the Government should own the softwood plantation estate, the core business.

At the same time, Forestry Tasmania had done work looking at the likely future of the softwood industry. At the time there was a plantation estate of about 38 000 hectares which had, as Mr Booth said before, suffered from a lack of a pulpwood market until Norske Skog or ANM as it was then, expanded to process pulp through a different process called TMP. Scottsdale's two major softwood mills at the time processed about 64 000 cubic metres of logs. All the analysis that had been done suggested that was not a sustainable position, a softwood mill in Australia needed to be much bigger than that, and unless the softwood plantations in the State could be substantially expanded, those mills were destined to have not much of a future; they would be uncompetitive and in bad market conditions they would be under severe difficulties.

One of the driving forces behind the eventual decision to put a half share of the softwood plantation on the market was to find a partner who was prepared to commit substantial capital to expand the softwood plantations in the State. At the time, Forestry Tasmania had plenty of land available, mostly native forest that could be converted to softwood plantations, but we did not have access to substantial sums of capital. The joint venture was structured around Forestry Tasmania's substantial commitment to expand in the State by providing land it already owned and most of the cash eventually came from the GMO side. We had the best of both worlds; we had a large, respected funds manager providing

capital growth for the long-term future of the estate and Forestry Tasmania using land it already owned to provide a softwood joint venture.

We had formed another joint venture immediately before this, with a company called Hokushin, which ended up building the MDF plant at Bell Bay, and part of the driver for that was, again, trying to find a market for pine pulpwood because if you haven't got a market for pine pulp it is very difficult to manage pine plantations and sawlog regimes.

Also, they had committed to an expansion of the estate, and we ended up planting about 2 500 hectares of extra softwood plantations in a joint venture with Hokushin. As it ended up, the softwood joint venture bought out Hokushin in that joint venture, so that again became part of the softwood estate. Once we decided on the model we went around the world talking to funds managers; the opportunity was opened up to a whole lot of domestic players in the Australian market as well, including Auspine and Frenchpine. A whole lot of information was produced about what the likely future availability of logs was under different plantation establishment scenarios and the overwhelming view from everyone who expressed interest in it was that we needed to get a bigger plantation estate or we would not have a hope of having sustainable jobs in the softwood sector.

The presentations which were done at that time all asked for a commitment from potential bidders to an expansion of the softwood plantation estate and a commitment of capital to that. All of the people who ended up putting in a complying bid were also committed to that strategy and when the softwood joint venture was eventually formed on 1 July 1999 the presentations that were jointly done to the industry, unions and general community all stressed the commitment of the softwood joint venture to that plantation expansion program. So if people ask me was it a good idea going into the softwood joint venture, my answer would be that if we had not I do not think we would have any sawmilling processing capacity in Tasmania at the moment. We would not be big enough; we wouldn't have the economies of scale that you need, and I think the money that has been spent since July 1999 is very, very substantial and would not have been spent if the plantations had stayed in State ownership.

CHAIR - Thanks Mr Gordon. Mr Jolly, would you like to add anything to that, or are you happy to take questions?

Mr JOLLY - I am happy to take questions.

Mr GUTWEIN - Mr Gordon, regarding the make-up of the Taswood Growers Board, how many representatives from Forestry sit on that, how many from GMO and who are the Forestry Tasmania representatives?

Mr GORDON - There are three from each. The current Forestry Tasmania representatives are me, Penny Egan and Paul Smith.

Mr GUTWEIN - We have heard this morning from Rayonier that the decision-making process in relation to the contract that was offered to FEA was such that Rayonier received from the Taswood Growers board an evaluation criteria to apply to bids and then they would give the board their assessment as to whether or not the bids met that evaluation criteria, but with no recommendation as to which was the better offer; it was

left to the Taswood Growers Board. Is that your understanding of the process and how Rayonier explained it to the committee this morning?

Mr GORDON - Correct. I was only in the process from the start of this year. I only joined as a representative of Forestry Tasmania in January; before that Mr Rolley was the representative. So if you want to go back through the history of it, you are probably much better off speaking to Ian Jolly because he was there the whole time.

Mr GUTWEIN - I was particularly interested in the decision part of it. We can perhaps extend that and have a look at the structure of the board as we move forward this morning.

From advice that the committee has received in regard to section 12A, my understanding is that section 12A does not apply on the basis that when the joint venture was originally constructed, included in that was the sales agreement which effectively passed all of the rights and responsibilities in regard to the sales and terms of sale regarding the timber to Rayonier. Now this morning the process that we have been informed of has indicated that the decision rested with Taswood Growers and therefore FT is one of the members on that particular board. Why doesn't section 12A have to be taken into account by Forestry Tasmania under those circumstances?

Mr GORDON - I understand, Mr Chairman, you have advice from the Solicitor-General about the operation of section 12A, and Forestry Tasmania also has advice from the Solicitor-General, and others. If you want me to go through the structure of the joint venture, and I think that is the issue Mr Gutwein is getting to -

Mr GUTWEIN - What I was getting to was that very clearly the advice that we received was that when Forestry Tasmania took ownership in the joint venture, the terms were that you held 50 per cent of the wood resource. The terms included a provision denying participants, including Forestry Tasmania, the right to sell the beneficial interests in the wood resource, otherwise in accordance with the associated sales agreement, which effectively passed the right to determine terms and conditions of sale to Rayonier.

Mr GREEN - The sales agent appointed by the board.

Mr GUTWEIN - The sales agent appointed by the board - so effectively, because Rayonier through its agreement was responsible for the terms and conditions of sale, Forestry Tasmania could not be held responsible to its obligations under section 12A. But in the process that was explained to us today, Rayonier did not make that decision, the decision was made by the board of Taswood Growers. So the question is, doesn't Forestry Tasmania have an obligation under section 12A under those circumstances, because the advice that we have is that your obligation was contracted to Rayonier. But Rayonier did not make that decision; you did.

Mr GORDON - Have you asked that question of the Solicitor-General? I have advice from him, and I am bound by his advice. Once we ask the Solicitor-General a question, we are bound by his answer. I do not know whether that opinion - it is not my document - I have one which the Solicitor-General provided to me, and I also have other legal advice which confirms that view.

I think the subtlety in terms of the structure is that the sales agency agreement commits the participants in the joint venture to only selling their product through the sales agent, and that is Rayonier. That is a different question than the one you are asking. I think the one you are asking is whether Forestry Tasmania or GMO could sell their wood outside the legal structures of the joint venture.

Mr GUTWEIN - No, no it is not. The question I am asking is in relation to the advice that we have, which very clearly indicates that the reason that Forestry Tasmania has no obligation or function in regard to 12A is that that function has been contracted to Rayonier as a part of the establishment of the JV. That is my understanding of it.

Ms THORP -No, that is not right - those rights and obligations, in my understanding, were abrogated when the joint venture was drawn up.

Mr BOOTH - Point of order, Mr Chairman. This interference by the members while someone is trying to follow a line of questioning is quite inappropriate.

Members interjecting.

Mr GUTWEIN - Just so we are clear, the advice that I have in front of me is this. As a result of that dealing, Forestry Tasmania, as a participant in the joint venture and subject to the terms of the joint venture agreement, has 50 per cent of the wood resource. . Those terms include, inter alia, provision denying participants, including Forestry Tasmania, the right to sell the beneficial interests in the wood resource, otherwise in accordance with the associated sales agency agreement, which effectively passed the right to determine terms and conditions of sale to Rayonier Australia Pty. Ltd. Thus, a consequence of the joint venture agreement is that in terms of section 12A of the Forestry Act, Forestry Tasmania since 1999 has not had the function of examining options, but in this case it appears that Forestry Tasmania did have the option of investigating the terms or it did need to satisfy 12A on the basis that Rayonier were not making the decision. This morning they said that under quite different circumstances to those under which they would normally operate they referred the decision back to the board.

Mr GORDON - Under the terms of the sales agency agreement.

Mr GUTWEIN - So it became a board decision?

Mr GORDON - The sales agency agreement which the Solicitor-General has, as he says, partly summarised; that is, he has not listed all of the terms and conditions under this agreement. This agreement means that the only route to market is via the sales agency agreement and the only route to market for either of the joint venture participants is the joint venture acting together. Forestry Tasmania, as a separate corporate entity set up under the Forestry Act, has no role in making a decision as part of the joint venture.

Mr GUTWEIN - My understanding, Mr Gordon- and perhaps you can clarify it for the committee - is that FT has 50 per cent of the joint venture and there is a 27:23 per cent split between the two companies associated with GMO that hold the other 50 per cent.

If Rayonier were not making the decision, regardless of what limits the agreement places on them in regard to route to market, very clearly in this particular circumstance it appears that Forestry Tasmania as 50 per cent owner of that wood resource did have to make a decision as to whether or not you agreed with either of the two bids that were placed before you?

Mr GORDON - No.

Mr GUTWEIN - So who made the decision?

Mr GORDON - The softwood joint venture made the decision and the softwood joint venture is made up of the directors nominated by each of the owners. These are separate legal entities from Forestry Tasmania.

Mr GUTWEIN - If the directors of FT who were part of the joint venture board had not agreed with the decision of the other directors, is there a dispute resolution process that assists the board to come to a position?

Mr GORDON - The reasons for taking all the trouble to choose a partner and set up the joint venture was to ensure we both had the same objectives: to expand the plantation estate, to maximise the value of the estate by increasing pruning and thinning, fertilising and doing all those things. As you would also be aware, in Australia you have to act in the interests of the shareholders otherwise you are in big trouble.

The directors of the softwood joint venture do not act on behalf of the individual entities by which they happen to be employed.

Mr GUTWEIN - Who are your shareholders?

Mr GORDON - The shareholders of the softwood joint venture?

Mr GUTWEIN - Yes.

Mr GORDON - Forestry Tasmania and the two GMO entities.

Mr GUTWEIN - Do you have to act on behalf of the shareholders or do you take into account the interests of your shareholders in regards to your decision-making process?

Mr GORDON - Correct. You have to act in the interests of the entity, the entity being the softwood joint venture.

Mr GUTWEIN - You indicated that you had advice that there was no requirement or obligation for you to take that into account section 12A. Do Forestry Tasmania directors sit on the board of Taswood Growers? Are you still obliged to take into account other State statutes or the remainder of the Forestry Tasmania act when you perform your functions on the Taswood Growers board? For example, could you act in contradiction to sections in the GBE act?

Mr GORDON - What sections?

Mr GUTWEIN - Let me come back a step. Are you bound by those acts in regards to your conduct as directors, as members of the joint venture?

Mr GORDON - You are bound by the laws of the State and Commonwealth.

Mr GUTWEIN - That is what I was asking. A principal objective of a GBE, Forestry Tasmania specifically, under section 7(1)(a) (ii) of the Government Business Enterprises Act is to achieve a sustainable rate of return that maximises value to the State in accordance with its corporate plan and having regard to the economic and social objectives of the State. I would have thought that that FT directors at least would have recognised that there probably would be some pretty horrendous social and economic outcomes for a particular part of the State as a result of any decision it might make when the decision was placed before the board of Taswood Growers. Did you consider that?

Mr GORDON - If you are asking the question, was it easy for the softwood joint venture to arrive at the decision it arrived at the answer is no. It took a couple of sessions, a great deal of analysis and thought, and it was not the most convenient short-term decision to make. Separate from Forestry Tasmania or the GBE, what we had to do as individuals and were liable to do as individuals was act in the best interests of the softwood joint venture entity, taking into account that one of our objectives is to have a long-term sustainable industry that is able to withstand competition from all other sorts of players. We still believe that we need to expand the plantation estate. That has become much more difficult as various interest groups have opposed plantation estates being established on farmland or on native forests. Every time we have attempted to expand the plantation estate people have said, 'No, we don't like that. We don't like you planting on farmland; we don't like you planting on ex-native forest sites'. So we had to come to what was a very difficult decision, balancing what we believe are the commercial interests and the longer-term sustainability of the industry. We carried out lots of inquiries, we had independent reports commissioned from experts, we carried out and received from Rayonier detailed analysis of the different options, and it was not an easy decision. No-one felt happy but we had to make a decision.

Mr GUTWEIN - If you received information from different industry experts about the long-term sustainability of the industry, what sort of information did you seek in regard to the social impact? I frame that question on the basis of the economic and social impact statement that was called for by government but was not available until after the decision was announced. What information did you have to hand to assist Forestry Tasmania in ensuring that the obligations that you had to your shareholders were being met in regard to the wider social impact?

Mr GORDON - I will say it again, Mr Chairman, it was not the decision that Forestry Tasmania made; it was a decision that was made by the softwood joint venture, and I will answer the question in those terms. We were provided with a detailed analysis looking at the likely future industry structure both in Australia and New Zealand, and wider afield. It looked at likely trends in the industry; it looked at what you would need to do in terms of economies of scale and processing technology to be a competitive grower and processor in the future and the consequences of not having a sustainable, viable softwood sector which also have substantial social implications. So we needed to weigh up and judge what were very difficult issues. As a softwood joint venture we did that to the best of our ability. Obviously some people are not happy with that and we accept

responsibility for that, but it was not an easy decision. We took the best advice available to us acting in the long term and in what we believe to be the long term interests of the softwood joint venture and, more broadly, the sustainability of the softwood sector.

Mr JOLLY - I could add a few comments to that. We have invested here for the long haul, and I do not think it is any secret that it has been a pretty tough ride so far. Much of the backdrop here - business is tough - is that we are working with customers who are telling us that our prices needed to come down so that their businesses could stay sustainable. At the same time we were making decisions as recently as last year to stop any non-essential expenditure in the forestry; we were costing jobs right then; to stop pruning, stop anything that was going to incur expense that we simply could not afford.

I believe that our managers at all times acted responsibly and fairly in making this resource available and we needed to achieve competitive prices to keep our business sustainable. Without the trees in the ground, obviously, and the investment from us and others in not only maintaining the existing crop, which is some \$40 million to \$50 million a year that we pump back into that forest, then there will not be a resource in the future to argue about. Nor will there be any interest in expanding the resource which we would dearly love to do; we believe Tasmania is a great place to grow trees and it is a wonderful place to be invested, but it needs to be competitive. Do we regret that there are a number of parties that are feeling disadvantaged and/or potentially disrupted by this decision? Absolutely we regret it. We regret making a decision in the long-term interests of our business, our shareholders, and we believe the long-term interests of the softwood industry here in Tasmania. Absolutely not - we are passionate about it; this is the right decision.

CHAIR - I will just remind members to maintain the line of questioning in regard to the terms of reference and the log supply deal. Let us not get into any long-winded philosophical differences or debate.

Mr BOOTH - Were you aware in 1998, when you were entering into the agreement, of the obligations Forestry had as a joint venture partner with regard to either the GBE act or the Forestry Act?

Mr JOLLY - I joined GMO in 2000 so was not party to those negotiations, but I would find it extraordinary that a commercial business such as ours would enter into a joint venture with a government business enterprise that was to be bound by anything other than commercial imperatives, so it was my understanding and is still my understanding that this business is to be governed by the laws of Tasmania and Australia, obviously, but by commercial imperatives.

Mr BOOTH - So when Mr Gordon speaks of one of the reasons for the joint venture from the Government's point of view - and I respect that you cannot speak for him in terms of what he was saying then - one of the reasons the Government had given at that time quite broadly was to create a sustainable and viable long-term softwood industry in Tasmania. I think the available harvest was not there to sustain more than 64 000 cubic metres per mill, I think he said, so the intention was to create a bigger estate. Is that a fair comment?

Mr JOLLY - Yes.

Mr BOOTH - So how does exporting volumes of logs - in other words, not providing some certainty of supply to local processors, exposing them to the global log price in terms of export - help to create a long-term viable softwood sawmilling processing sector here?

Mr JOLLY - Firstly, you raise a number of good points here and I am pleased to be able to answer them.

I think you heard Mr Nicholls say that over the course of the joint venture so far there has been some 17 per cent of total production exported and only 4 per cent is of sawlog quality. The vast majority of it is wood quality that we cannot sell here. If we could sell it here perhaps that would be a better solution or perhaps it would not, but if we cannot sell it at all and if for some reason the export market was not available to us or we failed to take that opportunity into account we would be sub-optimising the value of this resource for our owners. Relative to the competitiveness of mainland Australia which exports significant volumes of log and round fall and New Zealand that exports some 30 per cent of its round production and log fall we need to be competitive and the export market offers a viable and very valuable outlet for us, particularly for log grades that we cannot sell domestically.

If we were totally focused on the export market we would be selling everything right now because it is so much more attractive to us financially than the domestic market. But the export markets are volatile and we recognise that. We recognise there is value in long-term relationships with our customers and we have just entered into a 10 year contract. The vast majority of our sawlog resource and the quality of wood that we believe we can sell and process domestically is now contractually committed to domestic players in Tasmania.

Mr BOOTH - From your understanding of that joint venture, did the contract that was given to FEA provide similar terms to those Auspine was offered?

Mr JOLLY - Both parties were given exactly the same opportunity to compete for the wood. We made an assessment based on the proposals that were given to us and we accepted what we strongly believe was the best proposal.

Mr BOOTH - So your information is that they were on like terms?

Mr JOLLY - There were similarities and there were differences which obviously made them the same in some respects and different in others.

Mr BOOTH - What about the incapacity of the mill to process the bigger-end section material?

Mr JOLLY - As I say, we are working against the backdrop here where our existing customers or some of them were telling us that log prices had to drop but that was an unacceptable solution to us because we at that time were delivering wood at a loss. That is not sustainable, I can assure you.

Mr BOOTH - So you are saying Auspine's offer for the resource was less in that sense?

Mr JOLLY - That is the backdrop. What I want to go on to say is that overwhelmingly what is important to us as long-term investors is that we are setting ourselves up for the future and the long term. We regret that there are some transitional issues and some short-term difficulties - absolutely. It is going to be difficult but in the long term we feel it is our responsibility to our shareholders and to the softwood industry here generally to set up for a situation where Tasmania can be competitive on a world scale. There is a world-scale mill being built here with state-of-the-art technology and that is the way forward for processing in this country to be able to compete not only on a domestic scene here in Tasmania but with mainland Australia and elsewhere in Asia.

Mr BOOTH - So lower labour units per cubic metre?

Mr JOLLY - Inevitably that is the way of the future.

Mr BOOTH - Was the offer that Auspine say they made to match -

Mr JOLLY - Can I just add to that?

Mr BOOTH - Yes.

Mr JOLLY - Whilst there may be lower labour units in certain aspects of the processing sector, that view of the future I am giving you where we are competitive will stimulate our interest and the interest of others to invest further here in the softwood industry. Much of the rest of my week is going to be spent here looking to do just that.

Mr BOOTH - Yes that may be so but effectively then, FEA's intention as part of this contract presumably was to create a more modern mill facility with less labour units per cubic metre volume through it, and I accept that that is the case. A part of your assumptions in accepting that tender was based on Auspine's long-term lack of viability, was it, by running a fairly high employer -

Mr JOLLY - We assessed, and we were assisted in that assessment by consultants, as to which was a business plan that looked sustainable into the future and it was our assessment that FEA's business plan was more sustainable. Labour is a component of that, technology is a component of it, location is a component of it; there is a whole raft of factors involved in that but our assessment at the end of the day was that not only was the FEA a better deal for us but it was a better deal for the softwood sector here because we could see it being competitive into the future.

Mr BEST - I am starting to form a picture on what has been said. I know we have had some questioning throughout the day about the legal aspect and how the joint venture sits on its own from the 1999 agreement. It does appear, though, that in many ways there were a lot of quite complex competing factors that had to be considered in the overall process. There is your investment, for example, the ongoing social, economic and employment aspects and that long-term sustainability point. I am interested also in Mr Gordon's comments on this.

There is the fact that the joint venture in many respects sits on its own, it has to stack up on its own in balancing all of these things that you have been talking about. So there are a lot of competing issues to address and then to come up with the best decision. I am just

wondering what your thoughts might be on how that pans out. I am just interested in that part of it because that is really what we want to get to, to what was happening at the time. That is what I understood that you were set in those circumstances. That is why I was wondering whether or not you would concur with that or whether you had a different view.

Mr JOLLY - I concur with much of what you said. There are a number of competing interests here but at the end of the day it is a commercial business and we have a responsibility to our shareholders and a broader responsibility to act within the laws and regulations of the State. And our company here fosters honesty and integrity and fair play, and overwhelmingly long-term investments require long-term decisions and some of them are going to be tough.

More broadly as an institutional investor dealing in lots of short and long-term investments, the renewable resources division, which is a very small affiliated part of it, is a group of foresters and accountants who are not typically investment professionals. They are passionate about forestry and they have a very long-term view. They are thinking in terms of not only 10-year contracts but also 30-year rotations and longer of timber.

Mr GREEN - Your role is specifically in forestry?

Mr JOLLY - I am a bit of a strange animal. My background is as a forester. That is my training. I have spent many years in consultancy and evaluation and appraisal and the last seven years with GMO as a forest investment manager, for lack of a more public handle for it. My role is to look for sound places to invest plant funds in timber, land and trees and to hold it for the long term and for the benefit of the businesses that we invest in along with the ultimate benefit of our shareholders.

Mr HARRISS - I am interested in this matter about the Taswood Growers situation and how it has developed and so on. Bob, can you indicate to the committee as to whether back in 1999 when the joint venture arrangement was negotiated, the softwood resource had been identified in Forestry Tasmania's corporate plan as a main undertaking? I am taking that definition straight from the GBE act, the definition of 'main undertaking.' You will understand the following question then would be, if it was identified as a main undertaking then it could not have been sold under the provisions of the GBE act.

Mr GORDON - To go back and explain the process at the time and I think that it was about 1997, we appointed a probity auditor from the private sector, because at that time the Victorians had basically sold all their current assets and all these probity auditors were around that had been through this and we wanted to make sure that we had the process right. We also appointed a commercial law expert who had done a lot of international dealings. We also formed a steering committee which included representatives from Treasury, the probity auditor, and an independent accounting firm, and someone else - there was someone else - and all of those issues that related to principal undertakings, authorities to enter into joint venture, were covered off legally by that legal team, and overseen by the probity auditor. When the transaction was completed there was a report from the probity auditor that we had met good commercial practice about going out to expressions of interest and how we had dealt with it, and that we had covered off the legal issues, some of which were the principal undertaking, others to do with establishing

a clear legal framework for it, and there was a separate Auditor-General inquiry into that about three years ago, about the land transaction that was carried out, associated with the softwood joint venture.

So for all of those issues we had a team of probity auditors, legal people and accountants going through to make sure we had both the supervision and a sign-off on those issues.

Mr HARRISS - Just specifically, can you identify for the committee now, or if you cannot, can you advise us at a later stage, whether in the corporate plan, I presume 1998 because that was the lead-up to the 1999 -

Mr GORDON - I think we started the process in about 1996-1997 and one of the probity auditor's jobs was to make sure that every time we did something that was in a separate legal entity from what was being proposed, things had been done in accordance with the law.

So there was legal advice on that particular disposal of a main undertaking. There was legal advice on the way the joint venture was set up. There was legal advice and business advice on using the - I have just forgotten what the act is called; something like the Forestry Rights Registration Act. This divided up the trees from the forests that used to be under Commonwealth profit a prendre. So there was a whole series of those things that needed to be done in order to satisfy both the supervisory committee, which included Treasury and the probity auditor, that everything that had been done had been carried out in accordance with the law.

I can go back and dig out those documents from - I suspect it was 1996, 1997, 1998 and 1999 - we actually had the process in place for quite a while before the transaction was undertaken. I just need to get a legal view about how I could provide that because the advice included information about the process we went through with competing bidders. I might be able to extract parts of that to answer your question.

Mr HARRISS - Mr Chairman, I accept, because Bob is on oath, he has given us the advice that the probity audits were conducted at that stage to ensure compliance with the law. I accept that. If other committee members want to pursue the matter which Bob is offering then that is somebody else's decision, but -

Mr BOOTH - I think, Mr Chairman, just on that point, Bob is offering to provide that documentation, albeit removing bits to do with commercial negotiation and so forth, so that will save some questioning of him on matters that are from a long time ago. The Treasurer's consent, for example, might be found in those documents and so forth, so I have no doubt that with the process -

Mr GORDON - There is a whole series of issues -

Mr BOOTH - that has been engaged in the committee should have that to look at.

CHAIR - Are you happy to table that document?

Mr GORDON - I will have to go back and have a look at it because I cannot remember everything from 1997 to 1999, but I can clearly remember the list of issues that we

needed to address in order to satisfy ourselves and GMO, whose legal adviser carried out due diligence on the transaction to ensure that we had done all the things we were required to do by law in order to complete the transaction.

Mr HARRISS - While on that theme, the whole issue before the committee's consideration does in fact go back to the 1999 joint venture. That is why we find ourselves in the position we are in today with the joint venture partners being delivered the right, through that negotiated action, to make decisions with regard to wood supply allocation.

Mr GORDON - Correct.

Mr HARRISS - Whilst we are aware, as you are, that section 12A of the Forestry Act can be, as a result of that negotiation, set aside if you like, wouldn't the Forestry Tasmania directors - representatives; yourself, Penny and whoever else you mentioned - on the Taswood Growers board take significant account of section 12A, or are you, as Taswood Growers, entirely focused on the best commercial return for the softwood?

Mr GORDON - I would like to answer a question that you did not ask which is: was section 12A taken into account when we entered into the joint venture? The answer to that is yes. As I said, we were in a position where we did not have and would not have, unless there was a change, a sustainable forestry sector in the softwood sector in Tassie, either in growing trees, managing trees, or processing trees because the estate was not able to support efficient processing.

Part of the presentations that we gave to the investment community said, 'We've actually looked at this; we've had a long, hard look at our strategy; if there's going to be a sustainable industry in Tasmania in the softwood sector we must expand the estate; we haven't got the cash but we've got to do something about doing that'. Again, there was legal advice and some debate on that issue at the time the joint venture was entered into and we consciously looked at the long-term employment implications of either doing nothing or entering into this arrangement. The presentations which we gave at the time, and the ones subsequently, all contained that as one of the key messages. We said to people, 'If you're not interested in sitting down with us and expanding the softwood estate, basically don't bother putting a bid in because that's one of our key objectives and it's one we hold dear'. As it happened GMO and a couple of other people said, 'Yes, we agree; we've done the analysis; unless you can get a bigger estate, more wood available so you've got the capacity for efficient domestic processing we're not interested either'.

We actually addressed that issue when we made the decision. You cannot have a commercial situation where two parties are going to have completely different ideas about how you deal with competing offers. They have to act as a commercial entity, which is the softwood joint venture. As people, and I think GMO and FT have quite similar drives in this, we do care about the long-term sustainable business otherwise you do not invest in trees.

Did we take into account that it was going to cause some disruption in the industry? Yes, we did. It was a difficult decision, but we had to balance what we believed were the long-term sustainability of the whole sector with two competing offers and it was difficult.

Mrs RATTRAY-WAGNER - I was the member that brought this term of reference to the committee and I want to answer your question about why you are here. You are here because we have a community that I represent that is unable to come to terms with what has happened with the FEA awarding of that contract. I just want to make it clear that is why we are here; to obtain some answers for that community so that at least they can move on if that is possible.

I want to ask about the structure of the joint venture agreement. According to our information, Forestry owns 50 per cent, a company by the name of Southern Hemisphere Softwood Strategy is another percentage shareholder and Tasmanian Softwood Fund Pty Ltd owns 25 per cent. Can you tell me about those two companies as the GMO component of this joint venture?

Mr JOLLY - GMO Renewable Resources represents over 400 clients, mostly institutional investors. In this case a majority are Australian institutional superannuation funds. They invest through a variety of vehicles for different reasons to do with their own structuring or whether they are investing with a commingled fund or beside a commingled fund. It is not uncommon for us to finish up in a situation where we are representing a shareholding with a number of entities underneath it, structured for the client's individual needs. That is what we have here.

Mrs RATTRAY-WAGNER - Those two other entities I spoke of, aside from Forestry Tasmania, both have a 25 per cent share, is that correct?

Mr JOLLY - I do not remember the exact shareholdings but they are roughly equivalent, yes.

Mrs RATTRAY-WAGNER - So 27:23 or maybe 25:25?

Mr JOLLY - It would be something a little less than that because there are some other institutional funds that are not represented by those two entities.

Mrs RATTRAY-WAGNER - Okay. Would it be possible for this committee to receive a copy of the sales agreement with Rayonier?

Mr GORDON - The sales agency agreement?

Mrs RATTRAY-WAGNER - The sales agency agreement, yes.

Mr GORDON - The only issue I have with that is it is a part of about 7 000 or so pages of legal documentation which we provided to the Solicitor-General in good faith because we understood that he was going to do the analysis on behalf of the committee. We asked him to return it because we have to make a decision as a board and there are structures in that which might give us a competitive advantage over other structures.

I have made everything available to the Solicitor-General which is what he asked me to do. I did not know whether that was at the committee's request. I did get a letter from the Chairman asking that I make the documentation available and when I said that I thought that it would be better to give to the Solicitor-General that is what I did. Again,

there is a legal confidentiality issue about the agreements themselves but it was all made available to the Solicitor-General?

Mrs RATTRAY-WAGNER - Thank you, Mr Gordon, I will follow that through with the Chair when we meet after this today.

Mr BOOTH - If within the envisaged expansion of the plantation estate to make local processing internationally competitive, it is contemplated that the resource will be put up for tender internationally and the entire standing crop is exported for a high price, was it not foreseeable in 1998 when you entered into this joint venture agreement that potentially the agreement that you went into could do nothing more than provide an export opportunity and not necessarily provide any long-term sustainability to local mills in terms of an expanded world-scale resource?

Mr GORDON - The analysis that we went through at the time was based on independent advice. At the time we were facing a high probability that unless we did something to expand the estate and spend more money, particularly on silviculture, the most likely result of doing nothing was the vast majority of the wood being exported unprocessed, because we would not have had the volume or the capacity to have efficient processing. If the mills at Scottsdale had still been processing 64 000 cubic metres of logs they would have shut a long time ago.

The only way you can have efficient and competitive downstream processing is to get some economies of scale, which was the driver of going into this softwood joint venture in the first place. Sure, you are always making judgments about future markets but the strong advice we had was that the best chance to have long-term sustainable domestic processing and therefore a growing industry that had options about getting a fair return for product was to expand the estate and there was not the capital available either from Mr Groom's Government or Mr Rundle's Government or the Bacon Government to do that so we had to get external capital and we had to do it in a big way with someone who was preferably experienced in the forest sector, and that is what we ended up with with the GMO entities.

Mr BOOTH - Okay, you have sold half of the resource for seven years for \$48.8 million - I think that was the money that was paid up front for the standing resource at that point in time. Presumably that meant it valued that standing resource and its value in terms of asset generation over the next seven years, albeit with further investment from returns from sales at just under \$100 million for the resource.

You keep getting back to justification for it in terms of the collapse of the local processing. Ought you not have put into that 1998 agreement some requirement that local processing be an important consideration or should not some sort of priority have been given, or are you just prepared to simply allow an agreement to be struck that in fact gave no such guarantee of jobs in the future, because that seems to be what has happened? Although you have signed a deal with FEA that does process a portion of that product here at the moment, it is also true that there is no restriction to those logs being exported that do not make the current mill requirements into the export market.

Mr JOLLY - Isn't it the proof of the pudding that we have entered into those arrangements and that they are for the vast majority of the sawlog that we can produce for the next 10 years?

Mr BOOTH - Well, I was asking Bob whether in fact he felt it should have been part of the original agreement with GMO that they would go into . I accept what you have said before in that regard and, yes, it is a demonstration that a big part has been awarded locally but I would like to follow on from what Bob has to say.

Mr GORDON - I said the judgment at the time was: what has the greatest likelihood of allowing an efficient growing and processing sector? We knew, based on all the advice we had, that if we did nothing we would not have a domestic processing sector.

Mr BOOTH - You say you hoped for an efficient, world-scale processing sector but the nature of the agreement was such that there was no impediment to export that resource and not have any local processing.

Mr GORDON - At the time I think there were Federal Government log export licences in place. Forestry Tasmania had exported logs in the mid-1990s.

Mr BOOTH - Wasn't that expunged in about 1996 or something?

Mr GORDON - November - I cannot remember the date but 1997 when the RFA was signed. All of the analyses that we had done suggested - and Ian has a lot more experience in this than I have - that it would be very, very unusual behaviour for a forest grower not to want to sell most of their product to an efficient domestic processor because that is where you are always taking this risk. You are taking less exposure to foreign currency exchange, shipping, oil prices and all those sorts of things.

Mr BOOTH - When that deal was signed in 1998 those export restrictions had been removed by the RFA, is that correct?

Mr GORDON - Just, yes.

Mr BOOTH - So in the deal that has been struck with FEA, part of that deal enables processing to occur immediately of the smaller end section logs but there is a substantial portion of the big logs that we have heard in evidence today and it is blindly obvious that those logs will either be exported as whole logs or stand on the stump, 'on the hoof', as they say. When that deal originally went down, was it your understanding then that FEA would be exporting the big end section logs if they could not process them here locally?

Mr GORDON - Obviously you need to ask FEA. I think they are appearing -

CHAIR - They will be appearing this afternoon.

Mr BOOTH - No, that would affect your cash flow; that is the point I am getting to. Did you understand that your cash flow could be -

Mr GORDON - We understood that our cash flow would potentially take a hit during the 12 months or so of transition. As Rayonier probably would have said too, there are a whole

lot of other options about changing the mix of forests. There are a whole range of other things that can be done to make that easier, and Rayonier is working on all those issues. Again, it was not an easy decision.

Mr BOOTH - No.

Mr GORDON - It was a decision that had to be taken, in what we believed was the best long-term view.

Mr BOOTH - So the JV had contemplated that a quantity of these logs may be exported, not processed locally at least until a new milling facility was set up or alternative arrangements made.

Mr GORDON - Well, the joint venture contemplated a whole lot of options.

Mr BOOTH - But that was one of them?

Mr GORDON - That is a subset of them, yes.

Mr BOOTH - Alternatively then, the proposition is that the joint venture has entered into an agreement with FEA that enabled them to simply leave standing those big end section logs, and not pay for them until such time in the future when their mill would be in operation and would take them. So you were prepared to accept a tender that gave you a short-term pain perhaps, but from what you are saying in the long term it was a better commercial return over a 10-year period.

Mr GORDON - Obviously, when you are managing forests you take a long-term view, and that is normally done. I do not know anyone who would look at some sort of MPV in less than seven years, because it is normally seven to 30 years. You have to take a long-term view. Markets go up and down; the nature of the markets are quite cyclical so you need to take a long-term view.

Mr BOOTH - Given what we have just been through with the prospect of logs being exported and the prospect perhaps of there being a reduction in cash flow to the joint venture, what advice did you have that the FEA contract was so good for the long-term future of the industry that you were prepared to take it away from a company that had just invested \$35 million the previous year in processing the facility? It has had experience in the industry since, presumably, the 1960s or so in terms of processing, and operates mills in other States of Australia and exports timber globally. How did you make the value judgment that they would not, in turn, be able to streamline their production methods to prevent the inevitability that you have been alluding to, I think, that they in fact would have become uncompetitive, and therefore somehow unable to deal with the product or something? It just seems a perverse sort of a logic. I do not understand where you are coming from that you would make that judgment on behalf of your customer.

Mr GORDON - We made the judgment on the submissions that had been made by the two competing bidders, and we sought independent, expert advice on likely industry structures, competitive forces, on a whole range of issues, and we made our judgments based on the information and proposals that each of the bidders had made.

Mr BOOTH - So under the terms of the contract with FEA, is it a 10-year contract with an option to renew, or is it simply just a 10-year contract with no renewal exercisable options?

Mr GORDON - Mr Chairman, I am reluctant to go into the commercial details of the contract with one party without getting both parties to the bid giving permission for that, because there were bits that each bidder put in which were peculiar to their bids. I seek your guidance on that.

CHAIR - Yes, I will check that.

Mr BOOTH - Could we have it provided perhaps in confidence to the committee, in camera?

Mr GORDON - Well, I understood there was correspondence about getting each of the parties' agreement to that. I do not know has happened with that, with FEA and Auspine.

CHAIR - In terms of any commercial -

Mr GUTWEIN - We are crossing over into a -

CHAIR - Yes, Rayonier did write a letter.

Mr GORDON - And the Auditor-General, as I understand it, has had access to all that information on the basis that it was confidential to his enquiries.

CHAIR - Yes, I am just conferring with the secretary there, and if it is a decision of the committee that we require commercial-in-confidence material we can request it.

Mr GORDON - What I am pointing out is that we're really the custodians of that on behalf of the people who own the commercial information, and I'm just pointing that out that there are - well, I believe it needs their agreement to provide information; they've provided it to us in confidence, that contains what they believe to be commercially sensitive information. As I said, I understand all of that was provided to the Auditor-General because they had agreed to provide it to him.

Mr GUTWEIN - I would have thought, Chair, that if we wanted to request a particular document from any particular witness or entity that appeared before us we could do so, could we not?

CHAIR - That is the case, yes.

Mr BOOTH - I am happy, Chair, that that not be a public document. I am not objecting at all to the commercial in confidence, but I think it is necessary for us to seek that in order to drill down to whether the deal was like for like and whether in fact the Auspine bid has been is being fairly treated.

CHAIR - We will continue our line of questioning but we can deliberate on that and then decide as a committee as to where we go with that.

Mr GUTWEIN - If I can just get clarification from Mr Jolly first of all; it's on a minor matter but it's one that I think is important. You made the comment that customers had been telling you that prices had to drop. Can I just ask the question whether Auspine's final bid or any of the bids that it made through the process were actually less than what they'd been paying for their current -

Mr JOLLY - At various stages in the process, yes they were.

Mr GUTWEIN - So they were providing bids that were lower than -

Mr JOLLY - I don't want to wrap it up in a bid, and I wasn't directly involved in the negotiations of the discussions at that time. It was the domain of our manager, but the information that we were given back was that various offers leading up to and as part of the process were at prices lower than we had previously been receiving.

Mr GUTWEIN - And what about the final bid that they made; the final offer that they made?

Mr JOLLY - It was at a different level altogether.

Mr GUTWEIN - Rayonier mentioned that the issue of mediation was taken to the owners last year. Could you explain to the committee why that offer wasn't taken up, and if I could put a context to my question, if long-term sustainability has been one of the key issues for the owners throughout this process and whilst the market we understand was an imperfect market with effectively one major seller, one major purchaser; when negotiations broke down between your major domestic purchaser, why wouldn't it have been prudent to have entered into mediation if the backdrop that effectively you've indicated you were operating in was hoping to have a long-term sustainable industry - why wasn't mediation viewed as being an important part of the process?

Mr JOLLY - Well, it was debated at length at the time as to whether it was an appropriate process to move forward or not. Our experience to date is that mediation or even arbitration is a process that you follow down when you're in a bind between two contractually committed parties; if you're in a contract already and you've come to a situation where you can't agree on something you're going to have to have a relationship going forward so you either have a mediator or an arbitration or you follow whatever provisions are in your contract to resolve impasses. This wasn't a situation where we were at loggerheads over an existing contract. This was us attempting to go to the market in an open and transparent way and let the market speak, so the inter-mediation with one party did not at all seem appropriate, and it was not entirely clear to me at that stage that we were only ever going to be presented with offers from one party, yet to go into mediation with one party would imply that we were. It just didn't seem to me to be appropriate at all, but that's just my view; there were other views on the board and Bob will have a view as well I'm sure.

Mr GUTWEIN - When the original tender was let, how many parties indicated that they would be interested in such a larger parcel of what Auspine was bidding for?

Mr JOLLY - I would have to check with the minutes as to exactly how many there were but there were obviously two major players at that time, Frenchpine and FEA. There were other parties who were interested in coming to Tasmania and perhaps becoming established here who looked at it at the time; there were several other parties.

Mr GUTWEIN - Throughout the process that Taswood Growers were negotiating with Auspine up until when FEA came on the scene in November, did they go out and attempt to find other parties to enter the process or solicit bids?

Mr JOLLY - No, the process was managed by our managers. We were conscious of following a fair and rigorous process where the wood was made available through the manager, our sales agent, on a fair and transparent way so that anybody who had an interest in the resource and processing it here in Tasmania had every opportunity to negotiate with the manager and put in a tender.

Mr GUTWEIN - In regard to the issue of longer-term sustainability, can you explain why Auspine's offer was not considered to be a long-term sustainable proposition?

Mr JOLLY - It was less attractive to us. We had two offers at the end of the day and it was less attractive to us than the other offer. One of the criteria was long-term sustainability. The competing offer was based on a state-of-the-art, world-scale processing facility and the other was based on two sawmills. We have not seen any details of how they intended to make them competitive. It was a view that we arrived at consistent with the position that was being put to us by an independent consultancy group. We have seen massive investment on mainland Australia and we are seeing it now in New Zealand and other parts of the world where to compete in the solid wood-processing business requires scale, technology and innovation. One proposal had it in plenty and the other was silent on that.

Mr GUTWEIN - Did the board receive advice from an independent consultant on this matter? I think Bob might have indicated that there was a range of independent consultants.

Mr JOLLY - Yes we did. We are not abdicating our responsibility for this decision to them. We in our own right, as does Rayonier, own and operate a lot of forest elsewhere in the world. We have views based on our experience from elsewhere. And in this case Tasmania was not the mainland Australia and it is not New Zealand, and we wanted somebody else's view so we sought and we took those views.

Mr GUTWEIN - I just wondered whether or not that advice could be provided to the committee. As Tania Rattray-Wagner indicated, the key issue here that this committee is working towards is hopefully being able to provide some explanations to the community so that they can understand what has occurred. So could we request that that advice be provided to the committee and if at all possible, through you, Chair, if we could get the board minutes of the particular board meeting that made the decision?

Mr GORDON - I am just wondering how that is relevant to the terms of reference -

Mrs RATTRAY-WAGNER - It is the process that led to the supply decision.

Mr GORDON - in reference to State and Commonwealth laws. Is there a suggestion that the joint ventures have broken some laws?

Mr GUTWEIN - There are two terms of reference with regards to the committee; one of them goes to the process and I think very clearly you referred to number 2 there, to 'the process that led to the log supply decision with reference to'. With regards to 'reference to' it is the process that I am interested in and I think that we have to request that information.

Mr GORDON - With respect to which laws are you suggesting might have been breached?

Mr GUTWEIN - It is just in reference to the process. I do not think that it is actually explicit that it has to be in regard to any relevant laws that may have been breached.

Mrs RATTRAY-WAGNER - Through you, Mr Chairman - ultimately it is the decision that has been made that is difficult to understand for the north-east community. And not only the north-east but also other parts of the Tasmanian community. So it is extremely important for this community and these people who do not have a future after 31 March to comprehend or understand this process. So hence the reference to process.

CHAIR - That is something that the committee can request, in my view.

Mr GORDON - Did the committee request minutes of board meetings of the bidders?

CHAIR - Mr Gutwein, what were you actually after again?

Mr GUTWEIN - If we are going to the decision made by Taswood Growers, firstly, I would like to see the advice that was provided to assist Taswood Growers in its deliberations and, secondly, the minutes of the board meeting at which this decision was made.

CHAIR - I am aware that the time is past 1.30 p.m.. After lunch we have Mr Gordon back again for a short while and then we have FEA so if we can, I would like at this stage to pull stumps.

Mr BOOTH - Can I ask one question very quickly regarding the provision of information?

CHAIR - Yes.

Mr BOOTH - Thank you.

Ian and Bob, you suggested before that a big part of the decision was based on the long-term sustainability and capacity of the mills to compete internationally on a world-scale mill with appropriate technology and so forth. It seems odd to me that as a seller of a volume of wood, provided the person who is buying it has the capacity and in Auspine's case it is undoubted that they had the capacity from history to not only buy but to survive in a competitive environment and to pay for their wood, that it would be of such special interest to Taswood Growers that they would want to know what their processing facility was going to provide.

It is also on the record that FEA's plan A, I believe, was to pick up either one or two of the Scottsdale mills when Auspine fell over as a result of not getting any logs and plan B was to construct a second mill. Now if that is the case, how can you say that these negotiations that were so pre-eminently concerned with the capacity to process were based on that factor?

Mr GORDON - It is based on a false premise. You should ask FEA that.

Mr BOOTH - So you can attest to this committee that from day one FEA's enhanced processing capacity by the construction of a new mill at Bell Bay was part of that initial proposal?

Mr GORDON - Yes.

CHAIR - Thank you. I would like the committee to remain for a couple of minutes while we deliberate.

THE WITNESSES WITHDREW.