Quintis Limited (ASX:QIN) - formerly TFS Corporation Limited

Money Doesn’t Grow on Trees

- Bogus sales channels.
- Directors skimming cash through round robin scheme, which concurrently allows Quintis to artificially boost sales.
- Fictional institutional sales - Quintis books revenues which are intermittently used to gain access to debt finance, before being written off.
- Debt finance used to engage in Ponzi-like behaviour
- Viceroy’s price target for Quintis is **$0**. The scenario is reminiscent of historical MIS ventures such as Timbercorp and Great Southern, both of which are now defunct (consensus with Glaucus Research Group).

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1. Prelude

We have been looking into TFS/Quintis for almost a year now, and came to very similar conclusions to those of Glaucus Research Group's article published on 22 March 2016.

We don't think that a follow up is entirely necessary as it's quite clear how poorly the business is performing. However, there are some *instrumental* Ponzi-like historical events not yet covered, and should be brought to the attention of stakeholders.

Note that most of our research was completed prior to TFS rebranding as Quintis. We have not amended our notes to reflect the change in company name, but assume TFS means Quintis.

2. Summary Short Thesis

We believe TFS has utilized aggressive accounting practices, poor disclosure and marketed questionable sales channels in order to:

- Unrealistically portray the attractiveness of the underlying business model
- Unrealistically portray market growth projections
- Obtain access to further finance

We price TFS equity at $0.00.

Bogus Sales Channels

TFS's alleged sales channels include:

- A mysterious Chinese buyer, Shanghai Richer Link, who was uncovered by Glaucus to be a sandalwood smuggling ring.
- Medinext, who we believe could be evading import duties similarly to Shanghai Richer Link by undervaluing sandalwood exports on their customs data.
- Young Living, an essential oils MLM scheme that frequently receives warnings from the FDA because its sales agents claim, amongst other things, that their essential oils can cure diseases including Ebola.

Questionable Accounting Practices

TFS's revenue recognition policy allows it to **book revenues before any cash is realised or any contract is executed**. TFS recorded large sales to third-tier institutional MIS investors (glorified financial products salespeople) where cash was never realised.

TFS leveraged these fictitious revenues in order to gain access to financing through bond arrangements.

Directors Skimming Cash through a Finance Round-Robin.

TFS Founder and CEO Frank Wilson has been skimming cash from the business, facilitated through a loophole created by combination of TFS's promotional buyback policies and the Arwon investor financing subsidiary. The Arwon facility was initially established to facilitate a **tax evasion scheme**.

We believe the Arwon Round Robin scheme allows management to discretionally and artificially adjust top-line agricultural plot sales.

Misleading Marketing Material

As previously highlighted in the Glaucus report, TFS has historically engaged Incipient Capital to provide market projections and broker sales for TFS institutional investments while its founder and MD, Phillip Shamieh, is also a director of TFS's wholly owned subsidiary Gulf Natural Supplies.

Incipient Capital shares a financial services license with another of Shamieh's businesses, Wise Owl, an equity investment research firm who frequently promote "buy" rating reports for TFS.

We believe the consequence of the above indicate fraud and/or stock manipulation. Most certainly there is a conflict of interest.

TFS also engaged Dr Padmanabha, a sandalwood expert cited as an "independent" source of sandalwood demand studies. Coincidentally, it appears Dr Padmanabha's research has contributed in driving at least three other sandalwood investment schemes into the ground. Dr Padmanabha also runs his own investment scheme in India.

TFS's expert reports project the Sandalwood market will grow 5x by 2025. They appear to defy basic economic principles by charging the same luxury goods price for their product despite flooding the market with supply.

We believe TFS intentionally uses misleading statements, biased research and seriously questionable accounting practices to inflate the value of both the sandalwood and the company itself.

3. TFS: Background

TFS Corporation operates the world's largest legal Indian Sandalwood plantations located throughout the Australian tropics. The company funds its plantations through a Managed Investment Scheme (MIS) structure. For those unfamiliar with this model, we urge you to refer to the below article for background:

The Danger of Managed Investment Schemes:

http://www.moneymanagement.com.au/features/editorial/danger-managed-investment-schemes

Currently, ~70% of TFS plantations under management are owned by MIS investors, who are then entitled to the proceeds of sales. TFS charges maintenance and harvest fees either upfront or annually (elected by the investor), and TFS clips the sales if a predetermined target sale price threshold has been reached in the form of an incentive. For more information, please refer to the product disclosure statement. Note that the investment is tax deductible in Australia.

TFS owns and operates a Sandalwood Oil extracting facility, Mt Romance, which is entitled to government contracts for wild harvests as a further revenue source.

The Sandalwood

Indian Sandalwood produces an aromatic heartwood, which can be processed for use as timber (worship carvings) and oil (perfumes, cosmetics, incense). The tree is both commercially and biologically difficult to grow as[1]:

- It is a root parasite, meaning it requires plants to grow around it.
- Survival rates for the plant are typically low, especially in the first year.
- It requires 15-20 years to grow to commercial maturity (i.e. heartwood content is maximized).
- Host plants are not re-usable.

[1] http://researchonline.jcu.edu.au/23336/1/Page_2012_%234904.pdf

Conditions Necessary for Success

We believe sandalwood growers generally need to fulfill 4 conditions for success:

1. Yield Expectations
   Sandalwood trees in plantations have historically low rates of survival and are dependent on weather, pests and disease control and the condition of their host plants. A lead time of 15 years means that projections of survival need to be accurate in order to ensure that enough plants are left to make a profitable venture.
2. Price projection accuracy
   A lead time of 15 years means that the price of sandalwood products has to be predicted 15 years ahead of any realizable sales. An inaccurate price projection may threaten the profitability of the crop, or the entire feasibility of the project. Changes in the legality of sandalwood harvesting and limits on wild harvests have significantly changed the landscape of the sandalwood industry.
3. Market demand projection accuracy
   As above, the demand must be forecast 15 years ahead of time. TFS's most FY16 earnings presentation projects the market will remain flat until 2020, and subsequently grow 5x by 2025.[2]
4. Ability to maintain solvency during growing period
   Sandalwood farming is a capital-intensive and time-intensive activity requiring labor and host plants in addition to other farming expenses. For at least 15 years it can be expected that the business will generate little to no cash revenue. During this time the business must either have significant cash reserves or other means of raising revenue (in this case, as a MIS).

[2] TFC FY 2016 Earnings Presentation - http://www.tfsltd.com.au/files/2414/7216/9297/Presentation_-_FY16_Full_Year_Results.pdf

4. The Main Companies.

Quintis Limited (ASX:QIN) – Formerly TFS Corporation Limited (ASX: TFC)

Manages world's largest Sandalwood plantation

Arwon Finance Pty Ltd

- Investor loan facility wholly owned by TFS.
- Previously **facilitated the EKS tax evasion scheme**.
- Currently **facilitates a round-robin loophole to the benefit of management.**

Wilson and Atkinson

- Tax specialist law firm based in Western Australia.
- Founders: Frank Wilson and Steve Atkinson
- **Involved in several tax-evasion cases against the ATO on behalf of MIS investors in the 2000's.**
- Also **provided legal services for TFS.**

East Kimberly Sandalwood

- Precursor to TFS.
- Provided first TFS harvest of Sandalwood.
- Came under investigation in the 1990s. **Investments deemed tax evasive.**

Incipient Capital

- Investment services company based in Sydney, Abu Dhabi and Tanzania.
- Shares the same director as TFS subsidiary Gulf Natural Supplies: Phillip Shamieh.
- Operates under financial services licence of Phillip Shamieh's other business, **Wise Owl, who frequently promote 'buy' ratings for the stock.**

Shanghai Richer Link

- Exclusive TFS sales agent to China and India
- Exposed by Glaucus as having basically no assets to substantiate purchases as TFS's largest customer.
- Turned out to be a sandalwood smuggling ring.

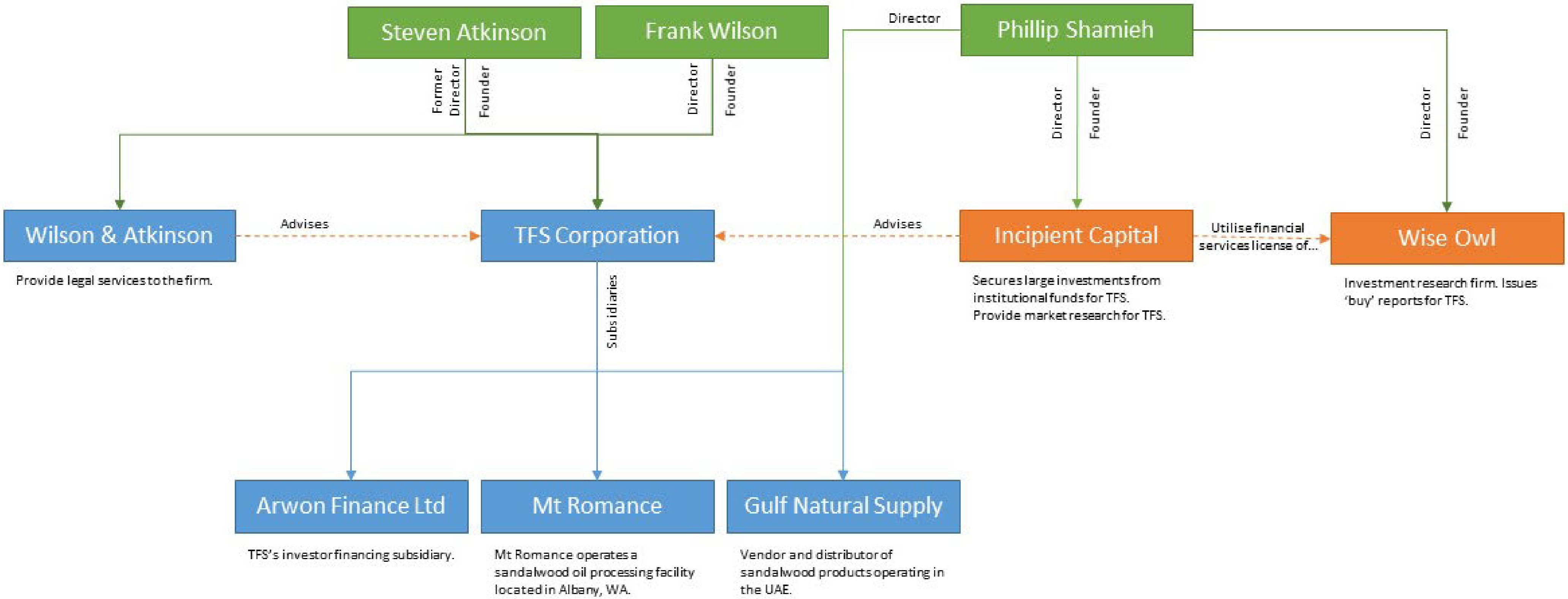


Figure 1 Organisational Structure

5. Questionable Accounting Practices

"Money you haven't earned is not good for you."

- *Robert Maxwell*

Our research indicates that TFS's aggressive accounting practices together with a discretionary revenue recognition policy allow it to book revenues well before cash payments. We believe this allows TFS to obtain access to further funding.

We demonstrate several occasions where TFS has booked revenue from wholesale investors on what we believe to be "exclusive" misleading terms, and **where cash payments were never received.** Further, we delve into the prospectuses of a third parties (referred to by the company as a "German Institutional Bank"), which we believe highlight the ability of institutional funds to withdraw from the investment after just two years, while the assets remain (literally) planted in the ground.

We have arranged the events pertinent to this discussion in chronological order as timing is a key component in understanding the Ponzi-like nature of the business.

The FY 2009 – FY 2010 Key Events

Pertinent to this discussion is the way in which TFS recognises sales revenue, particularly MIS investor revenue.

Since FY 2009, TFS's policy allows revenue to be recognised in "proportion to the establishment work performed at balance date", rather than when the contract is entered into or when cash is received[3]:

(z) Change in Accounting Policy

The economic entity changed its accounting policy in relation to the recognition of its establishment fee revenue for the year ended 30 June 2009. Establishment fees were previously fully recognised in the year that the application or contract was entered into. The economic entity has now chosen for establishment fee revenues in connection with sale of timber lots under an MIS project or under other timberlot establishment contracts to be recognised in proportion to the establishment work performed at balance date. In arriving at the proportion of work performed to balance date all activities relating to product development, marketing and distribution, land procurement and development, seed collection and propagation, planting, and other establishment activities are taken into account.

The directors are of the view that this change results in more relevant and reliable financial information as the structure of the establishment fee contracts is now more akin to the provision of a service.

Figure 2 Accounting Policy

TFS also introduced its Beyond Carbon (**BC**) initiative in FY 2009, where sophisticated investors can subscribe for $1M worth of units in a trust which:

- Contracts TFS to plant and maintain 7ha of new plantations ($595k);
- Purchases the land outright from TFS ($105k); and
- Uses the remaining $300kto buy-out existing investor lots in a secondary market

Why is all of this significant? Because **the revenue recognition policy now allows TFS to recognise sales to the unit trust before contracts are entered into!**

The **same 1 July 2009 Market announcement** discloses that an application has been received for the Beyond Carbon initiative by a sovereign wealth fund; the Emirates Investment Group (EIG):

[3] TFC FY 2009 Annual Report
http://www.asx.com.au/asxpdf/20090929/pdf/31l0k4zxvcpxq6.pdf

> • TFS has attracted non-MIS investment for the first time with an application received for 350 hectares in the new 2010 Indian Sandalwood plantations amounting to an investment of $35m, and a further $15m into the purchase of existing Indian sandalwood plantations in the secondary market

Figure 3 Non MIS Investment 2009

The EIG also agreed to establish a joint venture entity with TFS called Gulf Natural Supply (51% EIG, 49% TFS) which would be committed to promote investment from the Middle East and North Africa into BC[4]:

> Joint venture company established – Gulf Natural Supply (GNS). GNS entered into a supply agreement with MRA to supply Australian sandalwood (Santalum spicatum) to the Middle east and Northern African ("MENA") region
>
> EIG have underpinned the investment of a minimum of 200 ha per annum into BC, with FY09 sales of 350 ha already exceeding expectations

Figure 4 TFS JV Gulf Natural Supply

The cash for the 350ha Beyond Carbon plantation are not expected to be received until **at least mid-2010, the same time plantations commence**:

> Funds for plantation hectares applied for under the Beyond Carbon structure are expected to be received by April 2010 when planting is scheduled to occur.

Figure 5 Expectation of Funds by April 2010

And yet, in their earnings presentation, TFS advises that it has recorded sales for the Beyond Carbon plantations to the value of ~$29m[5] over FY 2009 and FY 2010:

[4] TFS Corporation FY 2009 AGM presentation
http://www.asx.com.au/asxpdf/20091119/pdf/31m59wv7711rbs.pdf

[5] TFS FY 2009 Earnings Bell Potter Presentation
http://www.asx.com.au/asxpdf/20090914/pdf/31kqbsggwxx8c6.pdf

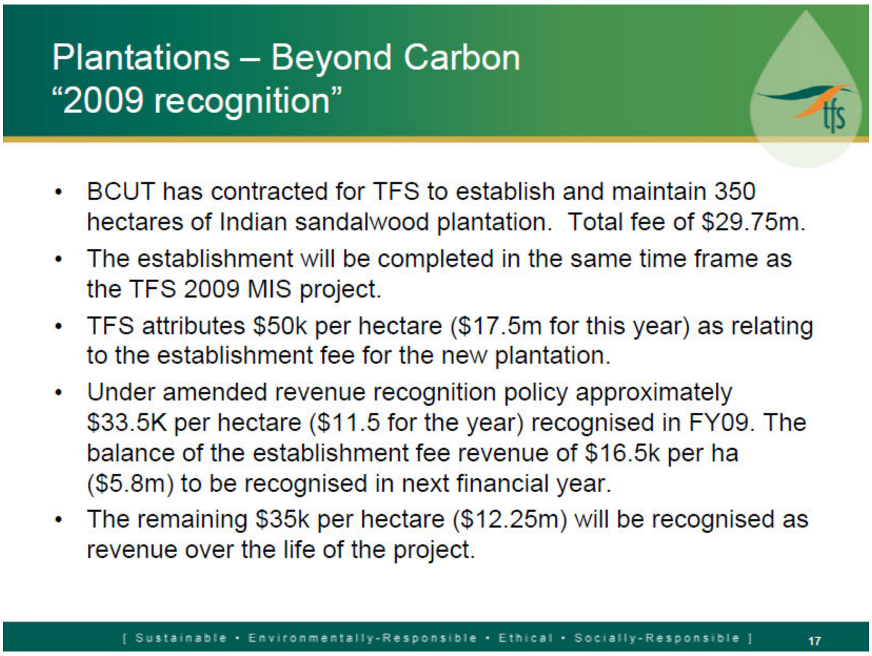


Figure 6 Beyond Carbon Presentation

TFS claims that the issue of risk is mitigated through the assumption that the value of the plantations (which TFS can reclaim in the event of default) is allegedly greater than the cash value of the debts[6]:

- In the event of MIS bad debts, TFS has no additional security for the receivable beyond the underlying trees and the legal obligation to pay. This risk is ameliorated by the fact that TFS can assume ownership of the trees which may have a value in excess of the debt owed.
- In the event of non-MIS bad debts from the Beyond Carbon project TFS has no additional security for the receivable beyond the underlying trees and the legal obligation to pay and faces the additional hurdle of enforcement against an overseas debtor. This risk is ameliorated by the fact that TFS can assume ownership of the trees which may have a value in excess of the debt owed.

Figure 7 Risk Mitigation in the event of bad debts

The FY 2010 Key Events

Fast forward to February 2010; TFS's earnings presentation reaffirms that FY 2009 BC cash is to be received by April 2010, but alludes to a risk of non-payment by **stating future BC sales will be on a cash basis**[7]:

First round sold 350 ha for a fee of $29.8m, cash to be received by April 2010 – on track
Second round of ~500+ ha is also on track for June, with sales to be on cash basis

Figure 8 1st & 2nd Beyond Carbon cash position

[6] TFS FY 2009 Bell Potter Earnings Presentation
http://www.asx.com.au/asxpdf/20090914/pdf/31kqbsggwxx8c6.pdf
[7] TFS HY 2010 Earnings Presentation
http://www.asx.com.au/asxpdf/20100225/pdf/31nxdkfv3vx555.pdf

By May 2010, the Beyond Carbon investor has defaulted on payment and been granted extended credit terms:

> **4. Update on 350ha sold in 2009**
>
> In FY09 TFS sold an investment of 350 ha to the first non MIS wholesale investor (not connected to EIG). At the time, TFS set extended payment terms, with payment due by April 30, 2010. The extended payment terms were part of an introductory offer to the first client of this new product initiative for TFS and were designed to align payment with the planting of the investment during the April to June planting season. The investor concerned has not met the April deadline for payment of all the funds but TFS is confident that full payment will be made by 30 June 2010.

Figure 9 Extension of Payment

Fast forward to TFS's FY 2010 results and any mention of the outstanding institutional investor's payment is non-existent. However, the breakdown of receivables shows a ***massive growth*** **in amounts outstanding from institutional investors despite management's prior assertion that future BC sales would be on a cash basis!**

NOTE 5: TRADE & OTHER RECEIVABLES (CURRENT)	2010 $'000	2009 $'000
Trade Debtors (a)	79,257	41,035
Provision for impairment of receivables	(327)	(2,850)
	78,930	38,185
Loans to growers (b)	7,165	11,507
Bonds & deposits	45	40
Prepayments	800	282
	86,940	50,015

(a) Included in Trade Debtors are amounts totalling $68.549m due from four institutional wholesale customers. These amounts relate to the sale & establishment of sandalwood trees as well as sub-divided land known as 'Kingston Rest' shortly before balance date. These wholesale sales are subject to normal commercial settlement terms which included the issuing of new title deeds by Landgate as well as Foreign Investment Review Board clearance, both of which were outstanding at balance date. The directors believe that once these conditions are satisfied the amounts outstanding will then be paid in accordance with the relevant sale agreements.

Figure 10 Receivable increases due to default in payment

The FY 2011 Key Events

Investors are once again reassured that payment for settlement of FY 2010 BC sales (500ha) and most FY 2011 BC sales will occur in FY 2011[8]:

> Trade debtors of ~$70m reflect
>
> - Fees to be received throughout the course of FY11 from wholesale investors once the subdivision of the Kingston Rest property is completed and new titles issue. These settlements will occur progressively commencing in September 2010.

Figure 11 Likely receipt of fees

[8] TFS Media Announcement - 31 August 2010
http://www.asx.com.au/asxpdf/20100831/pdf/31s6tmlc90mp87.pdf

Yet the FY 2011 accounts still show **receivables outstanding from the FY 2010 “cash basis” institutional sales**[9]**:**

NOTE 5: TRADE & OTHER RECEIVABLES (CURRENT)	2011 $'000	2010 $'000
Trade Debtors (a)	66,679	79,257
Provision for impairment of receivables	(256)	(327)
	66,423	78,930
Loans to growers (b)	6,262	7,165
Bonds & deposits	5	45
Prepayments	1,292	800
	73,982	86,940

(a) Included in Trade Debtors is an amount totalling $31.570m of which $12.100m relates to 2010 and an additional $19.470m relating to 2011 sales which are due from an institutional wholesale customer. These amounts relate to the sale & establishment of sandalwood trees as well as sub-divided land known as 'Kingston Rest'. It was agreed with the debtor to allocate plantings to another block at Kingston Rest. As such, the plantings will occur in 2012 and as a consequence it was agreed to change the settlement terms for repayment to June 2012.

Also included in Trade Debtors is an amount totalling $25.008m relating to sales, from another institutional wholesale customer, which were recognised in FY2010 The Group has agreed to extend the customer's payment terms until December 2011. The directors believe that it is highly likely that this debt will be recovered in this timeframe as funds are currently being raised via prospectus that is being distributed by a large European bank. Since invoice date to report date the customer paid $1.401m towards settling the debt. The trees have been established at 30 June 2011 and serves as security over the outstanding debt. At balance date the value of the trees were $26.810m, this valuation is based on the assumptions as set out in Note 12.

Figure 12 Outstanding receivables 2010

Note that a quick calculation by us on the $25m outstanding amount from FY2010 equates to approximately 380ha. Remember this number.

We also note that a 610ha Beyond Carbon investment was not recorded as the land subdivision had not yet been completed, thus leading TFS to fall short of its profit guidance. TFS claims all revenues would be recorded in FY 2012 instead of the usual two-year stagger as TFS had already completed the establishment works[10]:

The lower profit results reflected two key themes –

- The application of accounting standards provided that the sale of a wholesale investment of 610 ha could not be treated as revenue in FY11 as TFS had yet to secure rights over attributable land. This treatment only related to a timing issue. Since balance date, TFS has secured the necessary land for this sale. Subsequently, the sale will be treated at 100% for revenue recognition purposes in FY12, as all work under the provision of services accounting standard, will be completed in the current financial year.

Figure 13 Justification for Lower Profits

The FY 2012 Key Events

TFS’s FY 2012 results indicate that the payment for the 610ha lot is actually contingent on the ‘German Institutional Bank’ successfully raising funds through a prospectus, as the bank itself is not underwriting the investment[11]:

[9] TFS FY 2011 Annual Report http://www.asx.com.au/asxpdf/20110930/pdf/421g4f71yml035.pdf
[10] TFS FY 2011 Annual Report http://www.tfsltd.com.au/files/4414/2727/6499/Annual_Report_2011_WEB.pdf
[11] TFS HY 2012 Interim Report http://www.asx.com.au/asxpdf/20120229/pdf/424pr5vl3gd9ml.pdf

The Group has a further amount due to it by 30 June 2012 from another wholesale investor totalling $40.26m, being for establishment fees on 610 hectares of land and plantation located in Queensland. This amount forms part of an investment fund known as 'Beyond Carbon' which is being promoted by a large German institutional bank. The payment of this amount is dependent upon the success of this fund attracting sufficient investors. The impact of this transaction is to increase the net profit after tax for the period by approximately $8.5m.

Figure 14 German Institutional Bank Promotion.

The FY 2012 results then claim only 580ha of institutional lots were sold, and that the cash had not yet been received[12]:

TFS generated establishment fees across both wholesale and retail products of $51.2m (2011: $43.5m). Wholesale sales volume decreased 27.9% to 580 hectares, whereas the retail MIS product experienced an upward trend of 28.9% to113.8 hectares.

Figure 15 Lower Insitituonal Sales Accounts 2012

(a) Included in Trade Debtors is an amount totalling $38.28m relating to a signed contract with a wholesale investor for the establishment of 580 hectares of plantation in Queensland. This amount forms part of an investment fund known as 'Beyond Carbon' which is being promoted by a large German institutional bank. Under the terms of the original contract the investor was to complete the transaction on or before 30 June 2012. The Group has since agreed to extend the deadline for payment until 31 December 2012, as payment of this amount is depended upon the success of the German institutional bank attracting sufficient investors. The establishment services over the 580 hectares have been completed and as such, the plantation is now in existence and being maintained. At balance date the value of the trees were $42.43m, this valuation is based on the same assumptions used by the Group in valuing its own trees.

Figure 16Group Assumptions on Valuation of its 'own' trees

Considering $38.28M was added to receivables the year before, the new figures appeared to show a similar amount had been converted into cash year-on-year.

NOTE 6: TRADE & OTHER RECEIVABLES (CURRENT)	2012 $'000	2011 $'000
Trade Debtors (a)	71,825	66,679
Provision for impairment of receivables	(451)	(256)
	71,374	66,423

Figure 17 Trade Debtors and Receivables FY 2012

That was not the case.

The wholesale investor completely failed to settle the 380ha plot recognised in FY 2010, managing to raise only a nominal amount from its prospectus[13] as evidenced in the next figure.

[12] TFS FY 2012 Annual Report http://www.tfsltd.com.au/files/1014/2727/6489/2012_Annual_Report_Web.pdf
[13] TFS FY 2012 Annual Report http://www.tfsltd.com.au/files/1014/2727/6489/2012_Annual_Report_Web.pdf

NOTE 30: GAIN ON SETTLEMENT OF TRADE DEBTOR

Defaulted debt over 304.07 hectares			
- Land, Kingston Rest Lot 3		4,430	-
- Plantation establishment fee (Excluding GST)		14,695	-
		19,125	-
Fair value of assets taken back			
- Land, Kingston Rest Lot 3	11	4,430	-
- Plantation	12	24,725	-
		29,155	-
Accrued Stamp Duty reversal		284	-
Gain realised on settlement of trade debtor	2	10,314	-

The reclaimed land and trees were accounted for as follows. On 17 March 2012, after receiving notice from the Group a wholesale investor failed to settle in full the purchases of 384.07 hectares of land and plantations located in Kununurra (WA). Under the terms of the agreement the Group reclaimed 304.07 hectares of the underlying land and plantations as part settlement for the transaction. The wholesale investor has the right to settle the remaining 80 hectares and at 30 June 2012 has paid more than 75% of the debt associated with those hectares.

Figure 18 Debt Justification with regard to valuation

Again, TFS shakes off this speed bump under the assumption that the trees are worth more than the outstanding debt. **A default gain of $10M was booked.**

The FY 2013 Key Events

NOTE 31: GAIN ON SETTLEMENT OF TRADE DEBTOR

Defaulted debt over 580 (2012: 304.07) hectares			
- Land, 2013: Nil (2012:Kingston Rest Lot 3)		-	4,430
- Plantation establishment fee (Excluding GST)		34,800	14,695
		34,800	19,125
Fair value of assets taken back			
- Land, 2013: Nil (2012:Kingston Rest Lot 3)	11	-	4,430
- Plantation	12	85,306	24,725
		85,306	29,155
Accrued Stamp Duty reversal		-	284
Gain realised on settlement of trade debtor	2	50,506	10,314

On 30 June 2013, after receiving notice from the Group a wholesale investor owing $34.80m failed to settle in full the purchases of 580 hectares of plantation located in the Burdekin Queensland. Under the terms of the agreement the Group reclaimed all of the 580 hectares of the underlying plantation as full settlement for the transaction. The fair value of trees using the same valuations assumptions as set out in note 12 were calculated to be $85.31m resulting in a gain to the Group of $50.51m before income tax.

Figure 19 Gains on Settlement of Trade Debtor

We present this segment noting that the payment for the 610-then-580ha lot was never received[14]: Note that notice was only received on 30 June 2013. Also, note that the plantations would only just have been established per TFS's planting timeline (i.e. the related plantation is <1year old). Despite this TFS have propose a valuation of over double the establishment fee amount.

[14] TFS FY 2013 Annual Report http://www.tfsltd.com.au/files/1414/2727/6526/TFS_Annual_Report_2013_FINAL_WEB.pdf

TFS displays significant difficulty actually converting wholesale investors' revenues into cash.

The BIG Picture

So how does TFS float its business without investor cash flows? It appears that management leverage high institutional revenue as a platform to obtain access to debt financing[15]:

TFS Corporation Ltd ("TFS") (ASX code – TFC) has priced an offering in the international markets to raise US$150 million from the issuance of 11% Senior Secured Notes due 2018 (the "Notes") and Warrants ("Options") to purchase ordinary shares.

Investors will receive 370 Options for each US$1,000 principal amount of the Notes purchased, resulting in a total of 55.5m Options to be issued. Each Option will be exercisable for one ordinary share at a price per share of A$1.28 (a 40% premium to the 30 trading day volume weighted average price preceding the pricing of the offering), subject to adjustments permitted under the ASX Listing Rules. The Options will expire on 15 July 2018.

At the closing of the offering, 50% of the net proceeds (US$75m) will be deposited into an escrow account that restricts use of the cash in the account ("Restricted Cash"). One-third of the Restricted Cash will become available for use upon TFS receiving shareholder approval for the issue of the Options. The remaining two-thirds of the Restricted Cash will become available once specific sales targets have been met for Beyond Carbon institutional sales.

Figure 20 Figure 26 Extarcts fromTFS Raises US$150 Million in Senior Secured Notes Announcement 17 June 2011

In FY 2012, the funds became available to the business:

NOTE 10: OTHER FINANCIAL ASSETS (NON-CURRENT)

Cash Deposit - First Loss Account	4,430	5,417
Cash Deposit - Bank Guarantee Facility	2,708	700
Cash Deposit - Escrow Accounts (a)	-	44,512
Cash Deposit - MIS Custodian Accounts	4,897	-
	12,035	50,629

(a) At the closing of the offering of the Notes 50% of the net proceeds ("Restricted Cash) were deposited into an escrow account with The Bank of New York Mellon. One-third of the Restricted Cash became available on 1 August 2011 when the shareholders approved the issue of 55.5m warrants in favour of the Notes Issuer. The remaining two-thirds of Restricted Cash became available in June 2012 for use when the Group achieved the revenue target of at least US$100 million from wholesale establishment fees and land sales after 10 June 2011.

Figure 21 FY 2012 Accounts 'Other Financial Assets' 'Cash became available'

TFS would not have been able to meet its US$100M revenue target, save for its policy to allow revenue to be recognised significantly in advance of any future cash payment, which, as discussed, were typically never received.

To summarise, TFS's mark-to-model approach to biological asset valuations and revenue recognition policies allow it to leverage real capital. Accordingly, we believe that the only factor that would prevent this business from being a Ponzi scheme is [whether or not the underlying products are a feasible investment].

[15] TFS Media Announcement – 17 June 2011
http://www.asx.com.au/asxpdf/20110617/pdf/41z89sq1f06gtl.pdf

Who is the German Institutional Bank?

We considered that the German Institutional Bank would have had to market this product to its clients some way or another. A quick google search identified Jäderberg & Cie. (JC) as the "institutional bank", also noted in the Glaucus report.

JC may be German but they certainly did not have the implied capital, institutional investor reach, or any form of verifiable track record prior to marketing the TFS investment in 2010. **JC appears to deal exclusively in TFS investment products.**

The kicker for the German investors is that the investment terms appear to be much safer than those offered to the Australian MIS investors. Here is an extract of the terms presumably (because the plantation locations match) given to the proposed 380ha Beyond Carbon investment[16]:

[16] JC Indian Sandalwood 1 GmbH & Co. KG – Executive Summary of Investment (2011) from http://web.archive.org/web/20111216014153/http://www.jaederberg.de/tl_files/Jaederberg/Downloads/executive_summary_jc_indian_sandalwood_1_en.pdf

Facts & Figures

Investment object	Participation in *JC Indian Sandalwood 1 GmbH & Co. KG* via a trustee, *ProConsus Treuhand GmbH*. The KG is the only limited partner of *JC Indian Sandalwood 1 LLP*, who is the only owner of plantations and trees.
Asset	Indian Sandalwood plantations in Western Australia
Location of the plantations	Kingston Rest and Ord River Irrigation Area in Kimberley Region, Western Australia
Minimum investment amount per investor	AUD 300,000 (which approx. corresponds to the amount of EUR 220,000).
Maximum investment amount	AUD 50,000,000
Initial fee	6.5 % of the total contributions
Ongoing fee	0.8 % p. a. of the total contributions
Performance fee	10.0 % to the initial limited partner of all payouts to the investors made in excess of 110.00 % of the total equity of the KG 25.0 % to the asset manager of all payouts to the investors made in excess of 1,000.00 % of the total equity of the LLP
Tax	Australia: 30 % income tax Germany: income from the plantations is tax free according to the DTA, however, subject to progression
Estimated fund payouts in the business years (after tax)*	2013/14 27,0 % 2014/15 24,5 % 2015/16 23,0 % 2016/17 23,0 % 2017/18 23,0 % 2018/19 23,0 % 2019/20 6.5 % 2025/26 604 % **Total: 754 %**
Investment close date	31th December 2011
Early bird bonus	6 % p. a. interest on the investors paid in amount until the investment close date

Figure 22 Page 8 - JC Indian Sandalwood 1 GmbH & Co. KG A Private Placement in Indian Sandalwood in Western Australia

This further extract confirms **cash** distributions to investors from as early as 2013, where the investment close date is 31 Dec 2011[17]:

Early payouts & attractive return

- Vertical integration along the entire value chain significantly enhances the investor return
- Distribution to the investor planned to start already in 2013/2014
- Full pay back of investor equity expected in 2017/2018
- Total fund payouts amount to 754 %

Figure 23 Page 7 JC Indian Sandalwood 1 GmbH & Co. KG A Private Placement in Indian Sandalwood in Western Australia

And confirmation of the ~380ha plot size[18]:

Limited by size & Availability

- Access to the land for new plantations (373,9 ha) described in the PPM is exclusively possible via Jäderberg & Cie.

Figure 24 Page 8 JC Indian Sandalwood 1 GmbH & Co. KG A Private Placement in Indian Sandalwood in Western Australia

More recent full prospectuses (we were unable to source a full 2011 prospectus) show the option for the investors **or the issuer (specifically defined as JC) to withdraw from the investment for a predetermined amount as early as year 2[19]:**

How could JC possibly afford to pay dividends to investors when all of their assets are **literally planted in the ground for 15 years?**

Impact of early termination (prognosis)

After a (statutory) minimum term of 2 years, both the investor and the issuer have the option to terminate the equity loan prematurely. The total forecasted cash flows in case of early termination of the participation loan are presented below (in% of the participating loan).

Gesamtmittelrückfluss im Falle einer vorzeitigen Kündigung (PROGNOSE)											
Kündigung nach Jahren	2	3	4	5	6	7	8	9	10	11	12
Kündigung durch den Anleger	110%	115%	120%	129%	139%	149%	159%	173%	187%	201%	227%
Kündigung durch die Emittentin	120%	130%	140%	150%	161%	172%	183%	194%	205%	216%	227%

Figure 25 C Indian Sandalwood 5 (The yield for the investor - click here for more info)

JC appears to have negotiated an off-record put option with TFS.

How could auditors have signed off fictitious sales such as revenues from the German Institutional Bank?

Why is the German Institutional Bank given more favourable terms than other investors? Or do all institutional investors receive off-record put options?

Are bondholders aware that TFS released bond capital from escrow on the back of bogus sales?

[17] JC Indian Sandalwood 1 GmbH & Co. KG – Executive Summary of Investment (2011) (See Exhibits)
[18] JC Indian Sandalwood 1 GmbH & Co. KG – Executive Summary of Investment (2011) (See Exhibits)
[19] http://www.jaederberg.de/jc-indian-sandalwood-5.html

6. The Market

"Yesterday upon the stair, I met a man who wasn't there, he wasn't there again today…"

English WWII proverb

The individual MIS annual reports[20] has been useful in determining *how* TFS price its biological assets. Currently, the price is derived from the estimated oil content of each tree and the sales price. However, the price used to audit the accounts is US$2,800 per kilogram of oil, not the often quoted US$4,500 per kilo Indian auction value in TFS's presentations.

The US$2,800 figure used now appears to be derived from a price obtained from the Public Ledger, an agri-intelligence broker[21]:

> Due to the low quantities of auctioned heartwood, the valuation of the plantation for the current year has been derived by obtaining the current Indian sandalwood oil price as obtained from the "Public Ledger" publication and applying that price to expected oil yields within the plantation trees to arrive at an approximate for the relevant value of the sandalwood logs. The equivalent Australian dollar Public Ledger price for Indian sandalwood oil as at 30 June 2014 was A$2,653 per kg (2013: A$2,735).

The key takeaways from this piece of information is that it is *inherently* difficult to find market information on Sandalwood because it is a niche industry with ***low quantities auctioned***.

Global Oversupply

Note that it has been extremely difficult finding a *reliable* source of empirical data on the global sandalwood market as it is very hard to source a truly independent source. This section aims to challenge market projections and generalizations made by the industry as a whole.

In their FY 2016 earnings presentation, TFS announced that they had engaged a "top tier global management consulting firm" to provide an updated market study. The key emphasis by management was on the explosive demand projections, per the graphs on the following page[22]. In Quintis' response to the Glaucus report, this top tier consulting firm was said to have been McKinsey & Co.

Make note that the data presented in Figure 26 **Graph 1 (Next Page)** is only the total legal market condition, versus the total (including illegal) market on Figure 37 Graph 2 (Next Page).

[20] http://www.tfsltd.com.au/plantation-investors/retail/project-accounts/
[21] http://www.tfsltd.com.au/~tfsltdcom/files/6314/2853/8061/TFS2007_Financial_Report_300614_Web.pdf (pg. 3)
[22] TFC FY 2016 earnings presentation (pgs. 30-31)

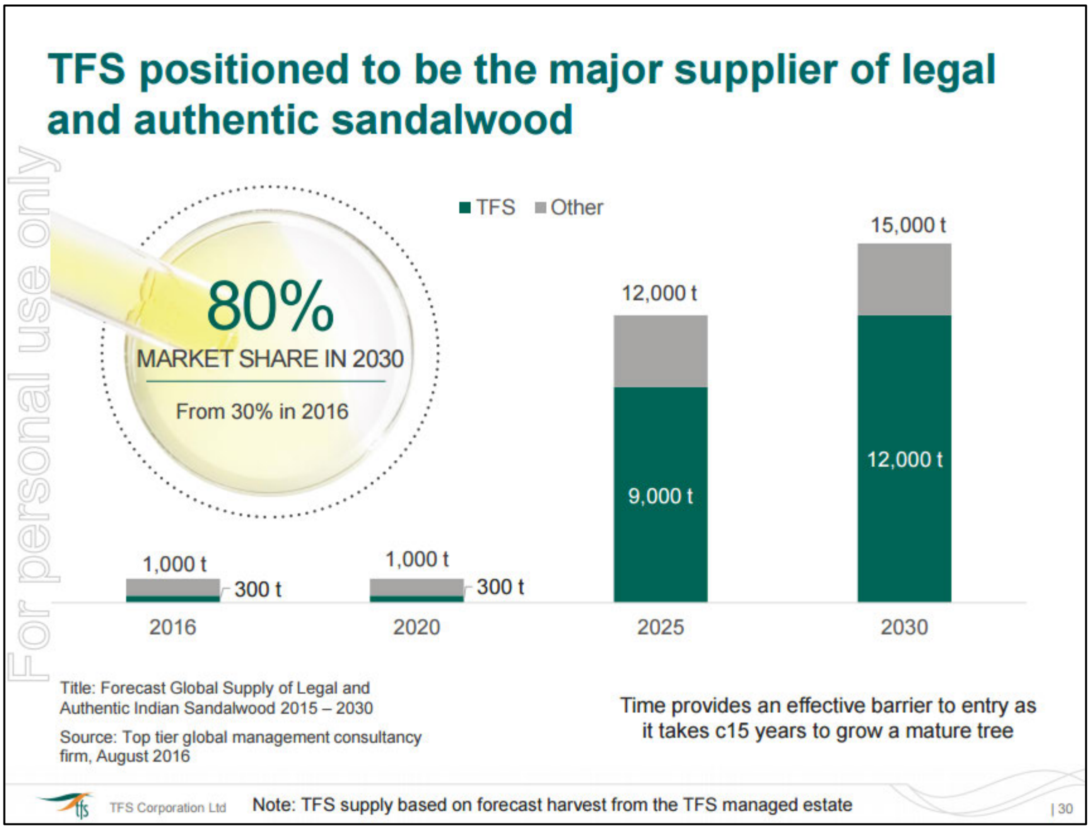


Figure 26 Graph 1

Graph 1 Page 31

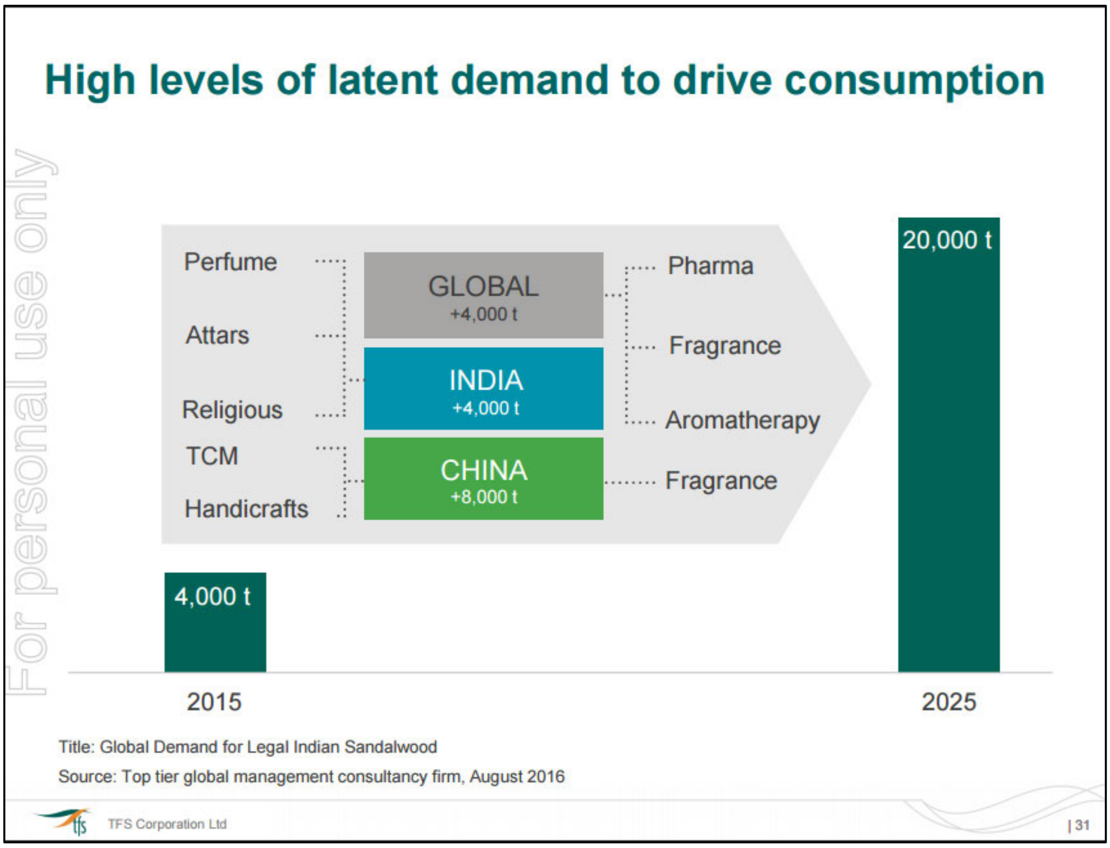


Figure 27 Graph 2

Firstly; we challenge the implied opinion that the illegal sandalwood market will grow concurrently (albeit, at a smaller pace) than the exploding legal market. There is no logic behind this projection. A comparable case study would be the impact of drug legalization on cartel activity within the USA, where, obviously, illegal activity dropped after an increase in legally available sources[23].

Secondly; we challenge the opinion that the global market for sandalwood products will increase 5x from 2020 to 2025. What is the basis behind this assumption? The listed possible-use items in Figure 27 Graph 2 (Perfume, Attars, Handicrafts etc.) have been practiced for centuries. Why will demand increase? It certainly is not organic growth.

Lastly; we challenge TFS's often quoted sandalwood oil wholesale price of $4,500/kg. Note the trends presented in the graph below,.

Again, we ask readers to evaluate this data with a grain of salt as the parties involved are in the sandalwood business (i.e. another presenter in this conference is TFS consultant, Mr Padmanabha).

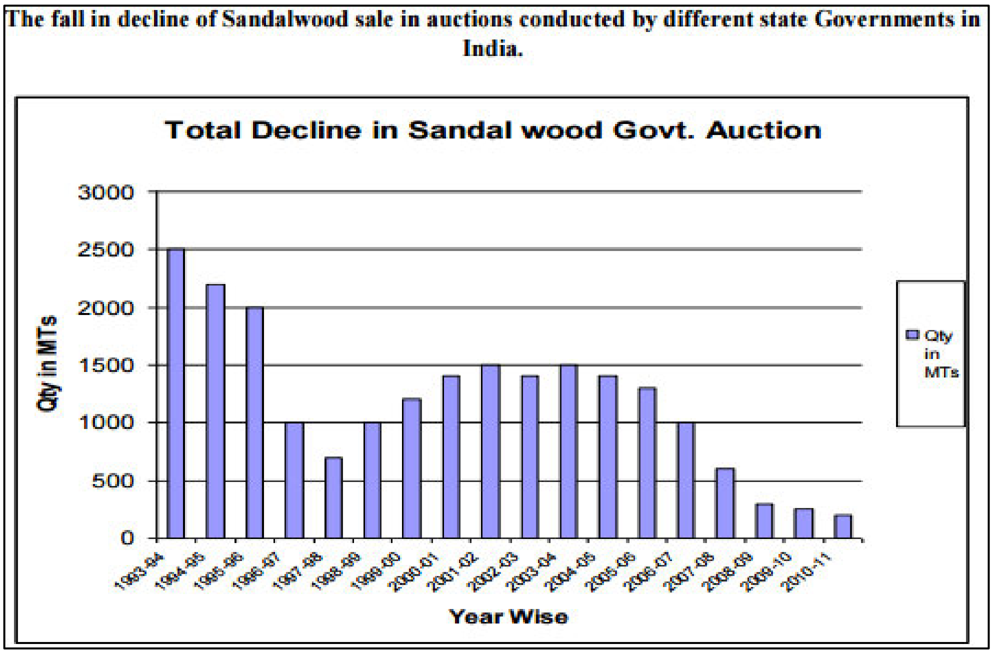


Figure 28 Graph 3 Proceedings of the Art and Joy of Wood conference, 19-22 October 2011, Bangalore

[23] https://www.washingtonpost.com/news/wonk/wp/2016/03/03/legal-marijuana-is-finally-doing-what-the-drug-war-couldnt/

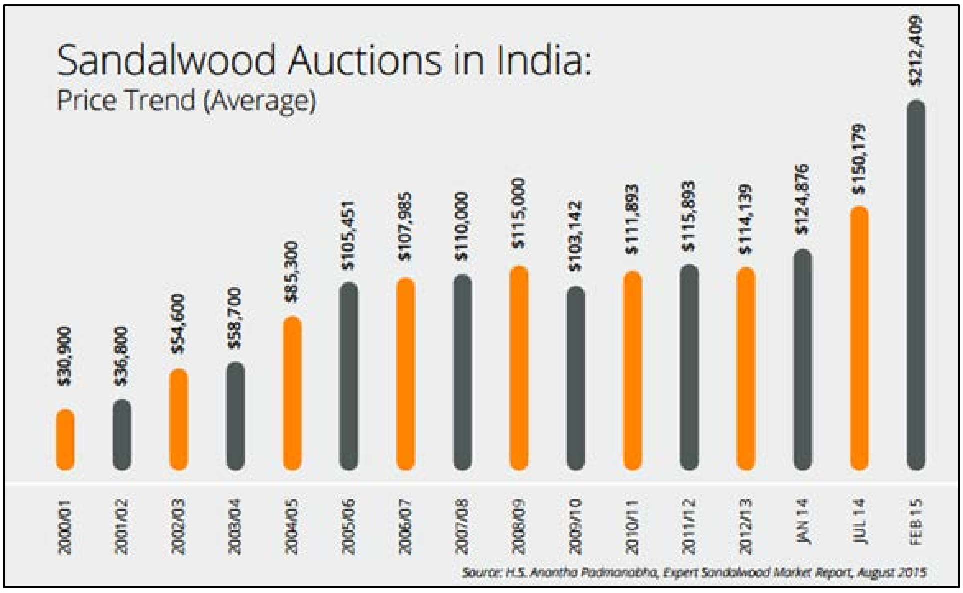


Figure 29 Graph 4 TFS PDS

Generally speaking, Figures 34 & 35 Graphs show the trends are economically logical: the price of sandalwood has increased to adjust for the decreasing supply. However on all of its marketing material, PDS and on its investment calculator provided to institutional investors, TFS assumes sales based on *current* prices.

We believe it is illogical to assume consumers will continue to pay the same inflated price for a product if supply increases 5x, with no obvious demand growth segments (as discussed earlier).

This fixed price assumption and total neglect of the possibility of oversupply violates *basic* economic principles of supply & demand. This assumption significantly depletes TFS's NPV/IRR estimates, as per screengrab of financial calculator below in which the sandalwood oil price assumptions are key to the calculation of returns:

Investment Size	$	2,000,000
Tax Rate		0.00%
Establishment fee (Excl GST) per Ha	$	80,000
Total investment ($)	$	2,000,000
Total investment size (Ha)		25.00
Investment period (years)		16
IRR - No deferral (Pay all fees)		**19.5%**
IRR - Defer all fees		**19.8%**
NPAT at harvest (Pay all fees)		**41,652,505**
NPAT at harvest (Defer all fees)		**34,239,312**
Financial Asssumptions		
Sandalwood Price Escalation (% pa)		**2.0%**
Cost Inflation (% pa)		**2.0%**
Oil Price USD		**$4,500**
Exchange Rate (AUD/USD)		**$0.76**
Oil price AUD		**$5,921**
Marketing Fee		**5%**
Yield Assumptions		
Hectares Purchased		**25.0**
Trees per Hectare (83% Survival)		**420**
Heartwood/tree (kg)		**20**
Oil content		**3.70%**
Oil per Hectare (kg/Ha)		**311**

Figure 30 Financial Calculation Assumptions

The Indian Market

Indian export/import data is easily available on [Zauba](https://www.zauba.com/) which show import/export prices are significantly below TFS expectations.[24]

Import data shows that approximately 50 tonnes of sandalwood oil (all types) has been brought into the country over the last two years (Aug 2014 – Sep 2016[25]) at an average price of US$505/kg. If we restrict data to commercial quantity imports (>50kg shipments), the average price rises slightly to US$507/kg. This is significantly below TFS's price assumptions of US$4,500/kg.

Note that the total amount of *Indian Sandalwood* Oil imported during this period is <1kg, with an average price of US$200-$250/kg, and was purchased from Indonesia. The remaining imports were typically Ugandan or Australian Sandalwood[26]:

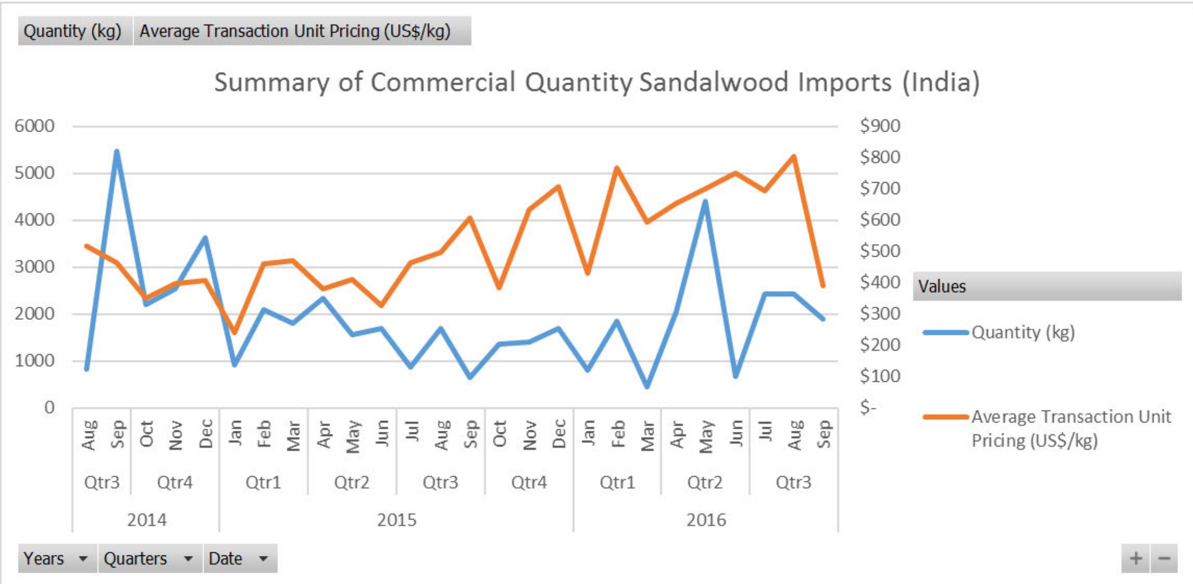


Figure 31 Commercial Quantity Sandalwood Imports (Summary to 2016)

Export data shows only 608kg of Sandalwood exports at an average price of US$786/kg[27]:

Date	Destination	Unit	Quantity	Value (INR)	Per Unit (INR)	Per unit (US$)
14-Jul-16	Singapore	KGS	2	219,615	109,808	1,647
20-Jan-15	United Arab Emirates	KGS	250	12,990,567	51,962	779
20-Jan-15	United Arab Emirates	KGS	250	12,992,425	51,970	780
14-Oct-14	United Arab Emirates	KGS	100	5,077,800	50,778	762
12-Sep-14	Thailand	KGS	3	292,500	97,500	1,463
9-Jan-14	Thailand	KGS	3	299,081	99,694	1,495
Total			**608**	**31,871,988**		
			USD	478,080		
			USD/kg	786		

Figure 32 Export Data

[24] Assumptions: INR 1 = US$ 0.015
[25] Roughly the date in which this report was compiled
[26] https://www.zauba.com/
[27] https://www.zauba.com/

Sandalwood chips and dust *import* data showed similarly disappointing results, however we were surprised to find that chip exports averaged a similar yield to TFS's claims, averaging US$153,000/tonne . However, export quantities appear to be to a single Hong Kong buyer and to the equivalent of 1ha of TFS plantations over more than 2 years, making them entirely uncommercial[28]:

Date	Destination	Port of Loading	Unit	Quantity	Value (INR)	Per Unit (INR)	Per Unit (USD)
15-Sep-15	Hong Kong	Banglore Air Cargo	KGS	200	3,366,197	16,831	252
2-Apr-15	Hong Kong	Banglore Air Cargo	KGS	909	12,116,970	13,330	200
19-Feb-15	Hong Kong	Banglore Air Cargo	KGS	630	7,742,700	12,290	184
19-Feb-15	Hong Kong	Banglore Air Cargo	KGS	360	3,097,080	8,603	129
1-Jan-15	Hong Kong	Banglore Air Cargo	KGS	1,100	13,816,000	12,560	188
29-Nov-14	Hong Kong	Banglore Air Cargo	KGS	500	6,160,000	12,320	185
29-Nov-14	Hong Kong	Banglore Air Cargo	KGS	1,000	8,249,472	8,249	124
29-Nov-14	Hong Kong	Banglore Air Cargo	KGS	1,000	12,320,000	12,320	185
26-Aug-14	Hong Kong	Banglore Air Cargo	KGS	660	5,765,925	8,736	131
17-Jul-14	Hong Kong	Banglore Air Cargo	KGS	400	3,782,400	9,456	142
17-Jul-14	Hong Kong	Banglore Air Cargo	KGS	560	4,302,480	7,683	115
17-Jul-14	Hong Kong	Banglore Air Cargo	KGS	220	2,080,320	9,456	142
3-Jul-14	Hong Kong	Banglore Air Cargo	KGS	1,200	9,271,644	7,726	116
3-Jul-14	Hong Kong	Banglore Air Cargo	KGS	1,000	8,117,006	8,117	122
6-Jun-14	Hong Kong	Banglore Air Cargo	KGS	450	4,255,200	9,456	142
6-Jun-14	Hong Kong	Banglore Air Cargo	KGS	400	3,782,400	9,456	142
Total				**10,589**	**108,225,794**		
				USD	1,623,387		
				USD/kg	153		

Figure 33 Sandalwood Chips & Dust Import Data

The Perfumers

Sandalwood

- Indian Sandalwood is nearing extinction in the wild.
- It is an oil bearing tree with fragrant and medicinal properties. Around the world it is used in a variety of markets and has strong global demand but falling supplies.
- The Chinese carving industry will pay more than **US$500,000 per tonne of Indian sandalwood** heartwood.
- **47% of all perfumes** created since 1790 contain sandalwood notes.
- TFS Indian sandalwood oil is the subject of clinical trials to develop a prescription drug to treat the skin.
- Over **three tonnes of sandalwood** was burned on Gandhi's funeral pyre.
- In India more than **500 million sandalwood incense sticks** are burned during worship each day.

Figure 34 FACTS & FIGURES from TFS Website[29]

- We are unable to confirm or deny that the Chinese carving industry would pay US$1.5m for Gandhi's funeral pyre.
- We are unable to find a reliable figure on the sandalwood content of 500 million incense sticks.
- We are unable to confirm or deny that 47% of perfumes contain sandalwood notes. Actually, we have no idea what quantifies a sandalwood "note".

[28] https://www.zauba.com/
[29] http://tfsltd.com.au/about/facts/

We believe that in reality, perfumers rarely use natural sandalwood oil in fragrances due to unsustainable (and illegal) methods used to harvest as well its high price. Several high-end perfume houses still use the oil, however we believe these entities are unlikely to change supplier considering:

- They already have a supplier who can provide enough oil to cover demand.
- Their products are characterised by uniqueness and consistency.
- Their products are highly sensitive to the nature of the ingredients.

In case our analysis isn't convincing enough: TFS shot themselves in the foot when they hosted a competition with the American Perfumers Society and marketed this well-worded but completely contradictory statement[30]:

> Perfumers, it's time to be reacquainted with Indian Sandalwood (Santalum album). One of the oldest perfumery materials in the world, this precious ingredient has had a tumultuous history, plagued by illegal poaching and adulteration. Little wonder it all but vanished from the perfumer's palette.

Figure 35 Indian Sandalwood Competition American Society of Perfurmers

Why does TFS use two different sandalwood oil prices for marketing and audit?

What is the basis for the presumed 5x increase in sandalwood demand?

Does TFS have any legally binding contracts with perfumers?

[30] http://www.indian-sandalwood-perfume.com/competition

7. The Agreements

‘We shook hands on a pact. Did you not shake my hand on it?’

‘You stuck your hand out, so I shook it. I don't know about a pact.’

-Seinfeld, “The Engagement”

We are highly sceptical of the legitimacy of TFS’s sales channels.

The Chinese Buyer

We believe Glaucus covered this quite well. Please refer to their report for in-depth details.

In short, days after the Glaucus report was published, reports surfaced of Chinese customs seizing millions of dollars of sandalwood from a tax-evading, smuggling syndicate:

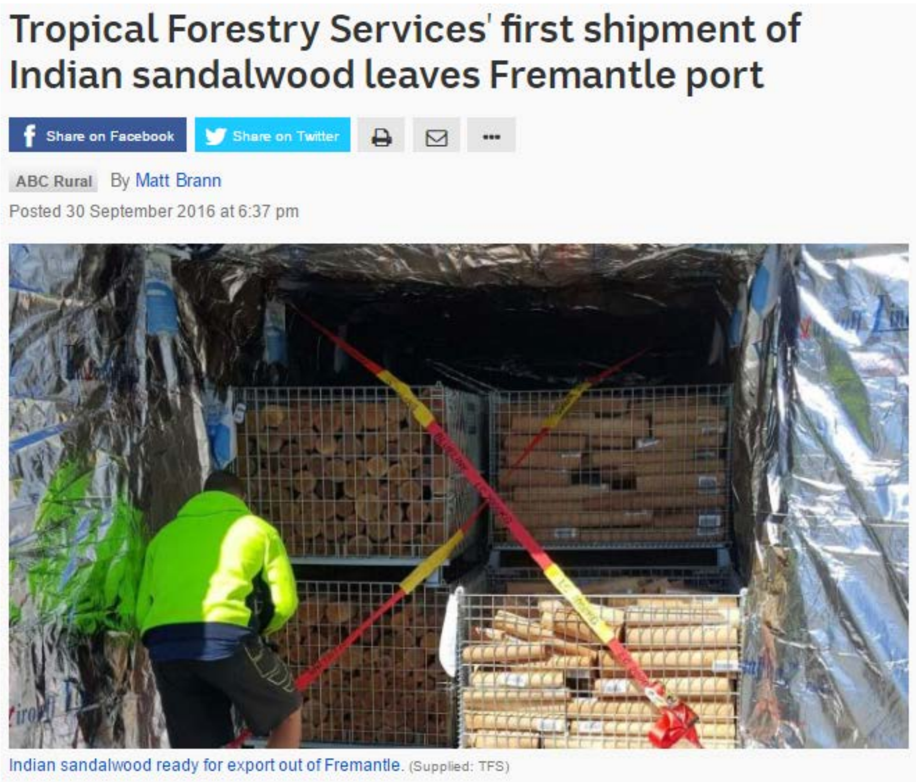
http://newscontent.cctv.com/NewJsp/news.jsp?fileId=401695

The TFS logo is clearly visible on the door of the office at 1:55 along with the name of a Richer Link director’s firm, Yitan Xiamen Spices.

There is further news coverage which shows that this syndicate has smuggled over $26m (currency not specified) of sandalwood into China:

https://www.youtube.com/watch?v=BYXT2aYx-FY&spfreload=10

The container at 0:36 matches pictures posted by the ABC in September of TFS’s the first shipment:


Tropical Forestry Services' first shipment of Indian sandalwood leaves Fremantle port

Share on Facebook | Share on Twitter

ABC Rural By Matt Brann

Posted 30 September 2016 at 6:37 pm

Indian sandalwood ready for export out of Fremantle. (Supplied: TFS)

Figure 36 ABC report – 30 Sep 2016[31]

[31] http://www.abc.net.au/news/rural/2016-09-30/first-shipment-of-tfs-indian-sandalwood-leaves-fremantle-port/7892254

It was later disclosed by TFS management that their largest customer had only purchased two shipments of sandalwood.

Glaucus noted that upon calling the Richer Link office, they were informed that they no longer do business with TFS by a clerk.

On top of Glaucus' research, we note that, per the company's website, the Chinese agency is the **exclusive** reseller of products in the Asia region:

https://web.archive.org/web/20161003134457/http://www.tfsltd.com.cn/contact-us/

There appears to be a lack of due diligence conducted by management, as this agreement would have eliminated TFS's own ability to sell to China. Why have they been in commercial discussions with other buyers since 2016? We believe this would have fallen within their continuous disclosure responsibilities.

Galderma

On 10 May 2017, The Australian Financial Review released an extraordinary piece of investigative journalism which highlighted that Quintis' Nestle contract had been cancelled.

We note from the following extract of the AFR article[32]:

> "**Quintis has not amended its profit guidance for 2016-17 because it had not factored any Galderma sales into its expectations**, and its contract with the Swiss group did not specify any fixed volume. The company is predicting 2016-17 sandalwood product sales in the range of $45 million to $55 million for the full financial year, up from $29.9 million, it said at its half-year results in February and reiterated in March. Also, "cash EBITDA" will increase by at least 25 per cent on 2015-16, it has stated."

We believe the company has not made any sales to Galderma for over a year as the Benzac sandalwood product was discontinued upon Nestle's JV agreement with "Proactiv"; touted to be a better product. This happened in MARCH of 2016[33].

> Management of the resource is the key and should be privatised and the farmers/harvesters allowed to sell to whom they like and DEC becomes the auditor – this would at least give local companies a chance to buy wood from numerous rather than one source giving more local, grass root working people much needed income. Whilst there e Private harvester licenses the volume of wood is not significant and as Mt Romance get a subsidised price for 550 tonnes per annum from FPC they have the capacity to outbid any other oil producers because they can amortise the premium price paid for wood over a vastly subsidised resource and still have cheaper oil than any other producer. It is really a negative outcome for the WA Sandalwood industry. Somehow the farmers who's land the wood comes from should be getting the benefit of that asset and not an inefficient Government department that is clearly not supporting the construction of a sustainable WA Sandalwood Industry.

Figure 37 Western Australia Parliament Submission

Management noted on its market announcement post the AFR article that it was unaware that one if its major clients had cancelled their contract, as staff from their subsidiary did not alert the board!

[32] http://www.afr.com/business/agriculture/crops/quintis-board-says-it-was-unaware-of-galderma-exiting-supply-deal-20170509-gw15kk#ixzz4genOaW8E

[33] https://www.bloomberg.com/news/articles/2016-03-24/nestle-forms-acne-joint-venture-with-maker-of-proactiv-brand

Quintis has supplied over 1,200 kg of EISO to Galderma under the supply contract, with all supplies occurring in the 2014 and 2015 calendar years. In March 2016 Nestlé entered into an agreement to acquire a majority stake in Proactiv, the world's leading non-prescription anti-acne brand. Quintis has not supplied any EISO to Galderma in FY2017 and EISO sales to Galderma have not been factored into the Company's sales forecasts for FY2017.

The Board of Quintis was advised late yesterday that on 16 December 2016, Santalis and Galderma entered into an agreement that terminated Galderma's licensing and supply arrangements with Santalis with the termination to take effect from 1 January 2017. Under the termination agreement, Galderma retained an option to reinstate the license and supply arrangements on or prior to 1 July 2017.

Prior to yesterday's advice, the fact and details of the contract termination had not been provided to current members of both the Board of Quintis and its senior management (outside of Santalis).

Quintis Chairman, Dalton Gooding, said: "It is unacceptable that the current Board was not made aware of the contract termination when it took place. We are taking immediate and appropriate measures to ensure that this type of communication breakdown is not repeated."

Figure 38 Galderma Contract announcement[34]

We are suspicious of management's wording in the above extract, where Dalton Gooding alludes that the *current* board were not made aware of the Galderma contract termination. Are investors, the market and financial regulators to interpret that former board members - including Frank Wilson - knew of the termination of this contract?

Medinext

Medinext was highlighted as the second largest buyer of Indian Sandalwood after Shanghai Richer Link in management's address of the initial Glaucus report[35]:

The following table lists customers Quintis has supplied wood or oil to under multi-year contracts:

Name	Jurisdiction	Product	Annual Volume	Price	Date Signed	Term
Galderma	USA	Oil	No fixed volume	US$4,500 per kg plus annual CPI (capped at 3%)	2014	20 years
Lush Cosmetics	UK	Oil	Minimum of 1,000 kg	US$2,000 per kg plus annual CPI (capped at 3%)	2008, effective from 2015	5 years
Medinext General Trading (1)	India, North Africa and Middle East	Wood	30t	US$155,000 per tonne plus 3% annual increase	2016	2 years + option to extend by 3 years
Shanghai Richer Link	China	Wood	150t	Pricing dependent on grade of wood; average of US$150,000 per tonne plus 3% annual increase	2016	5 years
Young Living	US	Oil	1,200kg	US$4,500 per kg plus 2.5% annual increase	2016	5 years
Note 1: Medinext General Trading is an associate of a customer who has been supplied and paid for AU$27.5m of spicatum oil since 2010						

Figure 39 Quintis Indian Sandalwood Customer List

34 http://www.asx.com.au/asxpdf/20170510/pdf/43j4xs4gfljh4p.pdf
35 http://www.asx.com.au/asxpdf/20170327/pdf/43h2grd1gyxnjl.pdf

We looked into shipment records and found a record showing Medinext General Trading shipping 25 tons of *Western Australian Sandalwood* (not Indian Sandalwood) from Australia to India:[36]

Sample shipment record for Ms. Medinext General Trading L.l.c

Ms Medinext General Trading Llc is an overseas supplier in **Australia** that exports products to **Aditi International**.

BILL OF LADING			
Manufacturer / Shipper	**Consignee**	ARRIVAL DATE	2015-01-10
MS MEDINEXT GENERAL TRADING LLC	ADITI INTERNATIONAL	HS CODE	12119050
Origin	**Destination**	QUANTITY / UNIT	25.00 / MTS
AUSTRALIA	INDIA		
Product Description			
WESTERN AUSTRALIAN SANDALWOOD POWDER (PRE GRIND)			

Figure 40 Shipment record – Medinext General Trading

We matched HS code and quantity to recurring import data listed on Zauba[37]:

Date	HS Code	Description	Origin Country	Port of Discharge	Unit	Quantity	Value (INR)	Per Unit (INR)
Jan **19** 2015	12119050	WESTERN AUSTRALIAN SANDALWOOD POWDER (PRE GRIND)	Australia	Nhava Sheva Sea	KGS	25,002	15,788,573	631

Figure 41 Zauba extract – 19 Jan 2015

Note that 25 tonnes has been shipped with value of around US$10/kg, or $10,000/tonne, less than 10% of TFS's sale price claim of $155,000/tonne. In fact, no sandalwood is currently being shipped with value over US$15/kg.

We believe that **either Quintis is misquoting its sales price, or Medinext is evading import duties in similar fashion to Shanghai Richer Link.** This is made more believable in noting that the goods are recorded on the import slip as the lower value Western Australian Sandalwood.

[36] https://www.importgenius.com/india/suppliers/m-s-medinext-general-trading-l-l-c
[37] https://www.zauba.com/import-12119050-hs-code.html

Givaudan

Management's rebuttal to the Glaucus report also highlights Givaudan as a major customer:

The following table lists customers Quintis has supplied wood or oil to under multi-year contracts:

Name	Jurisdiction	Product	Average Volume (1)
Givaudan	Switzerland/USA	Oil	2,040 kg pa
Berje Inc	USA	Oil	650 kg pa
Aveda Corporation	USA	Oil	600 kg pa
Oneworld Corporation/Aditi	India	Oil	830 kg pa
Swiss Arabian	UAE	Oil	530 kg pa
Robertet	France	Oil	460 kg pa
Fushankodo Co Ltd	Taiwan	Wood product	530 t pa
IFF	Europe and other	Oil	250 kg pa
Firmenich	Switzerland and USA	Oil	200 kg pa
Lush Cosmetics	UK	Oil	380 kg pa
Aroma Trading Ltd	UK	Oil	130 kg pa
Australian Botanical Products	Australia	Oil	80 kg pa
Note 1: Average volume per annum based on supplies from July 2015 to December 2016			

Figure 42 Western Australian Sandalwood customer list

This is very curious, because prior to this announcement even being released, we had already dismissed Givaudan as an ongoing customer. We understand that Mt Romance previously held a supply agreement with Givaudan, the largest flavour and fragrance house in the world, which was cancelled sometime prior to 2012. This was **disclosed by the former Mt Romance CEO David Brocklehurst** (who now works at a wholesaler which competes with TFS) in the last page of this WA Parliament submission as a request to break up the Mt Romance monopoly for exclusive government sandalwood processing contracts[38]:

> Management of the resource is the key and should be privatised and the farmers/harvesters allowed to sell to whom they like and DEC becomes the auditor – this would at least give local companies a chance to buy wood from numerous rather than one source giving more local, grass root working people much needed income. Whilst there e Private harvester licenses the volume of wood is not significant and as Mt Romance get a subsidised price for 350 tonnes per annum from FPC they have the capacity to outbid any other oil producers because they can amortise the premium price paid for wood over a vastly subsidised resource and still have cheaper oil than any other producer. It is really a negative outcome for the WA Sandalwood industry. Somehow the farmers who's land the wood comes from should be getting the benefit of that asset and not an inefficient Government department that is clearly not supporting the construction of a sustainable WA Sandalwood Industry.

We believe further disclosure from management is required to address this issue in order to avoid a Galderma-like situation.

[38]http://www.parliament.wa.gov.au/parliament/commit.nsf/(Evidence+Lookup+by+Com+ID)/CEB91421B46B4D0D48257AAD001DC0E6/$file/ev.san.Submission3.austoils+pty+ltd.pdf

The Young Living Agreement

TFS recently announced an agreement with Young Living to supply Indian Sandalwood oil at a price of US$4,500/kg with fixed annual increases of 2.5%[39]. Young Living is a multi-level-marketing scheme[40] offering essential oils and facilitating blatant lies as evidenced by the **FDA**'s scathing letter warning[41]:

> *"Your consultants promote many of your Young Living Essential Oil Products for conditions such as, but not limited to, viral infections (including Ebola), Parkinson's disease, autism, diabetes, hypertension, cancer, insomnia, heart disease, post-traumatic stress disorder (PTSD), dementia, and multiple sclerosis, that are not amenable to self-diagnosis and treatment by individuals who are not medical practitioners."*

These "consultants" are ostensibly Young Living salespeople attempting to drum up business.

This FDA warning was in response to several articles claiming that **ingesting** essential oils would either heal or lessen the effect of serious medical conditions, most notably Ebola. Not only misleading, but dangerous given the track record of other ingested essential oils in the past[42]. **This stern reprimand causes us to question whether Young Living's existence as an alleged supply avenue is appropriate given TFS's planned involvement in pharmaceuticals.**

TFS's subsidiary Santalis Pharmaceuticals Inc. is reportedly in the process of obtaining FDA approval for pharmaceutical grade sandalwood oil. We cannot imagine the FDA being content with TFS's involvement with Young Living, a company tarnishing the reputation of legitimate pharmaceutical companies.

TFS has made no comments regarding Young Living's interactions with the FDA, whether their products are safe for ingestion or if they possess any medicinal or magical capability.

We would advise our readers to look over the FDA warning in full, especially the section titled "Young Living Versus Ebola Virus" to fully understand the claims regularly made by Young Living "consultants" and for a laugh (the FDA has a sense of humor!).

Fun fact: the term 'Essential' when conjoined with 'Oil', is derived from the word 'Essence'. Therefore, it might smell nice, but you don't need it.

Why is TFS associating with a company which facilitated fraudulent and potentially dangerous advertising statements?

Does new management have any transparency in the company's sales channels?

[39] http://www.tfsltd.com.au/files/5014/7277/8698/Supply_Agreement_With_Worlds_Leading_Essential_Oil_Company.pdf

[40] http://youngliving.cdn.cymbeo.com/f/69rwmp3g/126c69rvgm8k/Compensation-Plan-Highlights_1.pdf

[41] http://www.fda.gov/ICECI/EnforcementActions/WarningLetters/2014/ucm416023.htm

[42] http://www.ncbi.nlm.nih.gov/pmc/articles/PMC3546250/

8. The Plantations

"Money trees is the perfect place for shade"

Kendrick Lamar, "Money Trees"

Indian Sandalwood (Santalum Album) is a member of the demi parasitic, long lived sandalwood family. It is harvested for its wood which is used for carvings, furniture, religious and cultural uses in Asia and the subcontinent and for its oil which can be used in fragrances and has some dermatological properties. The oil is extracted from the heartwood of the tree which grows as the trees mature. Generally speaking, the earliest harvest date for a tree is 15 years after planting. The heartwood is extracted and, depending on use, either processed as lumber or crushed into a mush through which steam is pushed to extract sandalwood oil.

The heartwood estimate

The measure of the worth of sandalwood trees relies on three factors; the heartwood content of the tree by weight, the oil content of that sandalwood by percentage and the santanol content of that oil by percentage. Below are the aggregated results of independent studies into sandalwood heartwood content and oil yield, which were also released in the Glaucus report.

	Publication Year	Tree Age (years)	Heartwood Yield (kg/tree)	Oil Yield (%)
Rai[43]	1990	20	4.0	3.8
Clarke[44]	2006	15	20.0	4.1
Brand et al[45]	2012	16	6.8	2-6
Rural Industries[46]	2012	15	6.3	3.8
Elders [47]	2013	15	6.7	4.1
Average			**8.76**	**4.06**

Figure 43 Aggregate Results for Sandalwood Yields

TFS projects their heartwood yield in kg/tree in their annual asset management reports and each year's respective PDS.

Plantation	Current Yield Estimate (kg/tree)	Initial Yield Estimate (kg/tree)
EKS	(actual) 3.1	N/A
TFS2	(actual) 4.9	N/A
2000	(actual) 9.7	N/A
2002	10.5	30
2003	10.9	30

[43] Status and cultivation of sandalwood in India (Rai), page 70
http://www.fs.fed.us/psw/publications/documents/psw_gtr122/psw_gtr122_rai.pdf
[44] Australian Government - Rural Industries Research & Development Corporation Australia's Sandalwood industry (Clarke), page 9
https://rirdc.infoservices.com.au/downloads/06-131.pdf
[45] Elders independent expert report (page 31)
http://www.tandfonline.com/doi/abs/10.1080/00049158.2012.10676406#.VZnjqfmqpBc ,
[46] Flood-irrigated tropical timber trials in the North of Western Australia (Rural Industries), page xii
https://rirdc.infoservices.com.au/downloads/12-044
[47] Elders independent expert report (page 30)
http://www.tandfonline.com/doi/abs/10.1080/00049158.2012.10676406#.VZnjqfmqpBc

Plantation	Current Yield Estimate (kg/tree)	Initial Yield Estimate (kg/tree)
TFS Gold	10.6	30
2004	7.6	30
TFS Premium	8.4	30
2005	8.5	30
2006	8.7	27.5
2007	10.5	27.5
2008	12.1	27.5
2009	15.7	27.5
2010	15.7	27.5
2011	15.7	27.5
2012	15.7	22.5

Figure 44 TFS heartwood yield in kg/tree as per annual their annual asset management reports and each year's respective PDS.

Aggressive Mark-to-Model Practices

We question how TFS can continually and substantially revise its biological assets upwards, considering actual harvest results have missed their initial MIS prospectus results by such a spectacular amount. **In FY 2013 there were large write-offs** to each of the MIS accounts to the net sum of almost \$100m, as the date of the first harvest approached[48].

Biological Assets Under Management					
Plantation		2013 Gain/Loss on Biological Assets	2012 Bio Assets	2013 Bio Assets	YOY Change
EKS	-	14,367,862	21,518,988	7,151,126	-67%
TFS2	-	5,814,719	7,292,685	1,477,966	-80%
2000	-	9,303,447	20,127,549	10,824,102	-46%
2002	-	3,394,839	12,149,959	8,755,120	-28%
2003	-	3,498,388	12,072,051	8,573,663	-29%
TFS Gold	-	1,438,291	4,599,710	3,161,419	-31%
2004	-	3,520,003	6,649,670	3,129,667	-53%
TFS Premium	-	8,313,957	19,400,422	11,086,465	-43%
2005	-	15,583,198	30,283,583	14,700,385	-51%
2006	-	39,013,073	73,805,247	34,792,174	-53%
2007	-	26,566,137	76,947,261	50,381,124	-35%
2008		10,412,060	119,320,897	129,732,957	9%
2009		10,012,874	91,150,782	101,163,656	11%
2010		5,560,381	31,634,786	37,195,167	18%
2011		3,743,641	6,461,628	10,205,269	58%
2012		2,156,700	8,275,750	10,432,450	26%
Total	**-**	**98,928,258**	**541,690,968**	**442,762,710**	**-18%**

Figure 45 Biological Assets Under Management

Similar biological losses were booked in FY 2014 for certain plantations, although not as extreme.

[48] http://www.tfsltd.com.au/plantation-investors/retail/project-accounts/

TFS's FY 2013 accounts show a net ***upwards*** revaluation of $12.5m to TFS owned plantations, which is plausible as TFS' company owned plantations are more heavily weighted towards beyond-2007, which, as per the table in Figure 5 (above), continued booking biological gains.

Considering how spectacularly off-mark TFS were to preliminary prospectus assumptions, and their continued inability to empirically evidence current biological assumptions, we speculate that more recent harvest (2008-onwards) will be subject to similar write offs.

We believe the 2013 write off acted as an "earnings bath" which allowed TFS to continue booking biological asset gains in FY 2014, FY 2015, and FY 2016[49]. For example:

	2013	2014
No. of Trees Owned	601,129	1,015,485
Biological gains ($'000)	12,475	63,301
Gain per tree ($)	20.75	62.34

Figure 46 Biological Gains 2013-14

Which leads to the question: who comes up with these assumptions?

How can TFS continue to report higher than reasonable heartwood content given recent harvests?

How can TFS continue to revise its biological assets upwards given recent harvests?

Are shareholders aware of TFS' loss hiding accounting practices?

[49] TFC Financial Reports, FY 2014 , 2015 & 2016 or visit http://www.tfsltd.com.au/investors/shareholders/annual-reports/

9. The Experts

'There's "…the truth", and there's "The Truth!"'

Lionel Hutz, The Simpsons

The Sandalwood Expert

TFS disclose market research data of Indian sandalwood auctions on various marketing documents including their PDS. [50]

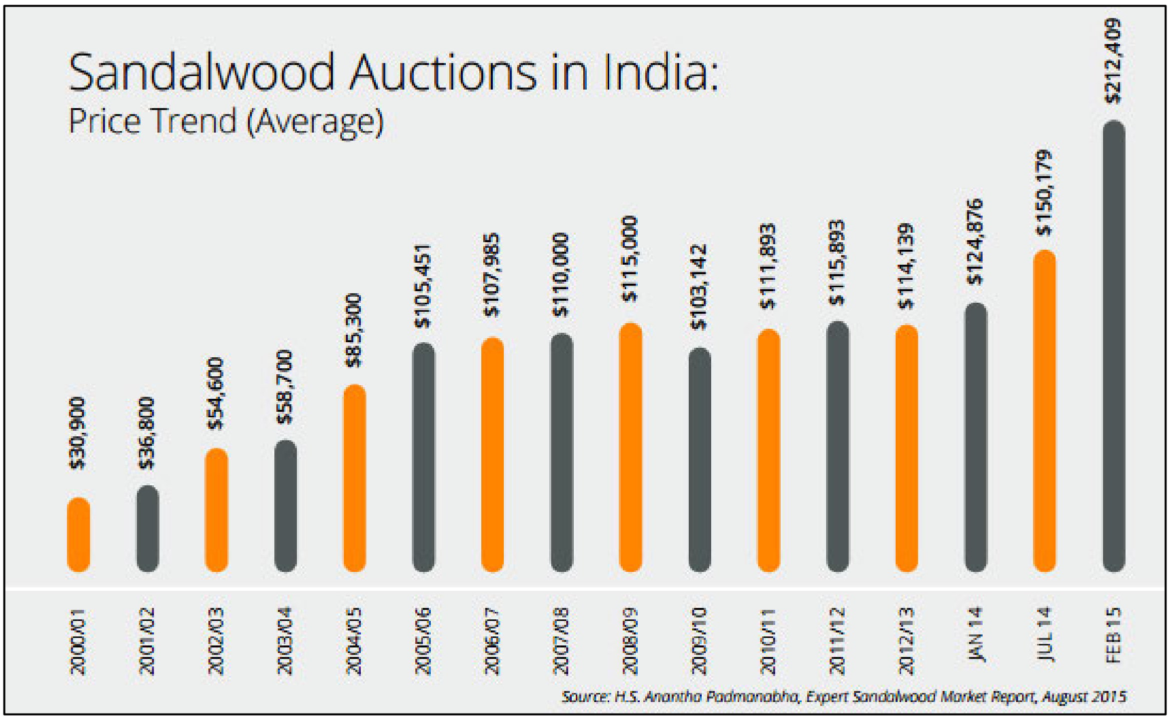


Figure 47 TFS Market Research

As alluded to in the Glaucus report, the data is sourced by "independent consultant" Dr H S Anantha Padmanabha, **who is also a biology and plantation consultant for TFS**. Previously Dr Padmanabha has advised (among others…):

- Touchwood Investments Co. Ltd – **In liquidation (insolvent)**
- Rewards Group Ltd – **In liquidation (insolvent)**
- AllRange Investment – **Tax evasion scheme, deregistered**

The above sandalwood managed investment schemes are now defunct. Touchwood's liquidation was not without issues as its directors formed a sandalwood maintenance company and continued to carry out 'work' at the expense of creditors and investors.[51]

In addition to this **Dr Padmanabha runs his own sandalwood managed investment scheme which he coins as a 'CSA' (Community Supported Agriculture) venture**, where farmers lease plots of land to investors to grow primarily sandalwood and receive a share of the returns.[52]

[50] TFC 2016 PDS
[51] http://www.sundaytimes.lk/160131/business-tim es/touchwood-liquidator-reveals-attempts-to-dupe-creditors-again-181032.html
[52] http://inacres.com/our-team/

We therefore question the data validity reported by Mr Padmanabha, as the success of his own venture is essentially leveraged by the success of TFS and his publicly available market insights.

The Incipient Capital Group

Incipient Capital Group is a merchant banking and investment services company with offices in Sydney, Abu Dhabi and Tanzania. [53]

From 2008 to 2009 Incipient Capital Group performed several advisory actions for TFS, most notably an often-cited worldwide demand study published in 2012:

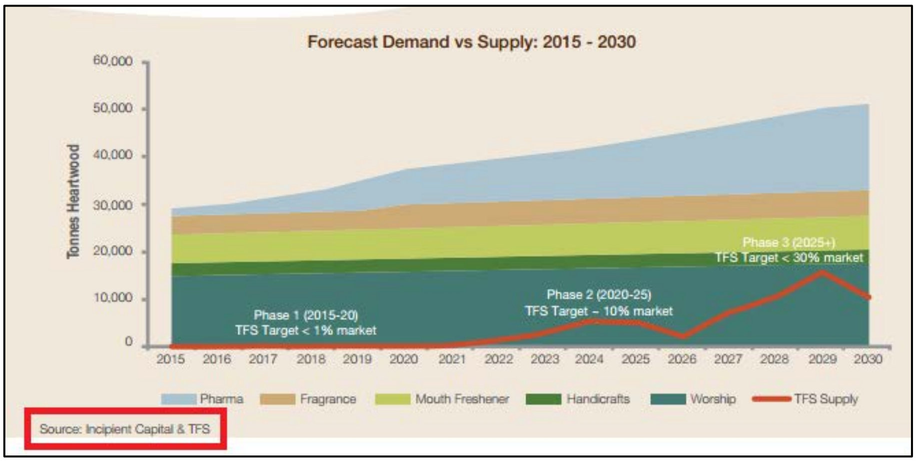


Figure 48 TFS Forecast Demand Vs Supply created/sourced by Incipient Capital & TFS.[54]

The worldwide demand is included in TFS's investment information memorandum in every year since 2012. A copy of the 2016 report (page 15) is as follows:

http://www.tfsltd.com.au/files/5514/5663/7499/SIO_2016_Information_Memorandum.pdf

The study comes from a report that cites a Global Sandalwood Conference in May 2008 which was hosted by TFS. This demand study is cited as TFS's main source on global demand on sandalwood[55].

We believe that Incipient Capital's role as source of research used for market projections is *especially* disturbing due to the conflict that exists between Incipient Capital and TFS.

Phillip Shamieh is co-founder and director of Incipient Capital. In 2009 Mr Shamieh became and still is a non-executive director of Gulf Natural Supply, a TFS subsidiary, formed in partnership with the EIG. In 2014 TFS wholly acquired Gulf Natural Supply[56].

Incipient Capital hold their Australian Financial Services License through Wise Owl, an Australian equity intelligence firm[57]. Wise Owl regularly releases 'buy' rating analyst coverage reports for TFS[58].

[53] http://www.incipientcapitalgroup.com/
[54] http://www.incipientcapitalgroup.com/pdf/Sandalwood-Demand-Study-Sample.pdf
[55] http://www.incipientcapitalgroup.com/pdf/Sandalwood-Demand-Study-Sample.pdf (if you highlight the entire blue page and copy into text, you can see all sources for the document)
[56] https://www.linkedin.com/in/phillip-shamieh-2a15a880
[57] http://www.incipientcapitalgroup.com/licensing.html
[58] https://www.nabtrade.com.au/content/dam/nabtrade/pdf/Growth_TFS%20Corporation%20Ltd%20TFC_2015.pdf

Mr Shamieh is also the founder and a director of Wise Owl, which we believe represents a material conflict of interest.

In its failure to disclose this very significant conflict of interest in its PDS, financial reports, and feasibility studies or on the ASX, TFS is **likely to have materially misled both its shareholders and its MIS investors.**

We believe these actions represent *blatant* **stock manipulation** through Wise Owl.

It is worth noting that between June 2009 and June 2012, Incipient Capital claim to have brokered at least $694m in TFS investments.

Event	Value	Role	Date
Strategic Review	Undisclosed	Advisor	Mar 08
Emirates Investment Group Joint Venture	Undisclosed	Advisor	May 09
Institutional Product Development	Undisclosed	Advisor	Jun 09
Capital Introduction from a German Consortium Fund	$4,000,000	Lead Manager	Jun 09
Investment by US-AAA rated institution	$100,000,000	Advisor	May 10
Capital Introduction from a US AAA-rated Institution	$20,000,000	Lead Manager	Sep 10
Capital Introduction from Middle East Sovereign Wealth Fund	$50,000,000	Lead Manager	Dec 10
Investment by Middle East Sovereign Wealth Fund	$250,000,000	Advisor	Dec 10
Capital Introduction from Middle East Sovereign Wealth Fund	$50,000,000	Lead Manager	Jun 11
US Secured Note Offering	$150,000,000	Co-Advisor	Jun 11
Capital Introduction from US AAA-rated Institution	$20,000,000	Lead Manager	Dec 11
Capital Introduction from Middle East Sovereign Wealth Fund	$50,000,000	Lead Manager	Jun 12

Figure 49 Capital Investment[59] [60]

[59] http://www.incipientcapitalgroup.com/advisory-and-valuations.html
[60] http://www.incipientcapitalgroup.com/capital-introductions.html

Possible Market Misconduct and Manipulation

We refer to Part 7.1 of the Corporations Act which prohibits market misconduct relating to financial products and services, and ASIC regulatory guide 232 which suggests a benchmark to be imposed on MIS responsible entities, including:

> *"Benchmark 4 – Experts*
> *Description: Where the responsible entity engages an expert to provide a professional or expert opinion on the agribusiness scheme, and the expert opinion is disclosed to retail investors in a way that may lead them to place reliance on the expert's expertise, the responsible entity only engages an expert that is independent."*[61]

In reference to:
1. TFS's undisclosed relationship The Incipient Capital Group and its managing director, Mr Philip Shamieh;
2. Wise Owl's undisclosed relationship with TFS Corporation through the directorships of Mr Shamieh;
3. TFS's obligation to stakeholders to disclose material interests of its market consultant, Dr Padmanabha's, being the marketing of his own investment scheme project and advisory of several defunct Sandalwood plantation operators.

TFS appears to be in breach of ASIC regulatory guide 232 through its release of information portrayed to be sourced by independent experts in its product disclosure statements, investment information memorandums and earnings presentations.

By publishing what we believe is a deceptive PDS for MIS investors with market projections created possibly conflicted third parties, we believe **TFS** is in breach of the following ***criminal*** offences:

1. Section 1041F of the Corporations Act : Inducing persons to deal in financial products
2. Section 1041G of the Corporations Act: Dishonest Conduct
3. Section 1041E of the Corporations Act: False or Misleading Statements

As a biased and conflicted third party through its industry market projection utilised in TFS's PDS, we believe **Incipient Capital Group** may be in breach of the following ***criminal*** offences:

1. Section 1041F of the Corporations Act : Inducing persons to deal in financial products
2. Section 1041G of the Corporations Act: Dishonest Conduct

We make note that Incipient Capital Group acted as lead manager for several large institutional MIS investments. We question whether Incipient Capital Group presented the PDS and Sandalwood industry research to institutional investors as a broker, and whether the relationship between TFS and Incipient was properly disclosed.

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[61] http://asic.gov.au/regulatory-resources/find-a-document/regulatory-guides/rg-232-agribusiness-managed-investment-schemes-improving-disclosure-for-retail-investors/

By publishing "Buy" rating analyst reports on TFS Corporation without disclosing Wise Owl and TFS are, through the directorships of Mr Shamieh, related parties, we believe **Wise Owl** could be in breach of the following ***criminal*** offences:

1. Section 1041F of the Corporations Act : Inducing persons to deal in financial products
2. Section 1041G of the Corporations Act: Dishonest Conduct
3. Section 1041E of the Corporations Act: False or Misleading Statements

The McKinsey Report

The McKinsey report alluded to by management in their Glaucus repsonse has never been published. In fact, McKinsey was never cited by management as having prepared the report prior to the Glaucus response. Management continually referred to the writer as "leading management consulting firm".

There are no sources cited in the rebuttal. As far as we know, it could be sourced from Dr Padmanabha or Incipient.

Frank Wilson purchased 50,000 shares on market with full knowledge of the McKinsey report on 23 March 2017, which is now claimed by management to be instrumental in end-market assumptions. Therefore, we believe that the **best case scenario for the company would result in Frank Wilson having committed securities fraud**, as we believe the McKinsey report would constitute material non-public information. **The company would also face action from the ASX by breaching continuous disclosure rules**.

An investigation should also commence as to how widely this report may have been distributed to institutional shareholders, as it would likely also constitute insider trading. Users on HotCopper stock forum claim to have 'read' this report[62]:

Profile
Follow
JID
3,120 posts.
Date: 28/03/17
Time: 08:25:45
Post #: 23665716

Morning guys,

I think that the response was as good as could be expected from QIN and investors/ speculators must now weigh up the merits of each argument.

For me, I view QIN as a genuine business vs. a ponzi scheme, but one that is operating in a completely new sector (Sandalwood plantations) and thus with an elevated amount of risk that a well establish business in a mature sector. This, however, represents a potential increased reward too if QIN is ultimately successful.

The risk primarily surrounds two key areas, IMO:

(a) ability to continue to source funding for the next 4-6 years until plantation sizes are at maturity - i.e. 15 years x 1,500ha per annum harvest = 22,500ha, of which QIN are currently sitting on c +12,000ha.

(b) that the operational expectations are met in regards to (i) mortality rates (ii) yields per tree (iii) demand size and price inelasticity

I have read the McKinsey report and I think that, in the fullness of time, and with the possibility of a few false starts in establishing supply chains there will be significant demand for QIN's end products with various markets exhibiting different pricing dynamics (some elastic - e.g. pan masala, and some inelastic - e.g. pharma).

Figure 50 HotCopper forum extract

Does Dr Padmanabha's track record of frauds, tax evasion and liquidations bode well for TFS' reliance on his market demand studies?

How can Incipient Capital act as independent advisors to the Company whilst simultaneously sharing directors and financial services license with a research house promoting the stock?

[62] https://hotcopper.com.au/threads/ann-resignation-of-managing-director.3324972/page-23?post_id=23669772#.WRKC9uWGOUk

10. The Arwon Loan Facility & Plantation Buyback Loophole

"It's a proprietary strategy, I can't go into it in great detail"

Bernard Madoff

The Financing Facility

Prospective TFS MIS investors are afforded the option to finance their investments through **Arwon Finance Pty Ltd (Arwon)**; a wholly owned subsidiary of TFS, funded by TFS. As background to this discussion, we refer you to the tumultuous history of MIS schemes in Australia, the Involvement of Wilson & Atkinson in Annexure 1, and the following extract from the MIS PDS[63]:

> *"Upon executing and returning an application Form, you acknowledge that the whole of the Establishment Fee is due and payable to the Responsible Entity. However, you may choose one of the following payment options in respect of satisfying the Establishment Fee:*
>
> *a. pay the whole of the Establishment Fee (and Upfront Annual Fee and Upfront Rent) upon Application;*
>
> *b. **approved applicants** can pay 20% of the Establishment Fee (and Upfront Annual Fee and Upfront Rent) upon Application and the remainder in instalments within 12 months after Application but prior to 30 June of the following financial year as agreed by Arwon Finance (the '12 Month Interest Free Loan Option'). An administration fee of $100 will apply to each 12 Month Interest Free Loan Application; or*
>
> *c. long-term finance is available to **approved applicants** for the Establishment Fee (and Upfront Annual Fee and Upfront Rent) via Arwon Finance. Enquire at TFS for an application form setting out fixed interest rates, eligibility criteria and other terms and conditions of the Principal and Interest Loan. "*

In summary; MIS investors can opt to deter the payment of fees through a loan. The repayment amount can be subtracted from the investment return at the end of the investment period.

The Buyback Scheme

TFS frequently claims their end-game is to own 100% of their plantations and aim to achieve this through increasing their investment in future plantations and buying back MIS land through a buyback scheme. The scheme offers investors a fair value for their semi-matured trees and the buyback purchases can be traced to 'Investment in Own Plantations' on TFS' statement of cash flows.

At present TFS does not have sufficient mature harvests to sell, and is still dependent on MIS investors for *cash*. At the same time, TFS is paying cash to 'buy out' MIS investors through the buy-back scheme and increasing TFS' share in the plantations.

Alluding to Section 5. - Questionable Accounting Practices, we reiterate that TFS's revenue recognition policy and mark-to-model biological valuation assumptions facilitate its access to capital, which we see is now spent on buying out "mature investments".

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[63] TFS Product Disclosure Statement 2016
http://www.tfsltd.com.au/files/1014/5516/2265/TFS_2016_Retail_Offer_PDS_Final.pdf

The Cash Skimming

The combination of the buyback scheme and the Arwon Financing facility, has allowed members of management to very quietly siphon cash from TFS and even claim commission, by:

1. Taking a *substantial* loan from Arwon to invest in the TFS MIS scheme.
2. Collecting commission for sales in the region of 10%
3. TFS immediately initiate a buyback scheme at a *large premium.*
4. Collecting the difference between the Arwon loan amount and the value of the land.
   OR
   Receive put-options to sell back to TFS in a couple of years' time.

This process occurs in a very short period of time, during which **the harvest could not possibly appreciate to the extent of the buyback value**. The *only* cash movement in this strategy is from TFS to the hands of its management; often in the millions of dollars. The best example is found within the FY 2013 financial statements[64]:

Other transactions with directors as project subscribers (on terms no more favourable than other project subscribers).
- Total new project subscriptions by FC Wilson during the year ended 30 June 2013 was $10,557,250 (GST inclusive) (2012: $1,985,544) and as a result of this he was entitled to $959,750 (GST inclusive) (2012: $218,592) of commissions to be offset against amount payable. This new project subscription was indirectly financed by a loan from a Group controlled entity, Arwon Finance Pty Ltd on normal commercial terms which has been repaid post balance date.
- After balance date the Group entered into agreement with FC Wilson and associated entity to acquire mature Indian Sandalwood trees for an amount totalling $12,393,475 (GST inclusive) as part of the Group's strategy to directly own more mature Indian Sandalwood trees. This transaction was settled on 2 July 2013 at arm's length and on terms no more favourable than three other project subscribers who also sold mature Indian Sandalwood trees to the Group at the same time. The indirect loan to FC Wilson from Arwon Finance Pty Ltd (see (v) above) was extinguished on settlement of this transaction.

Figure 51 FY 2013 financial statements

In FY 2014, Mr Wilson issued himself put options instead of immediately buying back his investment[65].

Other transactions with directors as project subscribers (on terms no more favourable than other project subscribers).
- Total new project subscriptions by FC Wilson during the year ended 30 June 2014 were 215ha at a cost of $14,190,000 (GST inclusive) (2013: $11,517,000) and as a result of this he was entitled to $922,350 (GST inclusive) (2013: $959,750) of commissions to be offset against the amount payable. This new project subscription was financed by a loan from a Group controlled entity, Arwon Finance Pty Ltd, on normal commercial terms. Included in this subscription, consistent with the terms offered to other high net worth investors in June 2014 is a put option whereby FC Wilson can sell 175ha of these trees to the Group at a predetermined price of $15.80m. This put option is to be exercised in September 2018 and would require the Group to pay the consideration in November 2018 and November 2019. This put option is consistent with the terms of the other high net worth product sales entered into in the period.

Figure 52 FY 2014 'Other Transactions'

[64] TFC Annual Report to Shareholders 2013 (page 108)
http://www.asx.com.au/asxpdf/20130913/pdf/42jc7jvg9kd6l0.pdf
[65] TFC Annual Report to Shareholders 2014 (page 100)
http://www.asx.com.au/asxpdf/20141027/pdf/42t71t5x3b0pdz.pdf

We think it is convenient for Mr Wilson that put options **were only offered to investors in June 2014, and not in subsequent or previous years**. We believe it is discouraging to see management have so little faith in the investments they are selling. Details of the options can be found in the FY 2016 annual report under 'Contingent Liabilities', because management is not of the belief that these put options will be exercised[66].

The Cash Movement

As mentioned above, these activities occur under the innocuous label of "Investment in own Plantation". The cash outflow is classified as an investment and doesn't to draw too much attention to itself as it leaves the *earnings* untouched[67]:

CASH FLOWS FROM INVESTING ACTIVITIES			
Proceeds from sale of property, plant & equipment		107	83
Payments for plant & equipment		(18,391)	(13,072)
Payments for investment in own plantation	25 (iv)	(12,966)	(7,983)
Receipts from investments		2,558	442
Payments for investments		(1,279)	-
Receipts from MIS Custodian accounts		2,340	4,221
Payments to MIS Custodian accounts		(3,786)	(2,803)
Payments for land & buildings		(1,602)	(1,313)
Acquisition of subsidiary (net of cash acquired)		(143)	-
Net cash used in investing activities		(33,162)	(20,425)

Figure 53 TFC Annual Report to Shareholders 2014 (page 45)

Note 25(iv)[68]:

- Investment in own plantation

During the year the Group acquired mature sandalwood trees from existing growers and re-acquired mature sandalwood trees from growers who had defaulted on their loan repayments and part of the proceeds ($40.08m) was offset against amounts the growers owed to the Group (included in Current Trade and Other Receivables).

Figure 54 TFC Annual Report to Shareholders 2014 (page 82)

As the Arwon loan allows these transactions to be conducted as in-house journal entries, this cash outflow is a *net* figure of the buyback sum offered against amounts outstanding by defaulting investors to Arwon.

[66] TFC Annual Report to Shareholders 2016 (page 90) http://www.asx.com.au/asxpdf/20160826/pdf/439nmz28kg4qsk.pdf
[67] TFC Annual Report to Shareholders 2014 (page 45) http://www.asx.com.au/asxpdf/20141027/pdf/42t71t5x3b0pdz.pdf
[68] TFC Annual Report to Shareholders 2014 (page 82) http://www.asx.com.au/asxpdf/20141027/pdf/42t71t5x3b0pdz.pdf

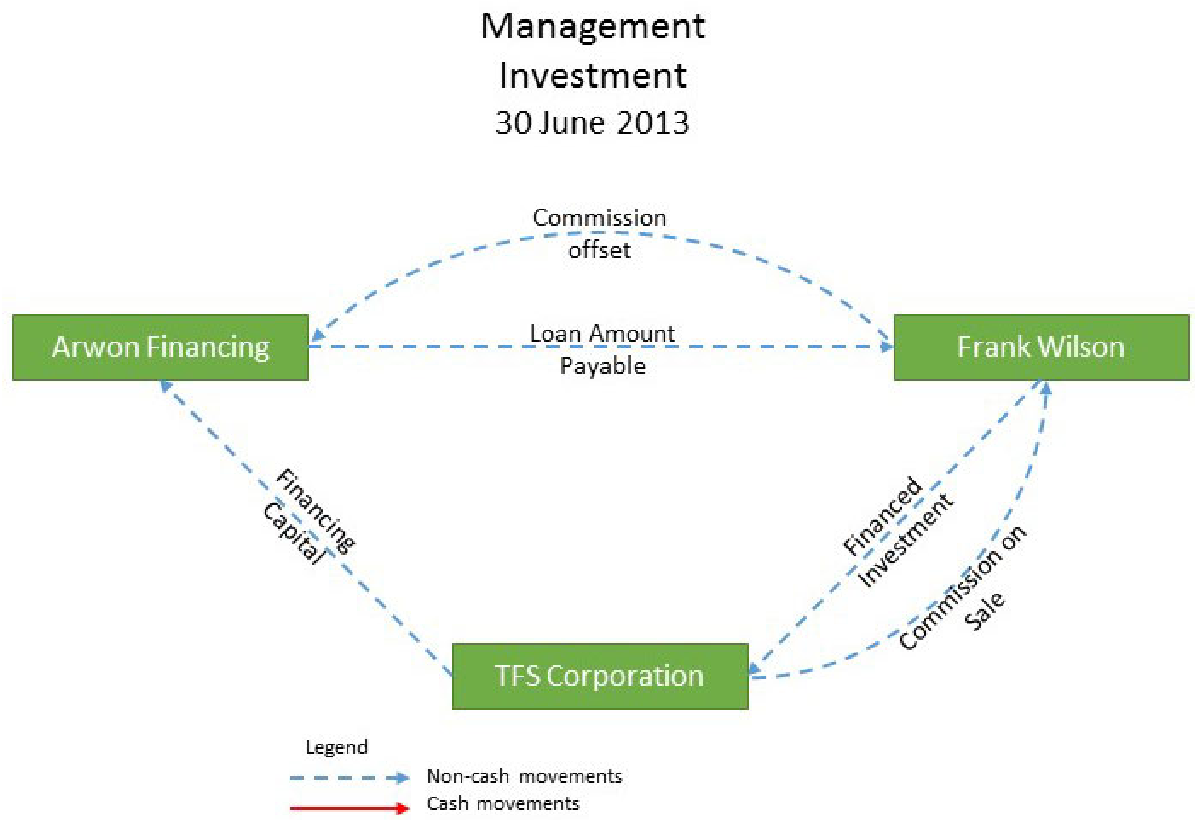
The FY 2014 annual report states that the net cash outflow amount was distributed to at least 3 other subscribers besides Frank Wilson[69]:

> - In July 2013 the Group entered into an agreement with FC Wilson and an associated entity to acquire mature Indian Sandalwood trees for an amount totalling $11,177,860 (GST inclusive) consistent with the Group's strategy to directly own more mature Indian Sandalwood trees. This transaction was settled on 2 July 2013 at arm's length and on terms no more favourable than three other project subscribers who also sold mature Indian Sandalwood trees to the Group at the same time. The final acquisitions from FC Wilson of 78.17ha were 5ha lower than reported in the 2013 annual report. The indirect loan to FC Wilson from Arwon Finance Pty Ltd to finance the previous year's project subscription was extinguished on settlement of this transaction.

Figure 55 TFC Annual Report to Shareholders 2014 (page 103)

With reference to the above wording, what terms were offered to investors who sold mature Indian Sandalwood trees to the Group at *another* time?

Illustration of the Round Robin:



Investment Initial Value – Commission Offset = Loan Amount Payable
FY 2013
$10.56m - $ 0.96m = $9.6m

Figure 56 Management Investment Example

[69] TFC Annual Report to Shareholders 2014 (page 103) http://www.asx.com.au/asxpdf/20141027/pdf/42t71t5x3b0pdz.pdf

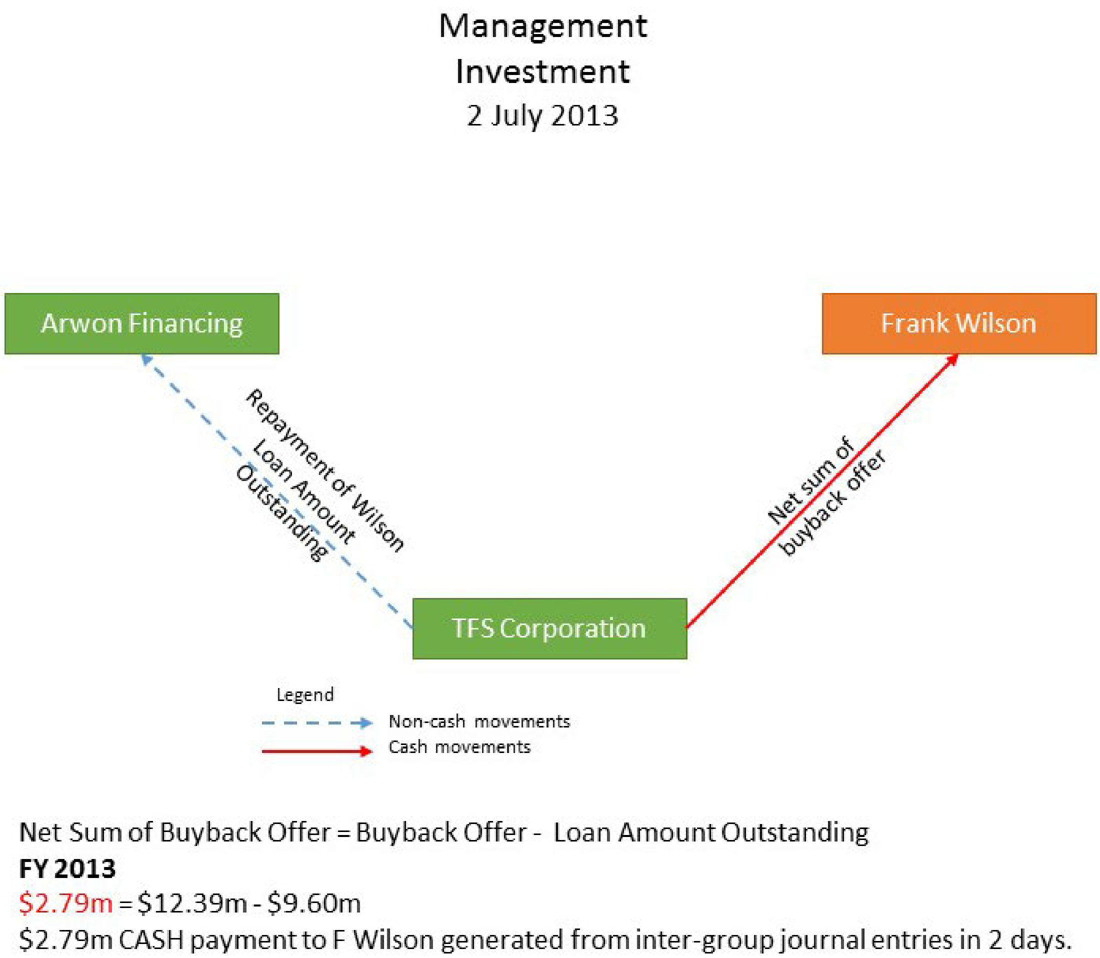


Figure 57 Management Investment Example TWO days later

Quintis Books Revenue on these company-funded management investments

We believe that a consequence of the above is that Quintis is actually buying its own revenues! There is no cash movement, except a net buyout figure to Mr Wilson, yet the transaction in FY 2013 allowed the company to book ~$10m of revenues, with similar transaction values in FY 2014.

Uncommercial Related Party Transactions

We believe Frank Wilson's Cash Skimming activities are in breach of Chapter 2E of the Corporations Act, specifically Section 208 – **need for member approval for financial benefit of related parties.**

Section 208 of the Corporations Act states that a public company must obtain the approval of ordinary shareholders in order to give financial benefit to a related party of a public company. TFS utilises an exception to this rule by claiming the transactions with Mr Wilson are at "arms-length" (i.e. on the same commercial terms provided to any other investor) per Section 2010 of the Corporations Act. We believe this is extremely contentious.

We reiterate the following notes from The Cash Skimming section of this document:

1. Put options were only offered to MIS institutional investors at the time Mr Wilson chose to buy into the MIS post 2014.
2. The plantations purchased by Mr Wilson in FY 2013 were bought back by TFS immediately upon the commencement of FY 2014 for a ***significant premium***.
3. Mr Wilson had the added benefit of a commission from sales to himself.

We believe the suggestion that either of the above transactions with Mr Wilson were at 'arm's-length' is an insult to shareholders and MIS investors. We believe ***Mr Wilson exercised discretion in his role as CEO of TFS to personally benefit from uncommercial and unfair transactions.***

It would be prudent for Mr Wilson to seek approval of ordinary shareholders for incurring these transactions, which may date back to as far as 2004.

Are shareholders aware that management is fraudulently siphoning cash from TFS?

Is the mature plantation selection for the buyback scheme entirely discretionary?

Why don't all institutional investors have the same put option terms as Frank Wilson?

11. The Target Price

$0.00 - Zero

Basis of Estimation

Sales channels are contentious. We believe the compare are engaging in desperate attempts to promote fictitious sales channels, which indicate highly marketed demand for product are also fictitious.

We believe the terms of TFS's bonds have been breached as TFS claimed escrow funds on the back of bogus institutional investor sales. We expect recourse action by bondholders, potentially commencing commercial recoveries through the appointment of a Receiver

We believe the price of the stock has been manipulated through the actions of related parties such as Wise Owl publishing third party marketing material for the company, and is subject to disciplinary action from ASIC.

MIS schemes have had a disastrous history in Australia. We allude to Timbercorp and Great Southern schemes.

Given TFS is unlikely to be able to obtain finance due to its poor corporate governance, we believe it **will not have sufficient capital to maintain plantations to maturity**.

As a worst-case scenario, we believe the company will face immense and immediate going concern risk and may have to appoint an Administrator. We believe a best-case scenario is that TFS continue to trade as an extremely highly leveraged penny stock.

The Risks

TFS still possesses substantial quantities of land, equipment and biological assets. In reference to case studies of Timbercorp Limited and Great Southern Limited, we find it unlikely that a sale of the business or assets will be achieved outside of a Liquidation fire-sale environment, save for the Mount Romance facility, which reportedly contributes $11M EBITDA to the business[70].

The Mount Romance facility still holds the position of the only sandalwood processor in Australia and is wholly owned by TFS.

[70] http://www.asx.com.au/asxpdf/20160826/pdf/439nmz28kg4qsk.pdf

12. Annexure 1: How TFS came to be…

“Make sure you pay your taxes; otherwise you can get in a lot of trouble.”

Richard M. Nixon

The tax evasion schemes of the 90’s

Australia experienced a mining boom in the late 1990s that is only just winding down today. Ground zero for this boom was outback Western Australia; towns like Kalgoorlie where down on their luck farmers beat their ploughshares into pickaxes. The result was many financially illiterate people suddenly making six-figure incomes.

With the money also came the vultures (financial planners) who aggressively solicited ‘tax effective schemes’ to blue collar workers with deep pockets

These ‘tax effective schemes’ were mostly fraudulent, however the biggest victim was arguably the Australian Taxation Office. These schemes followed a similar trend:

1. Investors would take out a loan from a financing company wholly owned by the scheme manager.
2. Investors would take out a loan default insurance from a (separate) financing company wholly owned by the scheme manager.
3. This loan and an establishment fee would be “invested” in the scheme.
4. The entire loan amount, establishment fee, management fees and loan default insurance fee was tax deductible, often resulting in a tax benefit much greater than the initial establishment fee.
5. The repayment of the loan balance remained contingent on the successful outcome of the scheme. .i.e. if there was no return, investors did not have to repay the loan (non-recourse loans).

The dream came to an abrupt end in 1999 when the Australian Tax Office (ATO) issued reassessments demanding the outstanding income tax be paid back. Investors were left with five figure bills and interest in the double digits.

Some of the scheme managers disappeared overnight, others were placed in liquidation where their limited assets were sold for scrap.

At the time Frank Wilson and Steven Atkinson were both directors of a sandalwood investment scheme which eventually served as TFS’s first plantation, the East Kimberly Sandalwood Company (EKS).

The Fighting Funds

The tax advisors that solicited some of these schemes, which may have included Wilson & Atkinson, had the audacity to ask investors for money to contribute to “fighting funds”. These fighting funds were used to pay legal firms' solicitor fees (including Wilson & Atkinson) for them to represent investors in cases against the ATO in court[71].

Six test cases were taken on by the ATO to determine precedent. Wilson & Atkinson represented the investors in 3 plus an additional case by an investor in the EKS (East Kimberly Sandalwood). They lost all cases because the court found that the schemes were primarily entered into for the purposes of evading tax. i.e. the absense of a tax scheme would otherwise have drawn no investors.

In summary, TFS was born out of the East Kimberley Sandalwood tax evasion scheme. What makes TFC different to EKS is that the loans offered to investors of the scheme must be enforced in the event that the company collapses, and not simply payable contingent on the outcome of an investment.

Due Diligence

So you can get an idea as to the extent of due diligence performed by TFS management, see Mr Atkinson's defence of the tax evading schemes industry in the 90's, heard at a senate hearing for possible MIS reform[72]:

> **CHAIR**—I understand that. We heard evidence yesterday in Kalgoorlie about investment schemes that we know have failed, such as Servcom, Oracle and Satcom. Not only have the investors got into a situation where they are confronted with tax debt but they are also being issued notices from one particular company, Servcom, with regard to that company seeking repayment of the loans or other payments associated with the scheme. I think it is a very serious issue; it is one that people such as you ought to give a lot of thought to.
>
> **Mr Atkinson**—I think in fairness—and I think this is what Kevin was saying—at the same time you have to look at the successes in the managed investment industry. Timbercorp was one of the top three most successful listed companies, if not the most successful, on the Stock Exchange in the latter half of the nineties. You have to look at the wine industry in the south-west of Western Australia. You have to look at Barkworth Olives and the absolute growth in the olive industry, which was almost non-existent six or seven years ago. I think it is very important to note that, without discriminating on a project-by-project basis, you cannot be seen to be giving a fair treatment of the industry. There are projects that have failed but, equally, there are projects that have been very successful and there are projects whose commercial viability is imperilled by only one thing, and that is the tax office's treatment of investors in that project in the last two years.

Timbercorp – Liquidated for scrap

Palandri's Wine – Liquidated for scrap

Barkworth Olives – Liquidated for scrap

[71] http://www.aph.gov.au/binaries/hansard/senate/commttee/s4655.pdf
[72] http://www.aph.gov.au/binaries/hansard/senate/commttee/s4655.pdf