Court File No. CV-12-9667-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c.C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SINO-FOREST CORPORATION

COMPENDIUM OF THE AD HOC COMMITTEE OF PURCHASERS OF THE APPLICANT'S SECURITIES, INCLUDING THE REPRESENTATIVE PLAINTIFFS IN THE ONTARIO CLASS ACTION

July 24, 2012

PALIARE ROLAND ROSENBERG ROTHSTEIN LLP
250 University Avenue, Suite 501
Toronto, ON M5H 3E5

Ken Rosenberg (LSUC No. 21102H)
Massimo Starnino (LSUC No. 41048G)
Tel: 416-646-4300 Fax: 416-646-4301
Email: ken.rosenberg@paliareroland.com
Email: max.starnino@paliareroland.com

KOSKIE MINSKY LLP
20 Queen Street West, Suite 900
Toronto, ON M5H 3R3

Kirk Baert / Jonathan Bida
Tel: 416-977-8353 Fax: 416-977-3316
Email: kbaert@kmlaw.ca
Email: jbida!@kmlaw.ca

SISKINDS LLP
680 Waterloo Street
London, ON N6A 3V8

A. Dimitri Lascaris / Charles M. Wright
Tel: 519-672-2121 Fax: 519-672-6065
Email: dimitri.lascaris@siskinds.com
Email: charles.wright@siskinds.com

Lawyers for the Ad Hoc Committee of Purchasers of the Applicant's Securities, including the Representative Plaintiffs in the Ontario Class Action

INDEX

TAB 1

MUDDY WATERS RESEARCH

Muddy Waters, LLC
www.muddywatersresearch.com
info@muddywatersresearch

Director of Research: Carson C. Block, Esq.

Company:
Sino-Forest Corporation
(TRE.TO, OTC: SNOFF)

Industry:
Forestry

Recommendation:
Strong Sell

Estimated Value:
< $1.00

Report Date:
June 2, 2011

Price:
$18.21

Market Cap:
4.2 billion

Float:
4 billion

Avg Volume:
1.4 million

- Like Madoff, TRE is one of the rare frauds that is committed by an established institution. In TRE's case, its early start as an RTO fraud, luck, and deft navigation enabled it to grow into an institution whose "quality management" consistently delivered on earnings growth.

- TRE, which was probably conceived as another short-lived Canadian-listed resources pump and dump, was aggressively committing fraud since its RTO in 1995.

- The foundation of TRE's fraud is its convoluted structure whereby it runs most of its revenues through "authorized intermediaries" ("AI"). AIs supposedly process TRE's tax payments, which ensures that TRE leaves its auditors far less of a paper trail.

- On the other side of its books, TRE massively exaggerates its assets. We present smoking gun evidence that TRE overstated its Yunnan timber investments by approximately $900 million.

- TRE relies on Jakko Poyry to produce reports that give it legitimacy. TRE provides fraudulent data to Poyry, which produces reports that do nothing to ensure that TRE is legitimate.

- TRE's capital raising is a multi-billion dollar ponzi scheme, and accompanied by substantial theft.

Introduction

As Bernard Madoff reminds us, when an established institution commits fraud, the fraud can become stratospheric in size. Sino-Forest Corp. ("TRE") is such an established institutional fraud, becoming massive due to its early start, luck, and deft navigation. At nearly seven billion dollars in enterprise value, it will now end.

TRE started humbly – as a fraudulent company going public on the Toronto Venture Exchange via reverse takeover ("RTO"). Sixteen years later, Muddy Waters would be exposing its US-listed imitators – companies such as RINO, DGW, ONP, and CCME. It seems impossible that a Chinese RTO coming public in 2010 could ever get to where TRE did. But for many years, TRE sat barely noticed on the Toronto exchange. It was committing fraud from the very beginning; but, there were not enough similar frauds to raise investors' awareness.

Then in 2003, it changed its business model – moving to a level beyond standard capex schemes that most China frauds run. Its new model, purchasing trees, gave it limitless room for growing its fraudulent balance sheet and vacuuming up money from the capital markets. At the same time, China was becoming a major investment theme. TRE became more sophisticated – engaging Jakko Poyry to write valuation reports, all the while giving Poyry manipulated data and restricting its scope of work. Thus more and more investors are drawn into TRE's fraud every year as it falsifies timber investments and manipulates Poyry further. At some point, TRE became an institution – a seasoned stock with "quality management" that consistently grew earnings over more than a decade.

Were Muddy Waters not to have come along, it is likely that this fraud could have continued for a few more years and billions of dollars more. Solving this fraud was not easy. In order to conduct our research, we utilized a team of 10 persons who dedicated most to all of their time over two months to analyzing TRE. The team included professionals who focus on China from the disciplines of accounting, law, finance, and manufacturing. Our team read over 10,000 pages of documents in Chinese pertaining to the company. We deployed professional investigators to five cities. We retained four law firms as outside counsel to assist with our analysis. We are confident that we have brought more expertise, time, and money to bear in analyzing TRE than has any investor or bank – by a substantial margin.

Executive Summary

Sino-Forest Corp (TSE: TRE) is the granddaddy of China RTO frauds. It has always been a fraud – reporting excellent results from one of its early joint ventures – even though, because of TRE's default on its investment obligations, the JV never went into operation. TRE just lied.

The foundation of TRE's fraud is a convoluted structure whereby it claims to run most of its revenues through "authorized intermediaries" ("AI"). AIs are supposedly timber trader customers who purportedly pay much of TRE's value added and income taxes. At the same time, these AIs allow TRE a gross margin of 55% on standing timber merely for TRE having speculated on trees. The sole purpose of this structure is to fabricate sales transactions while having an excuse for not having the VAT invoices that are the mainstay of China audit work. If TRE really were processing over one billion dollars in sales through AIs, TRE and the AIs would be in serious legal trouble. No legitimate public company would take such risks – particularly because this structure has zero upside.

TRE avoids disclosing the identities of all but one of its AIs "for competitive reasons." The one AI we know it has disclosed (at a credit analyst event in April 2011) is actually a connected party – to both TRE and one of its agents. Despite TRE's opacity on the revenue side, we have overwhelming evidence that the $231.1 million in Yunnan province timber TRE claimed to sell is largely fabricated. Such amount exceeds TRE's real timber holdings in Yunnan province. It exceeds the applicable harvesting quotas by six times. Transporting the harvested logs would have required over 50,000 trucks driving on two-lane roads winding through the mountains from this remote region, which is far beyond belief (and likely road capacity).

On the other side of the books, TRE massively exaggerates its assets. TRE significantly falsifies its investments in plantation fiber (trees). It purports to have purchased $2.891 billion in standing timber under master agreements since 2006. We have smoking gun evidence from Yunnan province that it overstated its purchases there by over $800 million. Of the five agents we have been able to identify (TRE does not provide Chinese names), Yunnan appears to have the only legitimate agent. The other agents have histories and connections to TRE that make it obvious they did not purchase billions of dollars in timber for TRE. Further, the other agents appear to be laundering money for TRE – moving large amounts of money to an undisclosed subsidiary of TRE and a trading company that TRE does business with. We also see clear evidence that TRE has falsified its books – Chinese government records make clear that TRE would have had a capital hole of $377 million to $922 million if it were making the investments it claims.

TRE then feeds the fraudulent data to Poyry, while allowing Poyry access to only 0.3% of its purported timber holdings. TRE touts the valuation reports as evidence of its credibility. One fresh example occurred at TRE's annual general meeting on May 30, 2011. At the meeting, CFO David Horsley emphasized to the shareholders in attendance that Poyry teams spend "six personal weeks" in the field for the valuations. On a June 1, 2011 telephone call with analysts to discuss the Poyry report, Poyry clarified that four men spent six days in the field, which the Company calculates is approximately six man-weeks.[1] Fortunately, it appears that in 2011 Poyry is becoming somewhat cautious about TRE using its name to bilk investors out of billions of dollars, and it has accordingly restricted how TRE may use the report.

TRE's claims to be "transparent" are interesting. Its offshore structure, which utilizes at least 20 British Virgin Island entities, is an unjustifiable black hole.

Auditors are far less effective in detecting fraud than most investors assume they are. The problem is that fraudsters are willing to forge documents. We show a suspicious letter from HSBC that was written on behalf of one of TRE's main subsidiaries, Sino-Wood Partners. We submitted this document to HSBC's department of fraud risk.

Another issue with auditors detecting fraud is that when the auditors are based in Canada, and the fraud is in China, the auditors are far less versed in the games fraudsters can play in China. As CCME and LFT show, even China offices of "Big Four" auditors have a number of issues detecting fraud. For most of its time as a public company, TRE's auditors have been Ernst & Young out of Canada. In TRE's case, the auditor problem morphs into another significant issue – that of TRE's poor corporate governance. TRE's board of directors appears to be the retirement plan for former Ernst & Young partners, and its audit committee members all fail PRC political,

[1] Muddy Waters is proud to say that by this methodology, we spent two man-years researching TRE and preparing this report.

industry, and cultural knowledge tests.[2] A favorite trick of Chinese RTO frauds is to gain credibility by putting Westerners without Chinese skills or background into management or onto the board. TRE probably pioneered the practice.

No fraud is complete without the payoff. Its constant capital raising is a multi-billion dollar ponzi scheme. We see some evidence of how TRE is stealing the hundreds of millions of dollars that have entered the PRC. Its financial tunnels include an undisclosed subsidiary that seems to act as a magnet for payments from many of TRE's disclosed PRC subsidiaries and the agents that purportedly purchase timber for TRE.

Valuation

Because TRE has $2.1 billion in debt outstanding, which we believe exceeds the potential recovery, we value its equity at less than $1.00 per share.

<u>Sino Forest Equity and Debt Estimated Values</u>

Sino-Forest has raised a total $3.05 billion from the capital markets. The capital structure consists of $1.892 Billion of bonds outstanding[3], Senior Secured Bank Loans of $207 million ($154.0 million from the Dec 31, 2010 financials and a new CNY 350 mil term facility. This makes debt outstanding $2.100 Billion.

In addition, it has raised $989 million of equity in shares sales going back to May 2004. Due to the SAIC filings, we know that a maximum of $1.2 Billion of cash has been injected onshore.

The Company also has a 63% stake in its listed subsidiary Greenheart Group, however, because we have concerns about this company, we do not factor it into our valuation.

The equity/credit analysis valuation analysis is very difficult as a result of the inability to rely on the audited financials and our belief that the company has far fewer assets than it reports. In order to value the equity and the credit, one has to assume one of two scenarios, both of which assume an injection amount of $1.2 Billion into China:

---

[2] TRE Management Information Circular, May 11, 2011, pp. 32-33

[3]

Issuer	Cpn	Maturity	Amt Out(M)	Curr	Mty Type
Sino-Forest Corp	9.125	08/17/11	87,670	USD	BULLET
Sino-Forest Corp	5	08/01/13	345,000	USD	CONVERTIBLE
Sino-Forest Corp	10.25	07/28/14	399,517	USD	BULLET
Sino-Forest Corp	4.25	12/15/16	460,000	USD	CONVERTIBLE
Sino-Forest Corp	6.25	10/21/17	600,000	USD	CALLABLE

Scenario 1: Assets in China are accessible to creditors and shareholders

If the assets in China were accessible, the first thing that creditors would have to do would be sell the small forestry assets that the company has and attempt to recover any cash balances. Given the propensity for theft, we will be liberal and assume that the recovery from asset sales and cash seizures is 50% of the amount injected – roughly $600 million. $50 million would be used to pay back the onshore RMB denominated debt. The rest would then need to be repatriated via a capital reduction process with SAFE, the Chinese capital account regulator. At an absolute minimum, the cost of offshoring this money would be around 15%, giving us a total recovery bull case of $467 million.

The offshore cash is not simply calculated by subtracted cash raised from cash moved into China. Management has been liberal with cash compensation. As well, they have spent $54 million on their Greenheart stake, $30 million in a consent payment for a bond exchange, and $7 million paying off Ms. Chen on the Homix purchase. If the convoluted BVI structure has yet to be used for theft, then the offshore cash balance could be as high as $1.5 Billion (Non-injected cash minus management compensation minus offshore acquisitions).

This gives us an asset base of $1.967 Billion in the best case, which we believe to be unlikely. Versus the current outstanding offshore debt of $1.893 Billion, the "real" best case net asset value is around $92 million. Divided by the current number of shares outstanding – 245 million - that leaves a share value of approximately C$0.38 at current exchange rates.

Scenario 2: Onshore Recovery of Zero.

Due to the time involved to actually change the legal representatives and liquidate collateral onshore, all the while chasing the cash balances and coordinating with authorities, historical precedent should show that there is little that can be done with onshore assets.

Using the above bull case of offshore assets, we estimate recovery for bondholders would be approximately 80 cents on the dollar, with a value of zero for the stock. Assuming that distressed investors target a 15% IRR (again, this would be extremely generous for a distressed Chinese credit), the absolute maximum an investor should be willing to pay for the credit is around 69 cents on the dollar. The recovery could be higher if less money was put into China.

Our belief is that the true recovery would be far lower, but without the aid of law enforcement, we will never really know how much money is there or where it went.

I. TRE Was Always a Fraud.[4]

TRE was engaged in aggressive fraud from the time it went public. Between 1994 and 1996, it generated between 65% to 77% of its reported revenues from an equity joint venture[5] with the Leizhou Forestry Bureau. All of these numbers were fabricated. In reality, TRE breached its commitment to contribute equity capital to the EJV. TRE's conduct so incensed the Leizhou

[4] Appendix A5 – Chinese and English translations available.
[5] China has two classifications of Sino-Foreign joint ventures: equity joint ventures ('EJV") and cooperating joint ventures ("CJV"). The main difference is that in an EJV, profits and assets (upon winding up) are distributed in proportion to the parties' equity holdings. In a CJV, the parties may contract to divide the economics disproportionately to their equity interests.

Forestry Bureau that it filed with the Zhanjiang City Foreign and Economic Relations and Trade Commission ("COFTEC") a letter containing numerous grievances. We show this letter and a translation in Appendix A5. This letter and the rest of the EJV's SAIC file make clear that the EJV never achieved the any operation remotely close to that envisioned by the partners or described by TRE in its annual reports. Moreover, the Forestry Bureau accuses TRE of misappropriating cash through improper transactions.

In its 1997 annual report, TRE claims that its Heyuan and Guangxi CJV partners took over the (fictitious) wood chip business from the Leizhou EJV – even growing it by 193% that year. Considering the base year (1996) revenue was zero, we believe investors should assume that 1997 results from the CJVs were shy of $16.1 million TRE reported.[6]

TRE's penultimate fraudulent act in Leizhou was to claim that the Leizhou Forestry Bureau reimbursed TRE $12.43 million between 1999 and 2003 through a series of payments consisting of logs. This claim that the Forestry Bureau owed TRE in excess of $10 million dollars was a gross exaggeration of the facts and contradicts the EJV's SAIC file, improperly adding $12.43 to TRE's shareholders' equity. This type of phantom transaction would become the blueprint for TRE's massive fraud.

There was another critical outgrowth from the Leizhou EJV. Upon termination, TRE converted the company to a wholly foreign-owned enterprise ("WFOE"). The WFOE's business scope[7] included "producing and selling wood products." TRE wound this company down in December 2003. This is the same year it began telling investors that it used AIs to handle its sales because it was not licensed to sell woodchips and wood based products domestically.[8] In other words, TRE wound down a business that was licensed to sell wood chips; yet, at the same time was stating that it was forced to use AIs because none of its companies were licensed to sell woodchips in the domestic market. At that time, the Leizhou WFOE could have utilized this business to take over and carry out the proprietary sales of the wood chip and processed wood business. Essentially because TRE learned that it could successfully lie about operating a factory with a party known to shareholders, it went two steps further – lying about operating a trading business with a party unknown to shareholders.

Leizhou EJV – The Ghost of Ventures Past

The Leizhou EJV, the Zhanjiang Leizhou Eucalyptus Resources Development Co. Ltd., came into being on January 29th, 1994. TRE subscribed to 53% of the equity, which was to total $10 million, and the total investment was established at $25 million. TRE's obligation was straightforward; it would contribute 53% of the investment in cash ($5.3 million) in phases. It was to inject 15% of the registered capital within three months of incorporation, and its portion of the balance of the registered capital within two years. It paid in one million dollars, which left a balance of $4.3 million. The Forestry Bureau was to contribute forest assets of 3,533 ha (note that this greatly contradicts TRE's Canadian filings, which state 20,000 ha), and other assets.[9] The articles of association show that the newly formed entity was created for the specific purposes of:

[6] Annual Reports 1997 p. 21, 1998 p. 25
[7] Leizhou WFOE business certificate April 12, 2000 See Appendix A10
[8] 2003 Annual Information, p. 22
[9] Leizhou EJV, Articles of Association, 1993 See Appendix A2

> "Managing forests, wood processing, the production of wood products and wood chemical products, and establishing a production facility with an annual production capacity of 50,000 m³ of Micro Density Fiber Board (MDF), managing a base of 120,000 mu (8,000 ha) of which the forest annual utilization would be 8,000 m³."[10]

The application included a detailed feasibility study for the MDF board production factory including financial analysis, market studies, and production plans totaling over sixty pages. Leizhou Forestry Bureau's expectation was that the factory would generate profit, provide value-added manufacturing jobs, and introduce new technology and management knowhow. The articles also reveal a plan for the Leizhou Forest Bureau to make additional land available for harvesting and replanting that would total 8,000 ha (including the original 3,533 ha). This concept formed the basis of TRE's "phasing-in" program and was also utilized to inflate TRE's forest rights claims. However, the EJV never achieved "normal operations", and neither the plans for the manufacturing facility, nor any additional land utilization or forest acquisitions were executed. The signature of TRE's president, K.K. Poon on the amended articles evidences this fact.[11]

The EJV's 1995 PRC Capital Verification Report (contained in the SAIC file) showed that the JV lost $1.1 million (RMB 8,709,107).[12] The audit report also shows inventory of only $1,100 (RMB 9,000), which is hardly the level required to support an operation making weekly shipments of woodchips of approximately $400,000, as claimed by TRE.[13] By mid-1995, TRE had still not injected the balance of investment. The Forestry Bureau solicited the local COFTEC[14] to send a formal notification reminding TRE of its obligation. By the time the contribution deadline arrived in January 1996, the TRE management team was incommunicado.[15] After the Jan 29, 1996 deadline lapsed, Allen Chan and Chan Shixing failed to respond to formal letters. They also skipped a Board meeting called to resolve the issues.[16]

---

[10] Id.
[11] Leizhou WFOE Amended Articles of Association, Appendix A3.
[12] 1995 Annual Audit Report
[13] In 1995, p. 13 of TRE's annual report claimed that TRE shipped out 204.2 BDMT of wood chips at an average price of $103/BDMT. This equals $21,032,600 USD, or approximately $420,652 per week based on a fifty week year.
[14] Zhanjiang City Foreign and Economic Relations and Trade Commission.
[15] Leizhou Forestry Bureau, Letter Requesting Termination of the EJV See Appendix A5.
[16] Leizhou Forestry Bureau, Letter Requesting Termination of the EJV See Appendix A5.

However, in Canadian filings, the Leizhou EJV was white hot. TRE disclosed the following information regarding the EJV.

Calculated Leizhou EJV Annual Sales According to Avg. Price and Qty in BDMT Reported by TRE			
Year	BDMT (Thousands)	Average price (USD/m³)	Amount (Thousands USD)
1994	156.3	85	$ 13,286
1995	204.2	103	$ 21,033
1996	212.5	102	$ 21,675
1997	45	98	$ 4,410
Total	618		$ 60,403

Source: 1994 ~ 1997 Annual Reports

TRE took a bit of a victory lap in its 1996 Annual Report, when it congratulated itself on the Leizhou EJV completing three years of profitable operations.[17] Moreover, the Company even claimed that the Leizhou EJV carried out $412,000 of research and development that year.[18] According to TRE, it was floating its partner (rather than the other way around) for $15.0 million:

> "The $14,992,000 due from the LFB [Leizhou Forestry Bureau] represents cash collected from the sale of wood chips on behalf of the Leizhou EJV. As originally agreed to by Sino-Wood, the cash was being retained by the LFB to fund the ongoing plantation costs of the Leizhou EJV incurred by the LFB."[19]

In 1998, the Leizhou Forestry Bureau finally lost its patience and submitted a letter to COFTEC containing numerous grievances, and requesting that the EJV be terminated.[20] In addition to grievances related to the failure to inject capital and develop the MDF board factory as planned, the Forestry Bureau accused TRE of improperly removing money and making payments to a third party with which the EJV had not done business:

> "After paying one million dollars, the foreign party not only failed to fully fund the company, but also approved in its own name the gradual withdrawal of funds in the amount of RMB 4,141,045.02 RMB [approximately $500,000], from the paid in capital provided by the company for the Joint Venture, among which $270,000 USD was paid out to the Huadu Baixing Wood Products Factory (花都市百兴木制品厂), which has had no business relationship with the joint venture at all. This amount of money equals 47.6% of the money [TRE's] paid in capital. Although our side has almost entirely paid in the capital to which we subscribed (all but 0.9% of the subscription total), because of the limited contribution from the foreign party, and its withdrawal of a huge amount of money from among those funds it contributed, it is impossible to put into practice the project that the joint venture aimed to construct or set up and the intended production and business operation activities. This is because the funding has been insufficient and the

[17] 1996 Annual Report, p.22
[18] 1996 Annual Information, p. 8
[19] 1996 Annual Report, p. 20
[20] Leizhou Forestry Bureau, Letter Requesting Termination of the EJV, Appendix A5.

> foreign party did not contribute the majority of the equity to which it subscribed. The joint venture therefore is merely a shell, existing in name only."[21]

In additional to phenomenally inflating the sales of woodchips from the EJV, TRE planted the seeds for a new mechanism that would propel its near infinite NAV growth, and enable it to create billion dollar forest accounts out of thin air. In the 1996 Annual Information Form, and that of previous years, TRE claims that the Leizhou JV had already "phased in" 20,000 ha of plantation lands from the Forestry Bureau.[22]

However, the Articles of Association clearly stipulate that if the project requires capitalization beyond $25 million USD total investment, then the foreign partner would contribute additional cash, and the Chinese partner would make additional in-kind contributions in the form of land use rights and forest assets.[23] Since the project was never fully capitalized, there was no need for the Chinese partner to make additional in-kind contributions, and therefore no new forest assets would have been added to the venture. Additionally, the 8,000 ha, were discussed in the Articles only in the section pertaining to the long range planning for the company. Those sections of the Articles defining the parties' respective capital contributions specifically state 3,533 ha (53,000 mu) as the Leizhou Forest Bureau's contribution.[24] In short, no additional contribution under a "phase –in" plan took place.

In addition to deducing that a scorned government EJV partner would not unilaterally contribute additional forest assets to support a manufacturing facility that had never been constructed, there is documentary proof that since inception, no significant increases in assets occurred. The EJV's PRC audit reports from 1995 and 1997 show no change in the intangible assets, under which heading forest assets are classified.[25] Had an additional 16,500 Ha been phased into the EJV, intangible assets would have increased by approximately RMB 86 million.[26]

In 1998, the two parties agreed to wind up the EJV. In the separation agreement, the parties agreed that the Forestry Bureau would receive all of the assets the Forestry Bureau originally contributed, and TRE would keep the entity and look for a new partner.[27]

Interestingly, in its 1997 annual report TRE described the agreement to terminate the EJV as entitling it to $12.4 million worth of assets from the LFB. TRE stated that it would in lieu receive payment over three years in the form of 730,440 m3 of standing timber the Forestry Bureau owned.[28]

Four years later, the 2003 Annual Report includes a claim that the Company completed its recovery of open receivables from the Leizhou Forest Bureau with a final collection in the amount of $10.2 million in the form of standing timber.[29] It is hard enough to collect on a debt

---

[21] Id.
[22] 1996 Annual Information, p. 5
[23] Leizhou EJV, Articles of Incorporation, 1993, p. 3 Appendix A2.
[24] Leizhou EJV, Articles of Incorporation, 1993, p. 2 Appendix A2.
[25] The 1997 audit report breaks out the forest rights as being valued at RMB 18,454,766. Appendix A9.
[26] The 1997 audit report itemizes the forest assets at a value of RMB 18,454,766, which equates to a total of 5,223 Rmb/Ha. A net increase of 16,467 Ha therefore should result in a net increase of 86,016,029 rmb. Appendix A9.
[27] Board Resolution, Leizhou Resources Development Company, June 3, 1998 See Appendix A6.
[28] 1997 Annual Report
[29] 2003 Annual Report, p. 34, 40

when the debtor really owes you money. It is substantially harder when you are really the debtor, and the counterparty is a government agency.

Leizhou WFOE A/R Collections from Leizhou FB		
Year	Amount ('000 USD)	
1999	$	1,125.00
2000	$	1,063.00
2001	$	-
2002	$	-
2003	$	10,242.00

Source: TRE Annual Reports

After the exit of the Leizhou Forest Bureau, the Company did not locate a new joint venture partner. In May of 1999, TRE converted the EJV into a Wholly Foreign-Owned Enterprise ("WFOE"). In April of 2000, the WFOE's new scope of business, which included producing and selling wood products, was formally approved.[30]

However, after receiving approval to reduce the size WFOE's remaining required capital contribution to only $1.4 million,[31] TRE still failed to do so for another three years.[32] In October of 2003, TRE finally wound down the Leizhou WFOE (without having contributed the additional capital). The application for deregistration was made on Oct 28, 2003 and approved by the Guangdong Zhanjiang COFTEC on November 4, 2003.[33] The key point to note is that in the 2003 Annual Report, TRE began disclosing that it needed to conduct business through authorized intermediaries due to lack of proper licensing, while failing to disclose that in the fourth quarter of the year, it was winding down an existing WFOE that had the business scope to do the business.[34]

<u>How to Succeed in Business Without Really Trying (by Finding AIs)</u>

TRE's initial AI model was that it purported to buy logs, turn them into woodchips, and then sell them to customers. TRE disclosed in 2003 that it had been engaging in this model via its Heyuan and Guangxi CJVs. (TRE makes shameless use of the corporate memory hole.)

This model appears to be a tortured attempt to create an accounting event for TRE even though it risked no capital and moved no physical goods. (TRE would later make this look less tortured by creating a third party to the transactions, the agent, which probably made its auditors feel better.)

---

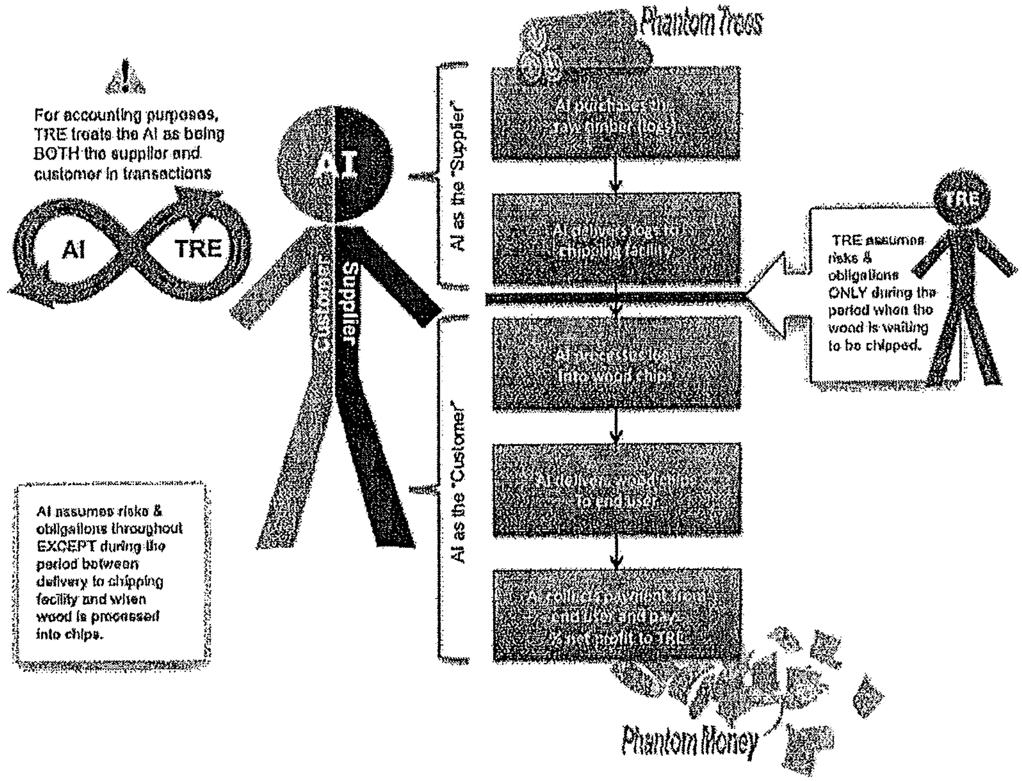
[30] Board Resolution, Dec 1, 1999; Wholly Foreign Owner Enterprise Change of Registration Approval, April 12, 2000. Appendix A10.
[31] Leizhou WFOE Application for Deregistration, Oct 28, 2003 Appendix A8; Zhanjiang COFTEC Approval for Reduction in Registered Capital, Dec 28, 1999. See Appendix A7
[32] 2000 Annual Information, p. 26
[33] Application for Deregistration of a Foreign Invested Enterprise, Guangdong State Administration for Industry and Commerce, Oct. 28, 2003 See Appendix A8.
[34] 2003 Annual Information, p. 22

According to the description in its 2006 annual information of how these transactions worked, TRE (through the magic of AIs) booked revenue and profit, but

- did not commit capital to purchase the logs,
- did not enter into contracts to purchase the logs from suppliers,
- did not take title to the logs,
- did not at any time store (let alone view) the logs,
- did not commit capital to process the logs into wood chips,
- did not contract to process the logs into wood chips,
- did not market the wood chips,
- did not enter into contracts to sell the wood chips, and
- did not receive cash from the parties purchasing the wood chips.

Instead it "agreed to reimburse the costs of the AI, including the cost of the purchase of raw timber, and to pay both a processing fee and management fee…" However, "…all of [the aforementioned fees] are deducted from the sales proceeds of the wood chips." In other words, TRE would not pay any money because the AI would be "reimbursed" when it sold the chips.

In order to make these transactions into accounting quasi-reality, TRE assumed "all risks and obligations relating to the raw timber once it arrives at the premises of the AI until it is processed into wood chips, except for any loss arising as a result of the AI's default." As the same filing specifies, the AI assumed the risks and obligations of the timber at all other times – from the time it is purchased until title passed to the customer. The below diagram illustrates the purported transactions:



Essentially, TRE's assumed risk was that a meteor would destroy the wood while at the AI's facility (assuming that the contracts lacked force majeure clauses). For this invaluable service, the AI paid TRE a fee on a "net basis after withholding of applicable taxes by the AI." In other words, there was no tax documentation that can be used to confirm whether TRE actually received any money in this way.

Believing that TRE actually generated substantial revenue this way strikes us as akin to believing in the power of diving rods to find precious metals. However, TRE was able to apply the same principles to a model that allowed it to raise billions of dollars more. The model is dealing in standing timber.

II. "AI" Really Means "Artificial Intermediary"

The structure of using anonymous parties that purportedly purchase from TRE without requiring TRE to generate VAT invoices allows TRE to invent sales figures without fear of being exposed by tax bureau records. Given that TRE has mostly been audited by accountants based in Canada, using this structure to commit fraud takes more audacity than skill. If TRE really is using an AI structure, shareholders should demand management be replaced immediately because TRE is running substantial and unnecessary legal risks. We are convinced that this model does not really exist though, so no board meeting to discuss the illegalities of the AI structure is yet necessary. As far as we are aware, TRE has disclosed the identity of only one AI, which happened at a recent credit analyst event in China. However, this purported AI's general manager, Lei Guangyu, is part of a web of shadow players spanning the AI, an agent, TRE, and Greenheart. He and the AI are closely related to TRE.

TRE May be a Great Supplier, but How Much Prison Time Would the AIs be Willing to do for TRE?

In a legitimate public company, management would be summarily dismissed for using TRE's AI structure, if it had not already been arrested. This model would violate fiduciary duties, and because it is so blatantly illegal in the PRC, would probably be beyond the scope of D&O coverage. Furthermore, it would be difficult for TRE to find a counterparty willing to work with it in this model in size. The size of the transactions is so large that the AI management would possibly be committing offenses that could land them lifetime prison sentences.

On the other hand, the cure for the problems is simple. TRE, which already has over 60 wholly-owned companies in the PRC, could buy and sell timber through new or existing WFOEs (wholly foreign-owned enterprises). It could pay its own VAT and enterprise income tax ("EIT"). This is what practically every other foreign investor with at least $100,000 in its pocket does.

It is illegal for foreign companies to engage in domestic (i.e., non-import / export) business in the PRC without having incorporated a local subsidiary to carry out the business. The PRC deems profits generated by foreign companies doing domestic business without a domestic subsidiary to be illegal. The prior two years of illegal profits are subject to confiscation. Therefore, if TRE were really using this structure for its BVI subsidiaries, they would be risking confiscation of the prior two years of their profits.

As foreign enterprises conducting domestic business in China, TRE's BVI entities would still be subject to the PRC corporate income tax. TRE's failure to pay corporate income tax for its profits generated in China would subject TRE to penalties more severe than those disclosed. The penalties (on top of the unpaid tax) would be 50% to 500% of the unpaid tax. There is no statute of limitations that would prevent the tax bureau from recovering all of TRE's unpaid taxes with per day surcharges and penalties.

Because of TRE's disclosed contingent tax liability of $156.9 million, it is clear that TRE's entities conducting a sizable portion of its business (whether foreign or domestic) are not paying taxes themselves under their own tax registration. Nor are the AI acting in a legal manner merely as tax payment agents that pay tax to the tax bureau in TRE's name. While such a situation would be critical for any company with sizable China operations, because TRE is free cash flow negative, such penalty would endanger TRE's solvency. Regardless, this is not what TRE is really doing. It is lying about selling such large volumes of timber to the AIs.

TRE would have numerous problems with the AIs trying to pay TRE's value added tax ("VAT"). Entering names other than the seller of the good on a VAT invoice is a tax crime. The penalty for VAT invoice-related crimes on large VAT amounts can be a lifetime prison sentence for managers of companies engaged in this behavior. We assume that many of these VAT payments would be in excess of the threshold to trigger such penalty; therefore, the managements of the AI would be risking the sentences in these transactions. It is difficult to understand how TRE generates a 55% gross margin from the AI on standing timber sales all the while risking their lives. TRE does not appear to add that much value.

TRE and the AIs' chances of getting away with the scheme would be low. The PRC banking system has controls in place for anti-money laundering purposes. The tax bureau is part of this platform. We consulted an attorney who is an expert in tax, foreign exchange, and banking matters. The attorney advised us that it is highly unlikely that TRE could have such large amounts of RMB sloshing around the banking system without corresponding VAT documentation. Note also as discussed infra in The Capital Hole, TRE's BVI companies would be unable to open up RMB bank accounts.

Because the AIs are not importing this timber, they would not have customs invoices, and would not be able to convert RMB into foreign currency and pay TRE offshore. While it is possible that the AIs could pay TRE offshore from the AIs' existing offshore accounts, with over one billion dollars in payments being made annually, the AIs would likely be left with unmanageable foreign currency / RMB imbalances. Therefore, the banking system and foreign exchange controls would likely have long ago ended TRE's AI business – in an unpleasant way.

Everybody's All-Intermediary: Lei Guangyu

To our knowledge, TRE has only unveiled one AI to investors. In April 2011, TRE introduced credit analysts to Lei Guangyu, who is the president of Shenzhen Hongji Enterprises (Holdings) Ltd. ("Hongji"). Both Lei and Hongji are related to TRE. At the time that TRE sold its 12.73% stake in Greenheart Resources Holdings Ltd. to Omnicorp, Lei Guangyu was the signatory for two BVI entities, Fortune Universe Ltd. and Spirit Land Ltd., which held a combined 7.41% of Greenheart. The 2007 audit report from one of TRE's subsidiaries, Heyuan Jiahe Forestry Development Co. Ltd. ("Jiahe"), lists an account payable to Hongji for approximately $400,000 (RMB 2.7 million) as a related party transaction. According to the audit report, Hongji's relationship to Jiahe is that they are both subsidiaries of the same parent. See Appendix BB1.

Hongji is engaged in irregular transactions with TRE. One of TRE's key PRC subsidiaries, Sino-Forest (China) Investments Co. Ltd. had an account payable of $4.2 million (RMB 35 million) to Hongji at the end of 2005. This is a large amount of money in the context of TRE's onshore transactions that we have been able to see. Further, it shows a flow of funds opposite of what should occur (i.e., AI to TRE).

We sent a field agent to Hongji's headquarters in Shenzhen. It has a subsidiary called Gaoyao Hongji Panel Co. Ltd.. The legal representative of this company Wang You Wang is the signatory on a lease contract for the factory belonging to Guangdong Jiayao Wood Development Co., Ltd., one of TRE's key subsidiaries. Gaoyao Hongji also appears to be the "arms length" purchaser of $30 million in machinery from TRE's Guangdong Jiayao on March 31, 2009. However, the owner of the company that leased the factory from TRE is a TRE and agent executive, Lam Hon Chiu. (We discuss more about Mr. Lam in TRE's Dodgy Timber Agents.) We are not sure what to make of this transaction, but it does not appear to be arms length to us.

As an aside, it appears that Hongji does not buy domestic timber from TRE. According to the person with whom we met at headquarters, Hongji primarily deals in timber imported from Russia and South America.

Below is Lei Guangyu's business card.

III. Gengma, Yunnan: Illegal Logging or Fraud? Timber Sales are Beyond PRC Quota

According to TRE's 2010 Management's Discussion and Analysis, the Company sold $507.9 million of Standing Timber, of which 45.5% ($231.1 million) of the sales were derived from broadleaf trees in Yunnan at an average price of 102 RMB/m^3. This equates to 2,265,000 m^3 of broad leaf timber in the form of "large logs".[35] In TRE's 2010 Annual Information Form, its claimed yield for broad leaf is between 105 to 210 cubic meters per hectare, which means that approximately between 10,800 ha (hectares) and 21,600 ha would be required for this sale. However, the 2009 Poyry report noted a regulation prohibiting clear cutting of these forests and revised the yield downwards by 50%:[36]

> Poyry has this year become aware that, under current regulations, this crop type cannot be clear-felled, but must be selectively logged, with only up to 50% of the volume allowed to be removed. Poyry has consequently adjusted the yield table for the broadleaf crop type, from 181 m^3/ha to 90 m^3/ha to reflect this constraint.[37]

At a maximum of 90 cubic meters per hectare, at least 25,000 ha would be required for this sale. That is the equivalent of approximately 96 square miles, or one and one half the total area of

---

[35] In the June 2, 2011 Poyry/Sino-Forest joint conference call, the Poyry consultant further specified that the high price for the Yunnan broad leaf of $102/$m^3$ was for "large logs"

[36] Sino-Forest Corporation, Valuation of China Forest Crop Assets As at 31 December 2009, Final Report, pp. 15 and A5-3. http://www.sinoforest.com/filings.asp

[37] Sino-Forest Corporation, Valuation of China Forest Crop Assets As at 31 December 2009, Final Report, pp. 15 and A5-3. http://www.sinoforest.com/filings.asp

Washington D.C. The volume required under either yield calculation is enormous and in excess of both TRE's contracted holdings as well as the Lincang region's local quota.

First, as described in detail in section IV of this report, TRE's contracted holdings in Yunnan are in Lincang City and amount to only 20,000 ha (300,000 mu, 15 mu = 1 ha), not the 200,000 ha claimed by the Company.[38] The 25,000 ha equates to 375,000 mu of forest land.[39] This 375,000 mu needed for the transaction is 75,000 mu in excess of its total contracted holdings and also ignores any previous depletions made in the years 2009 or 2008.

Second, the forest area required for harvest exceeds the total area available in the Lincang region under the annual quota of both 2010 and 2011 combined. In China, forest harvests have been strictly controlled through a quota system since 2001, with quotas established in the Five-Year Plans. The Provincial Forestry Bureaus proposes the quotas to the National Forestry Bureau and the State Council, which have approval responsibility. The Provincial Forestry Bureau then allocates quotas to the local forestry bureaus. Using the maximum yield estimated by Poyry of $90m^3/ha$, the minimum harvest area of 25,000 ha required to complete this sale by far exceeds the permitted logging quota for the Lincang City (which includes Gengma county) where the Company's operations and land holdings are located.[40] Our local field work in Lincang and Gengma, our calls to the Lincang and Gengma Forestry Bureaus, and open source research all confirm that this alleged sale of 2,265,000 m^3 of Yunnan broadleaf exceed the full available quota for natural forest (the classification for hardwood broadleaf) of not just the year 2010, or the two years of 2010 and 2011 combined, but all of 2010, 2011, 2012, 2012, 2014, and all of 2015! Our field agents contact the Lincang Forestry Bureau for re-confirmation of this fact, and the section chief there confirmed that the full years quota for each of 2009, 2010, and 2011 was 376,000 m^3.[41]

Yunnan Lincang City Region Annual Quota for Natural Forest ('10 & '11)	376,000 m^3
Years of Quota Req'd to Meet 2010Harvest From 2,265,664 (m^3)	6.02 years

How Much Forest Did Sino-Forest Forest if Sino-Forest Could Forest Forest?

Even if TRE's was able to simultaneous arrange unite a network of provincial traders in five surrounding regions, including from major competitors with both forests and local mills and plants, such as Yunnan Jinggu, Taixing Forestry, and Shanshui Forestry, around the common goal of filling TRE's order, there remain enormous bureaucratic and logistical obstacles. all of which could only be achieved through an miracle of political, labor, and logistics worthy of the last Great Chairman, Chairman Mao.

Assuming for a second, that all of the requisite plantation rights, logging permits, and transportation permits were properly secured, the actual task of logging still would need to be completed. The 2009 Poyry report explained that the typical harvesting practice in China as labor-intensive. This is especially so because of the required selective logging required for Yunnan broad leaf. Poyry states that, "Trees are typically felled by axe or handsaw, cut to length

[38] See Lincang City, Reply Regarding the Request for Approval D3 (English)
[39] Chinese land is typically measured in Mu (亩). 1 hectacre (ha) = 15 mu.
[40] Muddy Waters field research, and Lincang City Forestry Dept., Lincang Quota, See Appendix C1
[41] Muddy Waters field research, and Lincang City Forestry Dept., Lincang Quota, See Appendix C1

in the forest and then carried to the roadside by hand."[42] Additionally, Poyry found that logging broadleaf in Yunnan would be more expensive than any other region in China because of the mountainous terrain and the distances required for carriage of logs to a truckable road.[43] In the few of the Company's plots that Poyry visited in Yunnan in 2009, its forest description notes frequently indicate that the plots which had the best trees with "good form" or "higher stocking and standing volume" were either in places that were "remote", "several km from the nearest navigable road," or with "slopes [that are] steep up to 35 degrees" making the harvest all the more arduous.[44]

To understand the sheer magnitude of the task involved, it is important to understand that Yunnan is a remote, rugged, mountain province that rises from the mountainous border areas of Burma and Laos all the way into the Tibetan Himalayas. Lincang itself is 92% mountainous, with two peaks over 3,000 meters (9,000 ft.), Lincang Snow Mountain and Yongde Snow Mountain, and its southern border drops down to the banks of the Lancang river (headwaters of the Mekong) in a progressive sequence of mountains and valleys.[45] In this rugged geography even the less mountainous, or "hilly" areas, would make for a difficult harvest. The prospect of harvesting any sizeable quantity of logs by hand would be daunting, magnifying the inefficiency exponentially. This brings us to another major hard constraint in this supply chain: logistics.

If by some miraculous feat of human labor, the Company's army of farmers was able to selectively harvest the 2.2 million cubic meters of logs, there is the issue of actually transporting all of the wood. The roads through the mountains are dangerous, with switchbacks, steep precipices, and even no guard rails in the more remote mountain sections; roads leading into the agricultural areas are of a lower quality and often unpaved.[46] During the rainy season, which lasts from May to October, travel by road is further complicated by mud and occasional landslides. According to a local wood trader in Gengma city, Yunnan, the typical load for a small truck is about $20m^3$ and a large truck is 30 m^3. Even if TRE was able to load up all of its trucks with 25 m^3 and 35 m^3 of logs per load, somewhere between 65,000 to 90,000 truckloads would have been required to make the journey to nearest rail station 200 km (120 miles) away, assuming no losses of trucks or logs while navigating the precipices and hairpin turns.[47]

In short, unless this sale of 2.2 million cubic meters of broad leaf timber from Yunnan was fulfilled illegally (in excess of quota and without all of the requisite permits) and accomplished with an army of Chinese farmers and shipped out via a secret under-ground train tunnel running below the mountains, it either never happened or was grossly over-inflated.

IV. TRE's $800 Million Yunnan Scam Shows Timber Holdings are Forged

TRE claims to have purchased, under various master purchase agreements since 2006, timber costing $2.891 billion. Smoking gun evidence shows that TRE overstated purchases from the

[42] 2009 Poyry report, p. 21 http://www.sinoforest.com/filings.asp
[43] 2009 Poyry report, p. 22 http://www.sinoforest.com/filings.asp
[44] 2009, Poyry report, pp. A3-3 to A3-7. http://www.sinoforest.com/filings.asp
[45] Muddy Waters Research field work in Lincang and Gengma. For more information on Lincang city and the surrounding regions see: http://www.yunnanadventure.com/YunnanGuide/Lincang-Travel-Guide.html, http://www.seeyunnan.net/view.asp?id=224
[46] Blog: http://uselesstree.typepad.com/useless_tree/2011/04/dazhai-yunnan.html
[47] Muddy Waters Research Reports by FM and team.

Yunnan agent, Gengma Dai and Wa Tribes Autonomous Region Forestry Co. Ltd.[48] (also known as Gengma Forestry Co. Ltd. – see Appendix D1), which appears to be a legitimate agent, by approximately $800 million.

The value of purchases made under Yunnan master agreement is overstated by approximately $800 million. TRE announced in March 2007 that it had entered into a master agreement to purchase up to 200,000 hectares of plantation trees in Lincang City, Yunnan Province.[49] (Note that Gengma County is a sub-division of Lincang City.)

The SAIC file for TRE's Yunnan entity, Sino-Panel (Gengma) Co. Ltd. and the Lincang City Forest Bureau's 2008 – 2010 Work Completion Reports contain the following documents, which we used to understand the real terms of the Yunnan master agreement:

1) the Approval Letter by the Lincang City Commercial and Business Bureau (临商发《2007》68号) (Appendix D2)
2) the Approval Letter by Lincang City Development and Reform Commission (临发改经贸发《2007》234号) (Appendix D3)
3) the Lincang City's Forest Bureau 2008 Work Completion Report Summary and 2009 Work Leads (临林发［2009］1号) (Appendix D4)
4) the Lincang City's Forest Bureau 2009 Work Completion Report Summary and 2010 Work Leads (临林发［2010］1号) (Appendix D5)
5) the Lincang City Forest Bureau's 2010 Half Year Work Completion Report and Planning for the Second Half. (Appendix D6)

[48] This is the agent that TRE refers to as the Gengma Dai and Wa Tribes Autonomous Region Forestry Company in its March 2007 announcement of the master agreement.
[49] See Sino-Forest website.

The approval letters state that TRE has entered into an agreement to acquire 6,667 ha (300,000 mu) of forest plantation in Lincang City. TRE acquired 75,000 mu in 2007 from Gengma Forestry Co. Ltd. The Yunnan agent told us that after TRE completed this purchase, it helped TRE acquire another 13,333 ha (200,000 mu) in the nearby Lincang counties of Mengding and Cangyuan. Below is a photo of the agent's office that our field agent took.

Lest there be any doubt that the approvals omitted the other 160,000 ha that TRE claims is covered under the agreement, information about the local economy and forest industry make it clear that TRE did not enter into agreements to acquire such a large amount of forest, and at such a high per unit price.

The 2008 Work Completion Report states that Lincang City's forest industry output was approximately $380 million (RMB 2.6 billion). The report also states that the forestry business received only $32 million in foreign investment in 2008. TRE would have represented 80% of the forestry GDP for the entire city – let alone county. It would have invested approximately substantially more than the city reports in foreign investment in the industry. (Again, their main operation is in Gengma county, which is a sub-division of the city.) In the 2009 Report, the industry output reached approximately $440 million for the entire city. More interestingly, the report states that the city only issued forest rights concessions of 267 ha (4,000 mu) for the year. The 2010 semi-annual report states that as of 2010, Lincang City had issued forest rights concessions of 45,526 ha, valued at approximately $50 million. From these numbers, we can see that TRE is overstating the per hectare cost by about four times. Below is the calculation based on Lincang City's numbers:

$50 million / 45,526 ha = $1,098 per ha

vs.

TRE's claimed purchase price of $4,865 per ha.

The sheer scale of TRE's claims regarding its Lincang City, Yunnan transaction contradict reality. The Bureau of Statistics of Lincang stated the GDP of Lincang City was $3.1 billion in 2010 (Appendix D7). This contract alone would have caused local GDP to grow to four billion dollars, making Lincang the next Shenzhen in terms of growth rate.

From our fieldwork, we were told that Gengma County's 2010 total GDP was only $475 million. If TRE were to be believed, it would have been the vast majority of the entire economy of the county.

Further, we made calls to a local wood product manufacturer that appears to be one of the larger such companies in the area. He is familiar with TRE, and stated that he believes TRE purchased about 150,000 mu of plantation forest, which is in line with the documents we obtained. We spoke with a local official at the Gengma County Forestry Bureau who stated that TRE purchased 50,000 to 60,000 mu of forest. This range is a decent bit lower than the amount stated in the documents. The constant throughout is that the measurement unit is mu (again 6.7% of a hectare).

By all indications, the Yunnan agent is a legitimate agent. At least it is the only agent with a relevant scope of business. Its scope of business includes "wood and wood product purchasing, processing, and sales; forestry and forestry-related product planting, purchasing, processing, and sales; specialized economic forestry and wood project development and construction..." ("木材及木材制品收购、加工、销售；林业及林下产品种植、收购、加工、销售；特种经济林木及制品德基地建设和项目开发...")

V. TRE's Dodgy Timber Agents

Four Other Agents are Highly Unlikely to Have Sold the $2.9 Billion TRE Claims to Have Bought

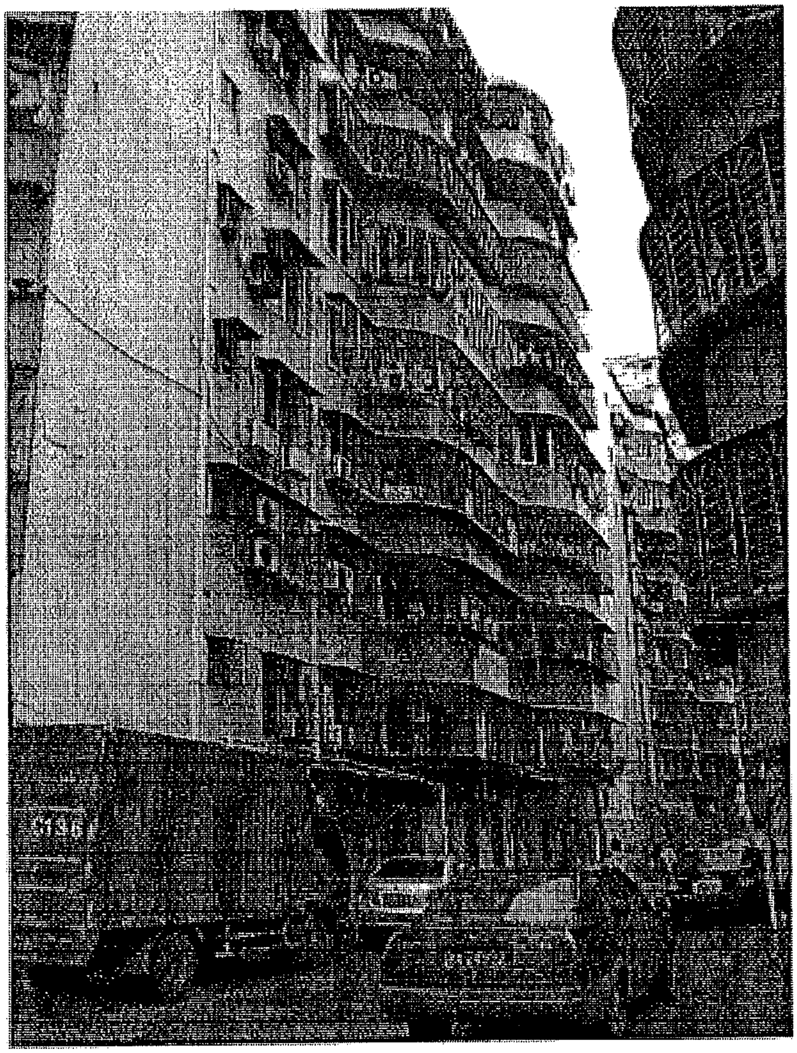
Four other agents are highly unlikely to have sold anything close to TRE's claim of a combined $2.9 billion. These agents, which would be among the largest private businesses in their locales, generally operated out of apartments while purportedly each doing annual revenue in the hundreds of millions from TRE alone. Two of these agents are managed by a senior TRE executive, Lam Hon Chiu.

TRE does not disclose the Chinese translations of its agents' names. We obtained the Chinese names from PRC audit reports (contained in the SAIC files) of various TRE subsidiaries. We show the various audit report pages with the agents' names in Appendix E1. We did not obtain the Hunan agent's SAIC file in time for this report, and we did not find the Chinese name for the Guizhou agent.

<u>Guangxi agent: Zhanjiang Bo Hu Wood Co. Ltd. (湛江博虎木业有限公司)</u>

TRE claims to have entered into a master agreement in December 2007 under which (as of December 31, 2010) it has purchased 150,000 ha of plantation for $646.6 million. We are skeptical for the following reasons:

- Bo Hu was incorporated only one month before TRE entered into this massive contract. See the business license in Appendix E2.
- Bo Hu was thinly capitalized at the time of entering into the agreement – its registered capital was only $135,000 (RMB one million) at the time. Obviously Bo Hu was not extending any credit to TRE for the tens of millions of dollars in timber purchases it was likely making at a given time.
- Bo Hu's scope of business does not include anything related to forest agency (unlike the Yunnan agent supra). Its scope of business at the time of purportedly entering into the agreement was "wood products, plywood, glues, paper products, and decoration material (木制品，胶合板，胶水，纸制品，装饰材料). Bo Hu did not add attempt to anything relevant to forest agency until September 23, 2008. See the application to change the scope of business in Appendix E2.
- Bo Hu is incorporated in Guangdong province, and would likely have substantial tax issues operating in Guangxi province (due to incessant competition among tax authorities in China). Further, all companies dealing with wood products must have a wood product permit issued by the forestry bureaus within the provincial jurisdiction. Bo Hu's license is for Guangdong – not Guangxi. See Appendix E3.
- While purportedly generating hundreds of millions of dollars in annual revenue, Bo Hu's office was in an apartment building in this apartment complex from August 2008 through sometime in 2009:



How many $200 million companies are in this apartment complex?

Bo Hu's current office is now in a proper office building, but the high level of security is unusual. On the ground floor, our researcher was stopped by security guards who seemed very cautious and alert. They questioned our researcher regarding why he was there. He was only permitted to enter the building after convincing the guards he had an appointment with Bo Hu's vice president of sales, Mr. Xu. There was yet another security guard stationed outside Bo Hu's office door on the second floor. This type of security around an office of this size is highly irregular in China.

- We spoke with a Mr. Xu, who is the vice president of sales for Bo Hu. He is certain that Bo Hu does not deal in Guangxi plantations. Mr. Xu did say however that Bo Hu is a customer of Sino-Panel (one of TRE's subsidiaries), and has been buying plywood from it since summer 2010 in volumes less than $1.5 million annually.

- Bo Hu's audit report shows that it has made substantial payments to TRE entities, including an undisclosed subsidiary. (See Appendix E4 & E5.) As we discuss infra in Glimpses of How TRE Steals the Money, we believe that some of these entities may be tunnels through which TRE steals investor funds.

- Bo Hu's 2008 audit report shows revenue of approximately $37,000 (RMB 250,189) – for the sake of clarity, that is thirty-seven thousand dollars. See Appendix E6. It is inconceivable to us that Bo Hu would be able to understate its revenue by over $200 million (or 99.9%) – at over $200 million in annual revenue, Bo Hu would be one of the larger privately-owned businesses in Zhanjiang. It would not be able to avoid booking so much revenue, in which case the revenue in the audit report would reflect much larger amounts.

Fujian Agent

- Zhangzhou Lu Sheng Forestry Development Company Limited (漳州绿盛林业发展有限公司) was incorporated on Nov. 19, 2007 (Appendix E7), just nine months before TRE entered an approximately one billion dollar (RMB seven billion) master contract with it.

- The registered capital was only $78,000 (RMB 550,000) (Appendix E7).

- The registered address was at Floor 1, No. 7 Xibian Hongyang New Village (Orchid Garden), Shan Cheng Village, Nanjing County (南靖县山城镇溪边宏洋新村（兰花园）7号1层) until November 29, 2010 (Appendix E10). This address is the personal residential address of Mr. Wang Rui Mei (Appendix E8), who is also listed on the SAIC filings to be the legal representative, executive director, supervisor, and manager of the company (Appendix E11).

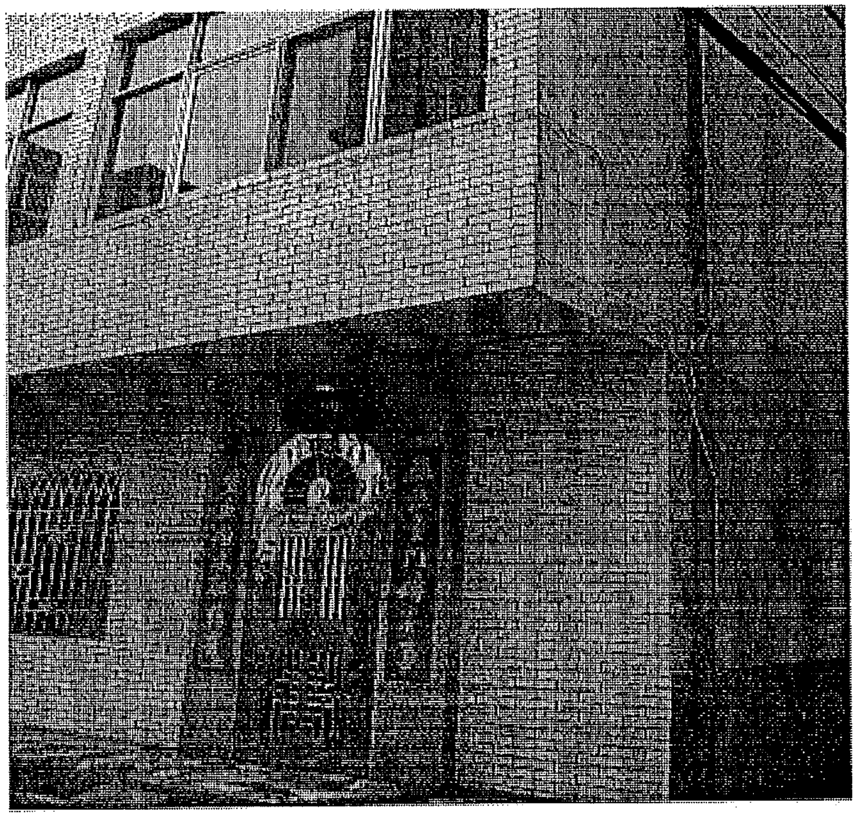
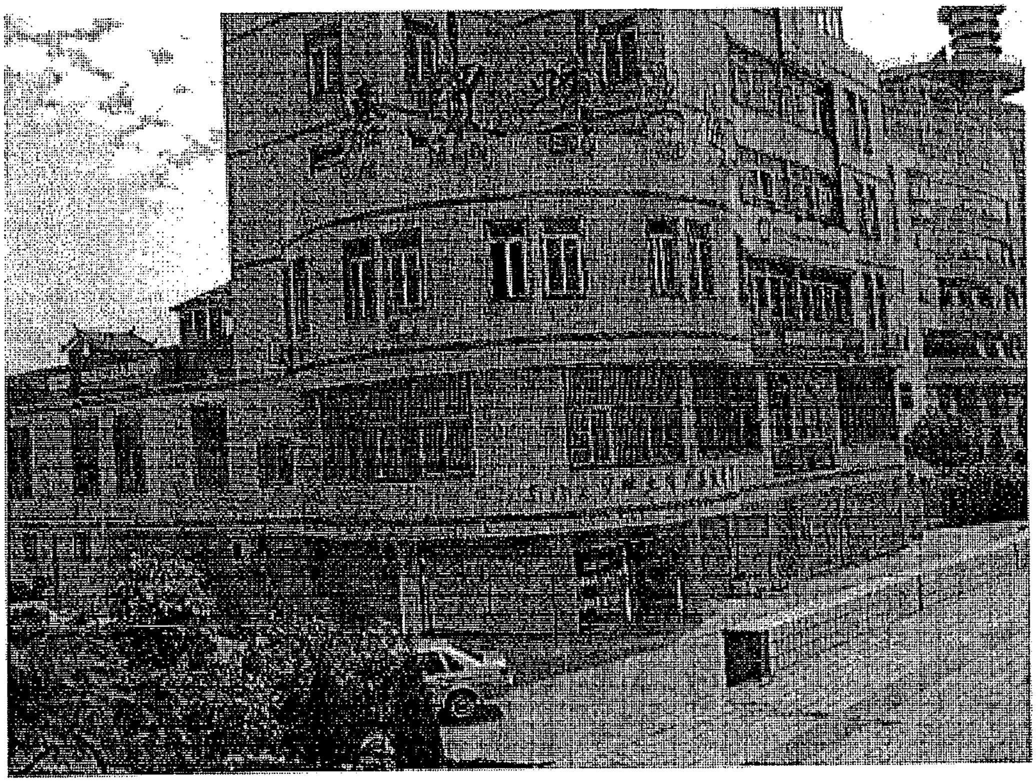
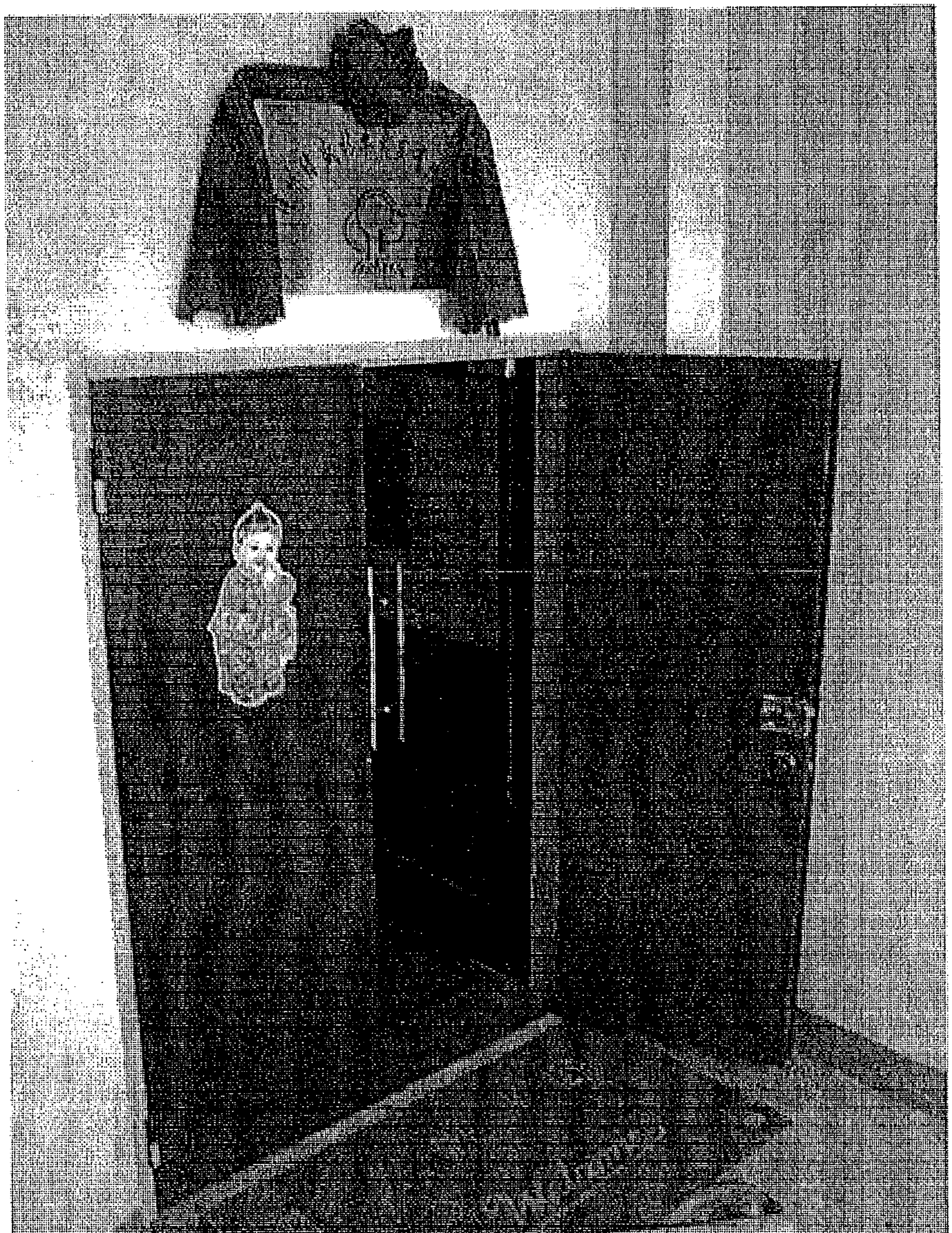


Image 10 No 7 Orchid Garden

- A copy of the master agreement signed by TRE and Zhangzhou Lusheng was found in the Sino-Panel (Fujian)'s SAIC files (Appendix E9a-E9g). It is a contract with a total of seven pages with no terms regarding liability – it seems to be an unlikely billion dollar contract. Interestingly, the contract stated that as of the time signing the contact Lusheng has already been authorized by the owners of 200,000 Ha of the forests in Fujian to act on their behalf. However, Lusheng did not have any wood or forestry related license at the time it entered into the contract.

- We sent a team of field agents to visit Zhangzhou Lusheng in Fujian. Our agents located the new registered address at 5th Floor, Jiamao Honey Industry, No 362 Construction Road, Shancheng Town, Nanjing County (南靖县山城建设路 362 号嘉贸峰业大厦 5 楼)。





Field enquiries confirmed that Zhangzhou Lusheng operates at the address on the 5th floor. There are four desks in Zhangzhou Lusheng's office, which appeared to be approximately 180 m2 with 5-6 employees in the office at the time of visit. This implies that Lusheng has an extremely efficient computer system (given that it processes so much money and so many payments with a small staff).

- Our researcher paid a visit to the Nanjing County Forestry Bureau and spoke with the Unit Head Mr. Ma there. Mr. Ma claimed that he has not heard about Zhangzhou Lusheng nor has he heard of Wang Rui Mei.

Jiangxi Zhonggan

- This agent is a related party. The legal representative and President of this company is TRE executive vice president, Lam Hong Chiu.

- Jiangxi Zhonggan Industrial Development Company Ltd ("Zhonggan")江西中赣实业发展有限公司 was incorporated on January 28, 2009 just five months before TRE entered into an approximately $700 million contract on June 16, 2009. See the business license in Appendix BB2.

  - Yun County Electronic Paper (云县电子报), an online newspaper operated by the Yun County local government (中共云县委云县人民政府主办), published an article naming Lam Hon Chiu as the general manager of Hong Kong Sino-Panel Company who has visited Yun County with government officials on July 23rd, 2010. http://61.166.10.99:8011/Qnews.asp?ID=5340&QID=1837 (Appendix E12)

  - Dongkou County Hunan, an online article published on Dongkou County government website stated that on Feburary 5, 2007, the county government met with the top management of Canadian Sino-Forest Group including Chairman Allen Chan (陈德源), VP Ye Han Xiang (叶翰祥) and VP Lam Hon Chiu (林汉钊)at Changsha discussing the possibility of investment in Dongkou County. http://dongkou.mofcom.gov.cn/column/print.shtml?/zhongyaozt/200707/20070704898019 (Appendix E13)

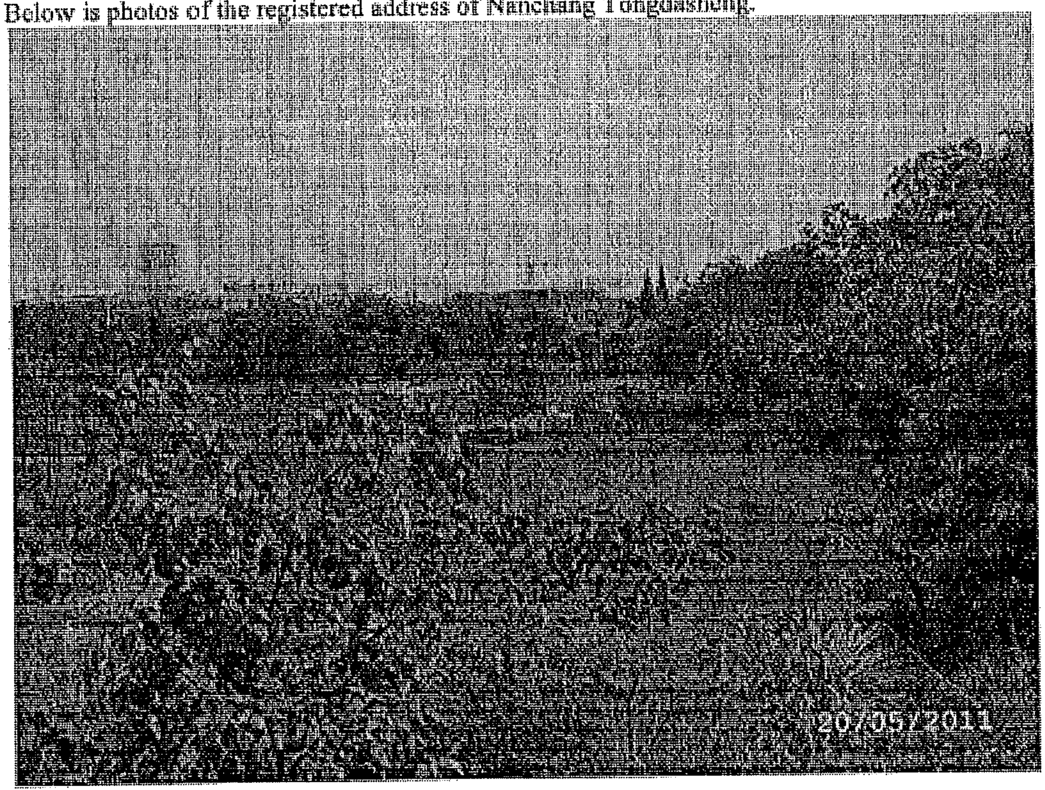
  - Qiqihaer City Heilongjiang, an online article published on June 20, 2006 on the Qiqihaer city's government website stated that the Qiqihaer government official met with the VP of Sino-wood (Asia) Limited Lam Hon Chiu (林汉钊) on their trip to Hong Kong to discuss investment in Qiqihaer City. http://www.qqhrmofcom.gov.cn/index.php3?file=detail.php3&kdir=2200134&nowdir=2030157&id=830707&detail=1 (Appendix E14)

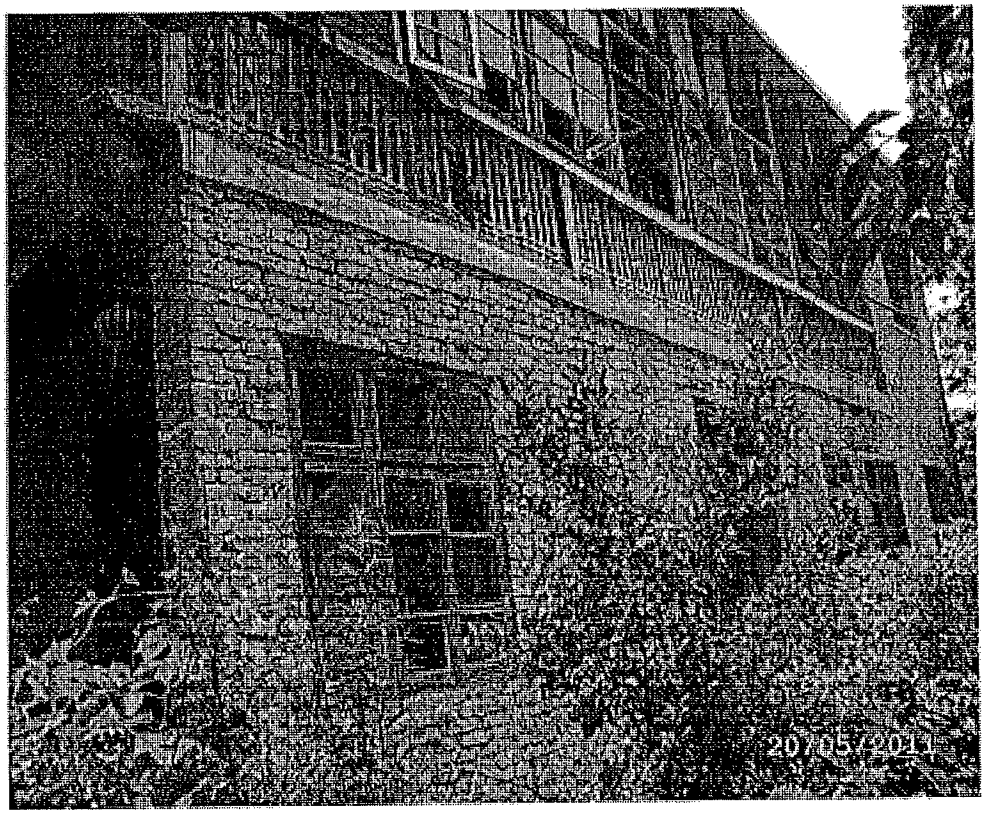
  - On one of the company listing website http://www.bldg-materials.com.hk/master.php?keyword=1854 listed Lam Hon Chiu as the Senior Manager of Sino-Panel (Asia) Limited. (Appendix E15)

  Jiangxi Zhonggan is clearly a related party related party.

- Jiangxi Zhonggan is a joint-venture incorporated by Hong Kong China Square Industrial Ltd. 香港中国坊实业有限公司 (China Square) and Nanchang Tongdasheng Industrial Company Ltd. 南昌市通达盛实业有限公司 (Tongdasheng) with a total register capital of USD 5 million with USD 4 million by China Square and USD 1 million by Tongdasheng.

- China Square is a company registered in both Hong Kong and BVI with Lam Hon Chiu as its legal representative, it seems to be a shadow actor on TRE's behalf to setup undisclosed but related subsidiaries in China.
- By looking at the SAIC file of Jiangxi Zhonggan's Chinese partner Nanchang Tongdasheng, we don't see any reason for its existence except that TRE needs a Chinese name to legally register a joint venture as its agent in Jiangxi. Tongdasheng was incorporated November 3rd, 2006, with a registered capital of 500,000 RMB. The registered address is a fishing village near Nanchang city 南昌市西湖区桃花镇渔业村. The business scope is Domestic Trading 国内贸易 (Appendix E16). According to the 2009 Annual Check Report in the SAIC files that the revenue of Tongdasheng for 2009 is USD 14,909.84 (RMB 104,368.93) with a net profit of USD 326.58 (RMB 2,286.07). It is nearly impossible for such a company to invest on its own with USD 1 million to setup Jiangxi Zhonggan with China Square unless someone else is "funding" the amount.
- Below is photos of the registered address of Nanchang Tongdasheng.





The 2008 and 2009 Jiangxi Zhonggang's audit report shows numerous large transactions between the Company, TRE, and other parties. However, none of these transaction is forestry related.

VI. The Capital Hole

Chinese government records show a capital hole that makes claimed timber purchases impossible.

China imposes capital controls that ensure there are records of significant movements of foreign currency into China. From TRE's PRC company SAIC files, it is clear that TRE's cash needs in China outstrip the capital it has contributed to its China operations by at least $377 million, and possibly quite more. China's capital controls prevent TRE from funding its operations from outside of the PRC by purchasing trees through payment of foreign currency.

When an existing PRC company wants to bring foreign currency into China as investment in the business, it applies to the Ministry of Commerce, the State Administration of Foreign Exchange, and the State Administration of Industry and Commerce ("SAIC"). Once the authorities approve the application, the company may bring in the approved amount of foreign currency. When an investor forms a new foreign-owned company, it must specify foreign currency it will invest.

The authorities will review the entire establishment application, including the portion requesting the right to bring foreign currency into China.[50]

A given company's SAIC file shows records current within a few months of all applications for injecting equity capital. Further, PRC law requires equity capital injections to be verified by PRC licensed accountants. The amount of debt a company can borrow is limited by law, and SAIC records reflect the amount of money that a company is approved to borrow from offshore. However, debt injections are not recorded in SAIC files. We totaled up all of TRE's actual equity injections and approved debt injections (again, the debt capital is not verified, but we gave TRE the benefit of the doubt), and the amount of capital that went into TRE's PRC operations is only \$1.213 billion since 1994. Its investments were \$1.7 billion larger than its operating cash flow during this period. (Note that these figures also exclude the need for operating cash.) Therefore, TRE has a capital hole of \$377 million to \$922 million. It could not have purchased the trees it claims to have.

(USD millions)	
OCF	3,308
CapEx - Disposals	5,058
Total ST Borrowings incl. Repayments	160
Onshore Capital Need	1,590
Capital Contributed - High	1,213
Capital Contributed - Low	668
Onshore Cash Hole - Low	377
Onshore Cash Hole - High	922

Cash flow numbers from Bloomberg. To be conservative, we assumed that all short-term borrowings were onshore.

TRE could not have funded its business with foreign currency. If TRE were going to pay the supplier in foreign currency, it would be illegal unless the goods sold were for export. Because the investments are not for export out of the PRC, the sellers would not be able to obtain customs declarations. Large amounts of foreign currency hitting the sellers' bank accounts without accompanying customs declarations would be quite risky for the sellers just on a one-time basis – such a transaction could lead to inability to convert the currency, and issues with the customs and tax bureaus. We do not believe that TRE found suppliers willing to engage in transactions with such large risks throughout its 16-year reporting history. Therefore TRE could not have made these investments by paying the sellers in foreign currency in the PRC.

TRE's agents under the master purchase agreements are thinly capitalized (see infra TRE's Dodgy Timber Agents). They could not have each funded hundreds of millions of dollars in undocumented currency swaps done through offshore bank accounts.

[50] For more on how China's currency controls work, see Collins, Robert and Block, Carson "Doing Business in China for Dummies" (Wiley 2007), chapter 9.

TRE's only means of funding these investments would have been by injecting investment capital into its own PRC companies, which it did not do in sufficient amounts. Therefore, TRE's claimed investments and revenues are fraudulent.

VII. TRE's Manipulation of Poyry Reports

TRE's abuse of Poyry's name is well-illustrated by a recent statement that TRE CFO David Horsley made at the annual shareholders' meeting on May 30, 2011 that Poyry teams spend "four to six personal weeks" in the field evaluating TRE's holdings. On a June 1, 2011 call the statement was clarified to mean that a team of four people each spends six days in the field, so that the total approximates six man-weeks of work. (Amusingly reminiscent of Bill Clinton's "I did not have sexual relations" comment.)

Since 2003 Poyry (Beijing) and its Shanghai branch have been engaged to conduct reviews of TRE's operations and value its assets; however, Poyry's purpose is only to estimate the market value of the forest assets based on information provided by TRE, and not to perform due diligence or confirm the ownership of the forest areas.[51] In numerous locations throughout the reports, Poyry adds disclaimers, stating:

- Poyry has not viewed any of the contracts relating to forest land-use rights, cutting rights, or forest asset purchases [52]
- It is important to understand that this is not a confirmation of forest ownership, but rather a verification of the mapped and recorded areas of stocker forest.[53]

However, despite a generally favorable report, Poyry nevertheless cannot hold back a degree of astonishment at TRE's unusual trading practices, describing in the reports opening paragraphs that TRE's forest holdings are "dynamic" (emphasis provided by Poyry).[54] Poyry states, "Unlike most forest owners and managers, Sino-Forest actively trades in forests. Each year the company both sells and buys forests, and accordingly the composition of the forest estate changes much more than for a business that is simply managing and harvesting a more static resource."[55] This fact greatly complicates its inspection and valuation process as "the composition of Sino-Forest's estate can change quite significantly from one year to the next."[56]

Certainly such dynamic trading complicates inspection and verification activities, as it is tantamount to a giant shell game. With a maximum of only 53% of existing 2008 forest being carried over into 2009,[57] it is easy to disclaim any specific accusation of lack of forest rights ownership in any given plot or region.

---

[51] Conference call, June 1, 2011, Poyry valuation discussion.
[52] 2009 Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. iv http://www.sinoforest.com/filings.asp
[53] 2009 Poyry, p. 12
[54] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. vi & 8
[55] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. vi & 8
[56] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. 8
[57] 2009 Poyry report, Valuation of China Forest Crop Assets As at 31 December 2009, 23 April 2010, Rev 03, www.sinoforest.com/filing.asp, p. 8

In introducing its methodology for assessing risk into the discount rate calculation, 2009 Poyry explains that the valuation of forest crop assets faces challenges, including:

- The reliability of forest descriptions
- The accuracy of yield prediction
- Achieving high growth rates in a consistent manner[58]

The Poyry report explains that its review of forest land holdings consisted of selecting 66 cluster maps that represented only 1,611 ha of forest, or only about 0.3% of TRE's claimed 491,000 ha.[59] During the June 1, 2011 conference call, Poyry revealed that the figure for the 2010 assessment was only 0.1% of estate holdings due to the substantial increases in newly acquired plantations. Poyry further reveals that current yield tables for these forests have not been properly established.[60] Poyry has performed some field studies and collected sample data from various plots, but its statistical analysis comes with the caveat that "in comparison with most other forests, the large Sino-Forest estate is significantly under-sampled for growth and yield purposes."[61] In short, due to the poor quality of data and documentation on the forest plot, until there is an opportunity to both verify the forest's physical characteristics and use satellite imagery on all forest claims, that the sample sizes are too small to establish significance. Poyry and all investors then can only take TRE at its word that the remaining 99.9% of its purported holdings are accurate in terms of their size, yield, and composition.

<u>Do You Think a 2.5% Risk Premium on TRE's Discount Rate for WACC Seems a Little Low?</u>

Poyry's 2009 report includes an appendix detailing the calculation method for the discount rate, WACC, and CAPM; wherein the consultant, Dr. Mardsen, from the University of Auckland's Dept. of Accounting and Finance of the School of Business, provides details on formulas used to value a generic forest asset in the China. Dr. Mardsen repeatedly emphasizes the need to keep in mind the additional risk associated with developing markets, such as <u>capital controls</u>, <u>political instability</u>, <u>corruption</u>, <u>poor accounting</u> and <u>managerial controls</u>, an <u>uncertain legal framework</u> and <u>lack of protection of investor property rights</u>; and factor a premium onto the discount rate of the cost of capital, stating: [62]

> In China and in emerging markets the level of corporate governance may vary significantly between companies. Corporate governance is important as it provides mechanisms whereby outside investors can protect themselves against <u>expropriation by insiders</u>. Corporate governance can impact on the risks that outside investors may face in respect of any expropriation of assets. These factors together with the size and other market frictions may warrant an adjustment to the cash flow expectations and/or an

[58] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. 55
[59] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. 11
[60] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. 17
[61] Poyry, Sino-Forest Corporation Valuation of China Forest Assets as at 31 December 2009, Final Report, 23 April 2010 Rev. 03, p. 17
[62] 2009 Poyry Report Appendix: Uniservices, Investment Appraisal for Forest Investment in China, 5 Jan 2010. P. 5

> increment to the cost of capital for the forest if investors' property rights are not clearly defined. Where control is not obtained a minority discount and / or illiquidity discount many apply. [63]

Dr. Marsden calculates the real pre-corporate tax WACC range of between 7.1% to 12.8%. Poyry then selected the current 8.5% to 9.0% discount rates in New Zeeland and adds a 2.5% to 3.0% resulting in a discount rate of 11.5%, providing for the 2006 pre-tax cash flow valuation of TRE's assets at $2,297.5 million USD as of December 31, 2010.[64] But, Dr. Marsden closes with a note and a warning:

> If significant corporate governance and agency cost issues between insides and outside investors arise (e.g. from lack of transparency, possible risk of expropriation of assets, restrictions of remittance of profits, or exchange rate control), the use of cost of capital at the upper end of our range may be warranted.[65]

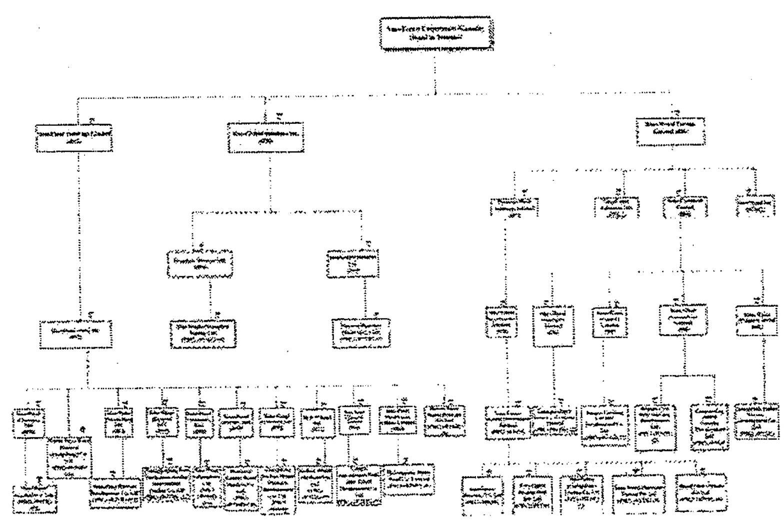
It begs the question; if evidence of systemic and comprehensive fraud and illegal activity is discovered in the Company from inception, throughout its operating history, and into the present, by how much would the discount rate need to be adjusted?

---

[63] 2009 Poyry, P. 4, 5
[64] 2009 Poyry, p. vi; 58; 2009 Poyry Report Appendix: Uniservices, Investment Appraisal for Forest Investment in China, 5 Jan 2010. P. 23.
[65] 2009 Poyry Report Appendix: Uniservices, Investment Appraisal for Forest Investment in China, 5 Jan 2010. P. 23

VIII. Egregiously Complex and Opaque Offshore Structure

In TRE's 2010 annual information form, it discloses that it has at least 20 British Virgin Island ("BVI") entities. As a recent South China Morning Post article points out, BVI is the favorite domicile of Chinese seeking opacity. There is no public shareholder registry, and there are no requirements to file tax returns. TRE no longer discloses its organizational chart, but the last one it made available in an annual information statement is from 2007 – see below. This structure is highly opaque, and in our view, unnecessary for legitimate business purposes. It is not a tax-optimized structure either due to direct ownership of PRC entities by BVI subsidiaries. (Dividends remitted to Hong Kong holding companies are taxed at a lower rate than dividends to BVI owners.) We therefore pose the following question to TRE's management (given its emphasis on its transparency): "Why have you structured the business in this way?"



IX. Suspicious Bank Document

Suspicious Bank Document.

The following bank letter appears to be written on behalf of Sino-Wood Partners, Ltd. We found it in incorporation applications in the SAIC files for four of Mandra's entities. TRE, which now owns 100% of Mandra, was a founding shareholder of Mandra with a 15% stake. Sino-Wood was the entity that was reverse merged into the public shell to make TRE a public company. It had been expected to IPO in 2003, but the IPO was unexpectedly canceled.

HSBC

PRIVATE & CONFIDENTIAL

Ref:

CMB TSD Division B

Relevant Approval Authorities and Administration Authorities for Industry & Commerce

1 February 2005

Dear Sirs

Re:MANDRA FORESTRY ANHUI LIMITED

At the request of Sino-Wood Bartners,Limited(the "Company"),we have pleasure in advising that the Company has maintained an active and satisfactorily conducted current account with us.General banking facilities to the extent of HKD medium eight figures have been granted to the Company on an unsecured basis. For the past twelve months, we have haneled their import/export bills business with satisfactory results.We. consider the Company is good for normal business engagement.

The aforesaidinformationis given in strict confidence and without any responsibility,howsoever arising,on the part of the Bank or any of its officers.

Yours faithfully

Regina Lee
Relationship Manager

c.c, Mandra Forestry Anhui Limited

The Hongkong and Shanghai Banking Corporation Limited
Tsim Sha Tsui District Commercial Banking Centre:
10/F HSBC Building Tsim Sha Tsui, 82 Nathan Road, Kowloon, Hong Kong
Tel: 2735 9111 Fax: (852) 2721 7648

X. Shoddy Corporate Governance

Internally, TREs fraud was enabled by poor corporate governance. The corporate governance issues include the following:

- TRE's board appears to be the retirement plan for partners of its auditor, Ernst & Young. It currently has five directors on its board from E&Y. We believe that such a clubby atmosphere can dull the auditors' ability to perceive problems.
- We are bothered by senior management's practice of paying its salary via fees to a consulting firm – this is inappropriate for a public company with a multi-billion dollar market capitalization. More disturbing is senior management's C$12 million buyout of its own shares in subsidiary with investor funds. (The subsidiary's planned 2003 IPO was unexpectedly canceled.)
- TRE failed to disclose a 2003 petition to wind it up at the listed company level.
- TRE has failed its internal control test. The 2010 failure is due to senior management personally handling settlement of accounts receivable and accounts payable. This is particularly troublesome because the notes to TRE's financial statements appear to state that the majority of TRE's receivables from its accounts receivable are paid by TRE's AIs to TREs agents to pay off timber purchases. If our reading is accurate, then a substantial portion of TRE's purported revenue would not even be expected to hit its bank account, thereby making the fraud substantially easier to carry out.

XI. Glimpses of How TRE Steals the Money

- From reviewing TRE and the "Agent's'" annual inspection and audit reports from the SAIC files, it seems that the agents mainly serve as a tunnel to move money for TRE.
- These agents generally report little to no revenue or profit, and pay little to no tax. However, they have balance sheets orders of magnitude the sizes of their revenues. The balance sheets mainly consist of receivables from TRE entities, and disturbingly, payables to TRE entities.
- Both Yunnan and Guangxi agents are sending a large amount of money to TRE's undisclosed subsidiary, Huaihua City Yuda Wood Co. Ltd. This subsidiary is based in Huaihua City, Hunan Province, which we suspect is the nerve center for TRE's illicit activities. We tried mightily to obtain SAIC files for TRE's four subsidiaries and the Hunan agent, but we were only able to obtain minimal information (such as shareholdings) after much effort. This is highly unusual.
- Payments to farmers and collectives for forest are noticeably scarce in the financial statements of the agents.
- The following tables shows the finances of three agents for 2008 and 2009

2008	Zhanjiang Bohu 湛江博虎	Jiangxi Zhonggan 江西中赣	Gengma Forestry 耿马林业
Revenue	¥250,188.59	¥0.00	¥161,944.45
Tax Paid	¥16,280.71	¥0.00	¥545,651.87
Profit	(¥707,828.30)	(¥473,604.40)	(¥1,730,241.89)
Total Assets (Year End)	¥328,764,932.35	¥78,342,694.60	¥127,590,736.52
Total Debts (Year End)	¥328,478,921.42	¥44,400,000.00	¥122,287,992.44

2009	Zhanjiang Bohu 湛江博虎	Jiangxi Zhonggan 江西中赣	Gengma Forestry 耿马林业
Revenue	Not Available	¥58,516,200.00	¥455,400.00
Tax Paid		¥0.00	¥122,757.00
Profit		¥42,528,626.48	(¥1,199,609.00)
Total Assets (Year End)		¥619,731,395.86	¥121,465,482.00
Total Debts (Year End)		¥543,260,074.78	¥120,338,833.00

Bohu's 2008 Transactions (TRE entities are highlighted) (Appendix E4 and E5)

Bohu 2008

Prepayments Made

Shaoyang Jiading (TRE)	邵阳嘉鼎	¥49,871,398.63
Hunan Jiayu (TRE)	湖南嘉裕	¥24,202,808.06
Xiangxi Jiaxi (TRE)	湘西嘉熙	¥30,925,793.41
		¥105,000,000.10

Other Account Receivable

Sino-Panel (TRE)	嘉汉板业	¥38,661,000.00
Guangxi Dacheng	广西大成	¥15,000,000.00
Xuwen Hengdong	徐闻恒东	¥7,610,000.00
Guangxi Bohu	广西博虎	¥3,200,000.00
Beihai Real Estate	北海房地产	¥27,813,100.00
Zhanjiang Tianxiang	湛江天翔	¥25,450,000.00
Zhanjiang Tianlun	湛江天伦	¥19,000,000.00
Leizhou Bangsheng	雷州邦盛	¥40,000,000.00
Leizhou Hengfu	雷州恒福	¥1,897,777.11
Other	其它	¥1,009,563.51
		¥179,641,440.62

Other Account Payable

Sino-Panel (China)	嘉汉板业（中国）	¥53,158,409.50
Sino-Panel (Sanjiang)	嘉汉板业（三江）	¥31,297,786.00
Sino-Panel (Luzhai)	嘉汉板业（鹿寨）	¥29,399,999.97
Sino-Panel (Hezhou)	嘉汉板业（贺州）	¥79,000,000.00
Huaihua Yuda	怀化裕达	¥134,900,000.00
Guangxi Bobai Forestry	广西博白林场	¥2.09
		¥327,756,197.56

From the above table, Bohu has made three prepayments to TRE's subsidiaries totaling RMB 105 million. This flow of funds contradicts the disclosed nature of the parties' relationship. Further, with such low registered capital and poor operating results, it is difficult to understand how Bohu's balance sheet is this large.

Bohu has an account payable of RMB 327.8 million to six companies. Four of the six companies are Sino-Panel Subsidiaries. The fifth company Huaihua Yuda is an undisclosed TRE subsidiary that has been receiving massive amounts of money from TRE's subsidiaries. The last company listed is Guangxi Bobai Forestry, which is supposed to be a partner forestry company in Guangxi; however, but the amount owed RMB 2.09 ($0.30) pales in comparison.

Jiangxi Zhonggan (an undisclosed related party) plays the same games. Its 2009 audit report shows that it had received a prepayment of RMB 448.6 million from Sino Panel China (Investment) Company Ltd. In the same year, it made a prepayment of RMB 212.0 million to Harbin Oubangde Economic and Trading Co. Ltd., a trading company in Harbin, whose business has nothing to do with acquiring forests in Jiangxi Province. According to the audit report, Jiangxi Zhonggang has dealt with more trading companies than forestry companies. (Appendix K3 and K4)

The same is true for Gengma Forestry (a mostly legitimate agent). Its revenue has been declining since it entered into the master agreement with TRE. The revenue was RMB 3.6 million in 2007, and declined to RMB 160,000 RMB in 2008 and RMB 455,400 in 2009. The assets and debts are 787 times 2008 revenue, and 266 times 2009 revenue. Although it really does broker forests, it appears to be helping TRE in some way beside acquiring forest.

TRE has a significant undisclosed subsidiary, Huaihua Yuda Wood Company Ltd. (怀化裕达木业有限公司). Huaihua Yuda has taken massive amount from TRE's subsidiaries, but its existence was never disclosed. In 2007, Huaihua Yuda received a prepayment of RMB 92.0 million from Sino Panel (Hezhou) and another payment of RMB 81.0 million from Sino Panel (Gengma). (Appendix K5 and K6) According to our research from two government websites, Huaihua Yuda is a subsidiary of TRE.

XII. The Multi-Billion Dollar Ponzi Scheme

Sino Forest to date has raised over $3.05 billion from the capital markets and has not paid a cent back from free cash flow, nor has it paid a dividend.

Sino-Forest raises capital in increasingly larger amounts, which is effectively a Ponzi scheme. TRE raises cash from the financial markets, purportedly buys forestry assets, which are then valued at a significantly higher level by Poyry (which takes TRE's word on the size and scope of the acquisition at face value), leading to a higher reported net asset value which acts as the support or collateral for an even larger capital raise. The first investor relies upon the new capital to generate the return, thereby fitting a classic Ponzi scheme definition.

It is a fairly standard capital markets transaction to complete a new financing of an asset that has increased in value. In isolation, this conceptually would not be a Ponzi scheme. However, a series of financings almost wholly reliant upon a series of unreliable reports covering the asset values of a company that has been free cash flow negative for 16 straight years should raise some red flags. In order to understand how this cycle has managed to continue for such a long period of time, it is important to understand two key issues: the manipulation of Jakko Poyry's valuation reports, and the way the TRE uses these reports to convince new investors to finance them.

With the exception of an incentive payment of $30 million to exchange an existing bond into a longer dated one, TRE has never returned any capital to shareholders despite so many financings. Because of the nature of the company, TRE must continue to spend in order to survive. Without an acquisition pipeline, TRE cannot justify raising capital from new investors. Without new investors, it cannot repay old investors, and would fall apart.

As expected, TRE is still talking about a large acquisition pipeline for 2011.

TAB 2

Court File No.: CV-12-9667-00CL

ONTARIO
SUPERIOR COURT OF JUSTICE
COMMERCIAL LIST

IN THE MATTER OF THE *COMPANIES' CREDITORS ARRANGEMENT ACT*, R.S.C. 1985, c.C-36, AS AMENDED

AND IN THE MATTER OF A PLAN OF COMPROMISE OR ARRANGEMENT OF SINO-FOREST CORPORATION

AFFIDAVIT OF DANIEL E. H. BACH

I, Daniel E. H. Bach, of the City of Toronto, in the Province of Ontario, MAKE OATH AND SAY:

1. I am a lawyer in the class actions department of Siskinds LLP ("Siskinds"), co-counsel for the plaintiffs (the "Plaintiffs") in the class proceeding styled *Trustees of the Labourers' Pension Fund of Central and Eastern Canada v Sino-Forest Corporation et al.*, bearing (Toronto) Court File No. CV-11-431153-00CP (the "Ontario Class Action").

2. As such, I have knowledge of the matters to which I hereinafter depose. Where that knowledge is based on information obtained from others, I have so indicated and believe that information to be true.

3. I swear this affidavit in support of the Plaintiffs' motion for an order, *inter alia*, terminating these proceedings under the *Companies' Creditors Arrangement Act* ("*CCAA*") and appointing a receiver of the assets, undertakings and properties of Sino-

Forest Corporation ("Sino"). No portion of this affidavit is meant to waive, nor should it be construed as a waiver of, solicitor-client, litigation or any other privilege.

CLASS ACTION LITIGATION INVOLVING SINO

The Ontario Class Action

Overview of the Ontario Class Action

4. On July 20, 2011, the Trustees of the Labourers' Pension Fund and the Trustees of the International Union of Operating Engineers commenced the Ontario Class Action by way of a notice of action. In addition to Sino, the action names 25 defendants, including Sino's former auditors, various underwriters and a forestry valuation company.

5. By way of a notice of action issued on November 14, 2011, Messers. Grant and Wong commenced an action (the "Grant-Wong Action"), arising out of the same facts, against Sino and certain of the other individual and corporate defendants.

6. On December 13, 2011, the plaintiffs in the Grant-Wong Action filed a statement of claim.

7. On January 6, 2012, the Honourable Justice Perell granted the Plaintiffs carriage of the Ontario Class Action, and consolidated the Ontario Class Action and the Grant-Wong Action.

8. On direction from court staff, the Plaintiffs filed an amended notice of action and a statement of claim on January 26, 2012 (the "Claim"). A copy of the Claim is attached and marked as Exhibit "Y" to the affidavit of Judson Martin, sworn March 30, 2012, which Sino has filed in this proceeding (the "Martin Affidavit").

9. Following the filing of the Claim on January 26, 2012, we undertook to Justice Perell, the case management judge assigned to the Ontario Class Action, to serve and file by no later than April 2, 2012 our clients' motions for certification (the "Certification Motion") under the *Class Proceedings Act, 1992* (the "*CPA*") and for leave to assert the statutory cause of action for secondary market misrepresentation (the "Leave Motion") under Part XXIII.1 of the Ontario *Securities Act* (the "*OSA*"). The Plaintiffs brought a motion seeking to have the Certification Motion and Leave Motions heard in late August 2012. This motion was scheduled for March 22, 2012.

10. However, on February 16, 2012, the Ontario Court of Appeal issued its decision in *Sharma v Timminco Limited*, 2012 ONCA 107 (CanLII). In that decision, the Court held, in essence, that the limitation period under Part XXIII.1 of the *OSA* was not tolled in that action by the filing of a pleading wherein the plaintiff declared an intention to seek leave to assert the Part XXIII.1 cause of action (as the Plaintiffs have done from the outset of the Ontario Class Action).

11. Immediately following the issuance of the *Timminco* decision, out of an abundance of caution, Dimitri Lascaris of Siskinds LLP wrote to counsel to those of the defendants in the Ontario Class Action against whom a Part XXIII.1 claim is sought to be asserted (the "Leave Defendants"), and requested that they enter into a tolling agreement, failing which the Plaintiffs would seek to have the Leave Motion heard on March 22, 2012.

12. On March 2, 2012, by which time none of the Leave Defendants had agreed to toll the Part XXIII.1 limitation period, we served upon counsel to the Leave Defendants the Plaintiffs' motion record in support of the Leave Motion. Pursuant to Part XXIII.1 of the *OSA*, a copy of that motion record was also served upon the Ontario Securities

Commission (the "OSC"). Attached and marked as **Exhibit "A"** is a disk containing an electronic copy of the motion record filed by the Plaintiffs in support of the Leave Motion.

13. On March 6, 2012, the Leave Defendants entered into a tolling agreement with the Plaintiffs. Pursuant to the tolling agreement, the parties agreed that the running of time for the purpose of asserting Part XXIII.1 claims was to be suspended as of March 6, 2012 until February 28, 2013. On that basis, the Plaintiffs agreed to postpone the hearing of the Leave Motion and Certification Motion until a date in the summer or fall of 2012 so that the defendants would have time to prepare responding materials and allow for full preparation.

14. The expiration date of February 28, 2013 was carefully crafted by the parties in the Ontario Class Action with the assistance of the Honourable Justice Perell in order for the Leave Motion to be prepared and heard, and for a decision to be rendered by him, before the expiration of the tolling agreement. As such, any interruption or delay to the timetable will have a pass-on effect, with the result being that the decision on the Leave Motion might not be released before February 28, 2013. This puts the Class Members at risk of having some or all of their claims extinguished as a result of the potential expiry of a limitation period.

15. In support of their Leave Motion, the Plaintiffs filed a proposed Fresh as Amended Statement of Claim (the "Amended Claim"). The Amended Claim, which will be filed with the Court in accordance with the reasons of Justice Perell, is different from the Claim. Among other things, the Amended Claim incorporates information revealed to the public for the first time by the special committee established by Sino's Board to

investigate the Muddy Waters allegations (the "SC"). It also incorporates information obtained through our own, ongoing, investigation and analysis, which was aided by various experts, and which was also aided by investigators based in Hong Kong. A copy of the Amended Claim is marked and attached as **Exhibit "B"**.

16. The Amended Claim alleges that Sino, certain of its officers and directors, its auditors, and its underwriters made material misrepresentations regarding the operations, revenues, net income and assets of Sino. The Claim seeks an aggregate of $9.2 billion in damages and is brought on behalf of:

> all persons and entities, wherever they may reside who acquired Sino-Forest's Securities during the Class Period by distribution in Canada or on the Toronto Stock Exchange or other secondary market in Canada, which includes securities acquired over-the-counter, and all persons and entities who acquired Sino-Forest's Securities during the Class Period who are resident of Canada or were resident of Canada at the time of acquisition and who acquired Sino's Securities outside of Canada, except the Excluded Persons (the "Class" or "Class Members")

17. The Amended Claim defines "Excluded Persons" as the Defendants, their past and present subsidiaries, affiliates, officers, directors, senior employees, partners, legal representatives, heirs, predecessors, successors and assigns, and any individual who is a member of the immediate family of an individual defendant.

18. The Amended Claim defines the Class Period as "the period from and including March 19, 2007 to and including June 2, 2011."

<u>The Evidence Supporting the Leave Motion</u>

19. The Part XXIII.1 cause of action which the Plaintiffs principally seek to assert is set forth in s. 138.3(1) of the *OSA*, which states in part:

138.3(1) Where a responsible issuer or a person or company with actual, implied or apparent authority to act on behalf of a responsible issuer releases a document that contains a misrepresentation, a person or company who acquires or disposes of the issuer's security during the period between the time when the document was released and the time when the misrepresentation contained in the document was publicly corrected has, without regard to whether the person or company relied on the misrepresentation, a right of action for damages against,

(a) the responsible issuer;

(b) each director of the responsible issuer at the time the document was released;

(c) each officer of the responsible issuer who authorized, permitted or acquiesced in the release of the document;

[...]

(e) each expert where,

(i) the misrepresentation is also contained in a report, statement or opinion made by the expert,

(ii) the document includes, summarizes or quotes from the report, statement or opinion of the expert, and

(iii) if the document was released by a person or company other than the expert, the expert consented in writing to the use of the report, statement or opinion in the document.

20. Under s. 138.8(1) of the *OSA*, an action may be commenced under Part XXIII.1 only with leave of the Court, which shall be granted if (1) the plaintiff is acting in good faith; and (2) there is a reasonable possibility that the action will be resolved at trial in favour of the plaintiff. Section 138.8 (2) of the *OSA* stipulates that, in an application for leave, the plaintiff and each defendant shall serve and file one or more affidavits setting forth the material facts upon which each intends to rely.

21. In support of the Leave Motion, the Plaintiffs have filed the following affidavits, all of which were served on counsel to Mr. Martin approximately four weeks before he swore the Martin Affidavit:

(a) One affidavit from each of the five plaintiffs;

(b) An affidavit sworn by me, to which is attached, among other things, a large number of Sino disclosure documents, and which also touches upon other matters, including Sino's historical results as compared to the results of its peers;

(c) An affidavit from Steven Chandler, a former senior law enforcement official from Hong Kong (the "Chandler Affidavit");

(d) An affidavit of Alan Mak, an expert in forensic accounting from the Toronto-based firm of Rosen & Associates;

(e) An affidavit of Dennis Deng, a lawyer qualified to practice in the PRC, and a partner in a law firm that is one of Beijing's leading law firms and is also one of China's largest law firms (the "Deng Affidavit"); and

(f) An affidavit of Carol-Ann Tjon-Pian-Gi, a lawyer qualified to practice in the Republic of Suriname (the "Tjon-Pian-Gi Affidavit").

22. Below I summarize the four affidavits on which the Plaintiffs principally rely to establish the merits of their proposed Part XXIII.1 claims.

The Chandler Affidavit

23. Among other things, Mr. Chandler examined various business records that had been filed with the Administration of Industry and Commerce of the PRC (the "AIC"), as well as certain filings with the Courts of Hong Kong. Based in part upon that examination, Mr. Chandler found, *inter alia*, that:

(a) A company from which Sino had claimed to have generated substantial sales was in fact a shell and never did any business from the time of its establishment;

(b) Neither Sino nor any of its subsidiaries appeared to have an interest in a Shanghai-based company of which Sino claimed to be part-owner;

(c) Sino failed to disclose that one of its officers was a major shareholder of a subsidiary of Homix Limited (a company discussed in the Martin Affidavit) at the time that Homix was acquired by Sino; and

(d) Contrary to statements made in the Final Report of the SC, maps are in fact allowed and have been widely used in the PRC for at least the last three years.

The Tjon-Pian-Gi Affidavit

24. Ms. Tjon-Pian-Gi opines on Sino's assertion that one of its subsidiaries, The Greenheart Group ("Greenheart"), was granted well in excess of 150,000 hectare of forestry concessions in the Republic of Suriname. Ms. Tjon-Pian-Gi's opinion undermines this assertion or, at a minimum, constitutes evidence that Greenheart's concessions may not be compliant with the laws of Suriname. In particular, the *Forest Management Act* of the Republic of Suriname prohibits a person or legal entity, or various legal entities in which a person or legal entity has a majority interest, from being granted more than 150,000 hectares of forestry concessions.

The Deng Affidavit

25. In essence, Mr. Deng opines, *inter alia*, that:

(a) It is unlawful in the PRC, and potentially punishable with severe criminal penalties, for forestry companies or their representatives to give gifts to employees of forestry bureaus (the SC disclosed that "there are indications in emails and in interviews with [Sino] Suppliers that gifts and cash payments are made to forestry bureaus and forestry bureau officials");

(b) Sino's BVI subsidiaries are likely engaging in "business activities" in the PRC in violation of PRC law, and the unauthorized conduct of "business activities" in the PRC is potentially punishable with severe penalties;

(c) It is likely that certain of Sino's authorized intermediaries and suppliers refused to produce requested documentation to the SC because that documentation may demonstrate that they were engaging in illegal tax evasion; and

(d) In the PRC, standing timber may not be purchased without purchasing land use rights, and because foreign forestry companies are not allowed to purchase land use rights, the standing timber purchase contracts entered into by Sino's BVI subsidiaries are void and unenforceable under PRC law.

The Mak Affidavit

26. Essentially, Mr. Mak opines, *inter alia*, that:

(a) From an accounting and financial reporting perspective, and based on publicly available information (including the SC's reports), sufficient appropriate evidence does not exist to justify Sino's reporting of timber assets and revenues for the vast majority of Sino's standing timber activities in 2006 to 2010;

(b) The annual audited financial statements of Sino for much or all of the period 2005-2010 should not have been issued to the public;

(c) The legal ownership and occurrence of *bona fide* economic transactions have not been established by Sino or by the investigation of the SC;

(d) Given the 'closed circuit' nature of Sino's standing timber business model, a serious possibility (if not high probability) is that Sino's entire standing timber business is an accounting fiction;

(e) Sino's timber assets, revenues and profits from at least 2006 to 2010 were grossly overstated;

(f) In direct contravention of Canadian GAAP, Sino grossly overstated its "cash flows from operating activities," a figure that is extensively relied upon by financial analysts to compute valuations of the company; and

(g) Ernst & Young and BDO failed to conduct their audits in accordance with Generally Accepted Auditing Standards, and failed to detect material misstatements in Sino's financial statements.

The Proposed Representative Plaintiffs in the Ontario Class Action

27. The trustees of the Labourer's Pension Fund of Central and Eastern Canada ("Labourers') are proposed representative plaintiffs in the Ontario Class Action. Labourers' is a multi-employer pension plan providing benefits for employees working in the construction industry. The fund is a union-negotiated, collectively-bargained defined benefit pension plan established on February 23, 1972 and currently has approximately $2 billion in

assets, over 39,000 members, over 13,000 pensioners and beneficiaries and approximately 2,000 participating employers. A board of trustees representing members of the plan governs the fund. The plan is registered under the *Pension Benefits Act*, RSO 1990, c P.8 and the *Income Tax Act*, RSC 1985, 5th Supp, c.1. Labourers' purchased Sino's common shares over the TSX during the Class Period and continued to hold shares at the end of the Class Period. In addition, Labourers purchased Sino's common shares pursuant to a prospectus and in the distribution to which that prospectus related.

28. The trustees of the International Union of Operating Engineers ("Operating Engineers") are proposed representative plaintiffs in this action. Operating Engineers is a multi-employer pension plan providing pension benefits for operating engineers in Ontario. The pension plan is a union-negotiated, collectively-bargained defined benefit pension plan established on November 1, 1973 and currently has approximately $1.5 billion in assets, over 9,000 members and pensioners and beneficiaries. The fund is governed by a board of trustees representing members of the plan. The plan is registered under the *Pension Benefits Act*, RSO 1990, c P.8 and the *Income Tax Act*, RSC 1985, 5th Supp, c.1. Operating Engineers purchased Sino's common shares over the TSX during the Class Period, and continued to hold shares at the end of the Class Period.

29. Sjunde AP-Fonden ("AP7") is the Swedish National Pension Fund. As of June 30, 2011, AP7 had approximately $15.3 billion in assets under management. Funds managed by AP7 purchased Sino's common shares over the TSX during the Class Period and continued to hold those common shares at the end of the Class Period.

30. David Grant is an individual resident in Calgary, Alberta. During the Class Period, he purchased 100 of the Sino 6.25% Guaranteed Senior Notes due 2017 pursuant to an

offering memorandum. Mr. Grant continued to hold those Notes at the end of the Class Period.

31. Robert Wong is an individual residing in Kincardine, Ontario. During the Class Period, he purchased Sino's common shares over the TSX and continued to hold some or all of such shares at the end of the Class Period. In addition, Mr. Wong purchased Sino common shares pursuant to a prospectus and continued to own those shares at the end of the Class Period.

32. Collectively, the Plaintiffs held in excess of 1.1 million Sino shares and 100 Sino notes at the end of the class period (on June 2, 2011).

<u>Other Class Members' Involvement in the Ontario Class Action.</u>

33. Our firm was recently retained by U.S.-based Davis Selected Advisors L.P ("Davis") in connection with, among other matters, the Ontario Class Action and this proceeding. Davis held approximately 31 Sino million shares, or 12.6% of Sino's outstanding shares, as of April 29, 2011, as well as various notes of Sino-Forest. I understand that that Davis is currently Sino's second largest shareholder.

34. Davis has instructed us to advise this Honourable Court that it completely supports the granting of the relief sought in this motion.

35. In addition, on April 10, 2012, I spoke to Richard Edlin of Greenberg Traurig, counsel to U.S.-based Paulson & Co. ("Paulson"). I understand that Paulson held approximately 34 million Sino shares, or 14.1% of Sino's outstanding shares, as of April 29, 2011, but that Paulson sold its Sino stake in June 2011, after publication of the initial Muddy Waters

report. Mr. Edlin advised me that Paulson completely supports the granting of the relief sought in this motion.

36. Finally as of April 11, 2012 Siskinds and Siskinds Desmeules had been contacted by 311 putative class members, and Koskie Minsky had been contacted by 204 putative class members.

The Defendants

37. Sino purports to be a commercial forest plantation operator in the People's Republic of China and elsewhere. Sino is a corporation formed under the *CBCA*. At material times relevant to the Ontario Class Action, Sino was a reporting issuer in all provinces of Canada, and had its registered office located in Mississauga, Ontario. At the material times, Sino's shares were listed for trading on the TSX under the ticker symbol "TRE," on the Berlin exchange as "SFJ GR," on the over-the-counter market in the United States as "SNOFF" and on the Tradegate market as "SFJ TH." Sino securities were also listed on alternative trading venues in Canada and elsewhere including, without limitation, AlphaToronto and PureTrading. Sino's shares also traded over-the-counter in the United States. Sino has various debt instruments, derivatives and other securities that are traded in Canada and elsewhere.

38. Allen Chan is a co-founder of Sino, and was the Chairman, Chief Executive Officer and a director of the company from 1994 until his resignation from those positions on or about August 25, 2011.

39. David Horsley is Sino's Chief Financial Officer, and has held this position since October 2005. Mr. Horsley resides in Ontario.

40. Kai Kit Poon is a co-founder of Sino, and has been the President of the company since 1994. He was a director of Sino from 1994 to May 2009, and he continues to serve as Sino's President. Mr. Poon resides in Hong Kong, China.

41. Peter Wang is a director of Sino, and has held this position since August 2007. Mr. Wang resides in Hong Kong, China.

42. Judson Martin has been a director of Sino since 2006, and was appointed vice-chairman in 2010. On or about August 25, 2011, Mr. Martin replaced Allen Chan as Chief Executive Officer of Sino. Mr. Martin was a member of Sino's audit committee prior to early 2011. He resides in Hong Kong, China.

43. Edmund Mak is a director of Sino and has held this position since 1994. Mr. Mak was a member of Sino's audit committee prior to early 2011. Mr. Mak resides in British Columbia.

44. Simon Murray is a director of Sino and has held this position since 1999. Mr. Murray resides in Hong Kong, China.

45. James M.E. Hyde is a director of Sino, and has held this position since 2004. Mr. Hyde was previously a partner of the defendant, Ernst & Young. He is the chairman of Sino's Audit Committee and a member of the Compensation and Nominating Committee. Mr. Hyde resides in Ontario.

46. William E. Ardell is a director of Sino, and has held this position since January 2010. Mr. Ardell is a member of Sino's audit committee. He resides in Ontario.

47. James P. Bowland was a director of Sino from February 2011 until his resignation from the Board of Sino in November 2011. While on Sino's Board, Mr. Bowland was a member of Sino's Audit Committee. He was formerly an employee of a predecessor to Ernst & Young. Mr. Bowland resides in Ontario.

48. Mr. Bowland was initially a member of the SC. However, on November 4, 2011, in the middle of the SC's investigation into the Muddy Waters allegations, Sino issued a press release announcing that Mr. Bowland had resigned as a director of Sino. No reasons were given in that press release for his resignation. Attached and marked as **Exhibit "C"** is a copy of the November 4, 2011 press release.

49. Garry J. West is a director of Sino, and has held this position since February 2011. Mr. West was previously a partner at the defendant, Ernst & Young. Mr. West is a member of Sino's Audit Committee. He resides in Ontario.

50. Ernst & Young was engaged as Sino's auditor from August 13, 2007 to April 4, 2012. Ernst & Young was also engaged as Sino's auditor from Sino's creation through February 19, 1999, when Ernst & Young resigned during audit season and was replaced by the now-defunct Arthur Andersen LLP. Ernst & Young was also Sino's auditor from 2000 to 2004, when it was replaced by BDO Limited.

51. BDO Limited is the successor of BDO McCabe Lo Limited, the Hong Kong, China based auditing firm that was engaged as Sino's auditor during the period of March 21, 2005 through August 12, 2007, when they resigned at Sino's request, and were replaced by Ernst & Young.

52. Pöyry (Beijing) Consulting Company Limited is an international forestry consulting firm which purported to provide certain forestry consultation services to Sino.

53. A number of underwriters are also named as defendants in the Amended Claim. These underwriters include Banc of America Corporation, Cannacord Financial Ltd., CIBC World Markets Inc., Credit Suisse Securities (Canada) Inc., Credit Suisse (USA) LLC, Dundee Securities Corp., Maison Placements Canada Inc., Merrill Lynch Canada Inc., RBC Dominion Securities Inc., Scotia Capital Inc., and TD Securities Inc.

54. The various defendants are represented in the Ontario Class Action by the following firms:

(a) Bennett Jones LLP – Sino, Edmund Mak, Simon Murray, Judson Martin, Kai Kit Poon, Peter Wang;

(b) Wardle Daley Bernstein LLP – David Horsley;

(c) Miller Thomson – Allen Chan;

(d) Osler, Hoskin & Harcourt LLP – William Ardell, James Bowland, James Hyde, Garry West;

(e) Lenczner Slaght Royce Smith Griffin LLP – Ernst & Young LLP;

(f) Affleck Greene McMurtry LLP – BDO Limited;

(g) Baker & Mckenzie LLP – Pöyry (Beijing) Consulting Company Limited; and

(h) Torys LLP – all Underwriters.

Other Class Proceedings

Parallel Ontario Actions

55. On June 6, 2011, the law firm of Rochon Genova LLP commenced an action (the "Smith Action") against Sino and certain other defendants arising out of the same set of allegations as those advanced in this action.

56. On September 26, 2011, the law firm of Kim Orr Barristers commenced an action (the "Northwest Action") against Sino and certain other defendants arising out of the same set of allegations as those advanced in this action.

57. By an order dated January 6, 2012, Justice Perell stayed the Smith Action and the Northwest Action, and carriage of the action was granted to the Plaintiffs. A copy of those reasons are marked and attached as **Exhibit "D"**.

Parallel Quebec Action

58. On June 9, 2011, Siskinds Desmeules, a Quebec City law firm affiliated with Siskinds, filed a petition for an order authorizing the bringing of a class action and granting the status of representative in the Quebec Superior Court (the "Quebec Proceeding"). The petition in the Quebec Proceeding defines the proposed Class as:

> all persons or entities domiciled in Quebec (other than the Defendants, their past and present subsidiaries, affiliates, officers, directors, senior employees, partners, legal representatives, heirs, predecessors, successors and assigns, and any individual who is an immediate member of the families of the individual named defendants) who purchased or otherwise acquired, whether in the secondary market, or under a prospectus or other offering document in the primary market, equity, debt or other securities of or relating to Sino-Forest Corporation, from and including March 19, 2007 to and including June 2, 2011.

59. I am advised by Simon Hebert, the lawyer at Siskinds Desmeules with carriage of the Quebec Proceeding, that he anticipates that, prior to the hearing of the Quebec Proceeding, the class definition will be revised so that it is limited to Quebec residents eligible to participate in a class proceeding under the Quebec *Code of Civil Procedure*, which expressly excludes entities employing more than 50 persons from participating in a class proceeding.

60. By virtue of our relationship with Siskinds Desmeules, we believe we can coordinate the progress of the Quebec Proceeding and the Ontario Class Action in a complimentary and efficient manner.

Parallel United States Action

61. On January 27, 2012, the Washington, DC-based law firm of Cohen Milstein Sellers & Toll PLLC commenced a proposed class action against Sino and certain other defendants in the New York Supreme Court (the "U.S. Action"). The U.S. Action defines the proposed class as:

> (i) all persons or entities who, from March 19, 2007 through August 26, 2011 (the "Class Period") purchased the common stock of Sino-Forest on the Over-the-Counter ("OTC") market and who were damaged thereby; and (ii) all persons or entities who, during the Class Period, purchased debt securities issued by Sino-Forest other than in Canada and who were damaged thereby.

62. I am not aware of any material steps having been taken by the plaintiff in the U.S. Action to advance that action.

63. To my knowledge, Sino has no offices or operations in the United States.

Parallel Saskatchewan Action

64. On December 1, 2011 the Merchant Law Group LLP commenced a proposed class action against Sino and certain other defendants in the Saskatchewan Court of Queen's Bench styled as *Haigh v Sino-Forest Corporation* (the "Saskatchewan Action"). The proposed class in the Saskatchewan Action is defined as:

> All persons and entities wherever they may reside who acquired securities of Sino during the Class Period either by primary distribution in Canada or an acquisition on the TSX or other secondary market in Canada, other than the Defendants, their past and present subsidiaries, affiliates, officers, directors, senior employees, partners, legal representatives, heirs, predecessors, successors and assigns, and any individual who is an immediate family member of an Individual Defendant.

65. I am not aware of any material steps having been taken by the plaintiff in the Saskatchewan Action to advance that action.

66. To my knowledge, Sino has no offices or operations in the Province of Saskatchewan.

67. I am not aware of any other civil actions having been commenced in Canada or elsewhere against any of the Defendants in relation to the facts pleaded in the Claim.

The Status of the Ontario Class Action

Motions Relating to the Ontario Class Action

68. There are currently four motions scheduled to be heard in the Ontario Class Action. These are:

(a) The Plaintiffs' motion for certification for the purpose of settlement only as against the defendant, Pöyry (Beijing) Consulting Company Limited ("Pöyry"). The Plaintiffs have reached a settlement with Pöyry, and the motion for certification is brought on consent. The motion is scheduled to be heard on April 17, 2012. In order for this settlement to be effected, it will also have to be approved by way of motion by the Quebec Superior Court. Attached and marked as **Exhibit "E"** is a disk containing an electronic copy of the motion record filed by the plaintiffs in support of the motion for certification for the purpose of settlement. .

(b) The Plaintiffs' motion for approval of a litigation funding agreement reached between the Plaintiffs and Claims Funding International, PLC ("CFI"). In the motion, the Plaintiffs also seek an order that all communications between CFI, class counsel and the Plaintiffs are confidential, that CFI provide security for costs, and that class counsel and the Plaintiffs may provide documents to CFI on the condition that CFI and its staff are subject to the deemed undertaking pursuant to Rule 30.1.03 of the *Rules of Civil Procedure*. The motion is also scheduled to be heard on April 17, 2012. Attached and marked as **Exhibit "F"** is a disk containing an electronic copy of the motion record filed by the plaintiffs in support of the litigation funding motion.

(c) The Leave Motion and the Certification Motion, the latter of which was served on the defendants on April 2, 2012. These motions are scheduled to be heard from November 21 to 30, 2012.

<u>Timetable of Pending Motions</u>

69. On March 22, 2012, the Honourable Justice Perell heard a contested motion regarding the date on which the Leave and Certification Motions would be heard. All of the defendants

made submissions and opposed the scheduling of the certification motion for November 2012.

70. In reasons dated March 26, 2012, the Honourable Justice Perell ordered that any Leave Defendant who elects to file an affidavit in opposition to the Leave Motion would be required to serve a Statement of Defence. The defendants in the Ontario Class Action had opposed an order requiring them to serve a defence before adjudication of the Leave and Certification Motions.

71. In his March 26, 2012 reasons, Justice Perell also set a timetable for the Plaintiffs' motion for funding approval, Leave Motion, and Certification Motion. The reasons for decision are marked and attached as **Exhibit "G"**.

72. The timetable, as set out at paragraph 93 of those reasons, is as follows:

<u>Funding Approval Motion</u>

March 9, 2012: Plaintiffs to deliver motion record (completed)

March 30, 2012: Defendants to deliver responding records, if any

April 6, 2012: Plaintiffs to deliver factum

April 13, 2012: Defendants to deliver factum

April 17, 2012: Hearing of the motion

<u>Leave and Certification Motion</u>

April 10, 2012: Plaintiffs to deliver motion record

June 11, 2012: Defendants to deliver responding records

July 3, 2012: Plaintiffs to deliver reply records, if any

September 14, 2012: Cross-examinations to be completed

October 19, 2012: Plaintiffs to deliver factum

November 9, 2012: Defendants to deliver factum

November 21-30, 2012: Hearing of the motion

Osler's Dual Roles in the SC's Investigation and in the Ontario Class Action

73. Osler, Hoskin & Harcourt LLP ("Osler") is counsel to the defendants William Ardell, James Bowland, James Hyde, and Garry West in the Ontario Class Action. Each of these individuals was a director of Sino during the Class Period.

74. On June 3, 2011, Sino-Forest issued a press release announcing the creation of the SC, which initially consisted of the defendants, William Ardell, James Bowland, and James Hyde. The mandate of the SC was said to be to "thoroughly examine and review the allegations contained in Muddy Waters' report". The SC appointed Osler as its legal counsel. A copy of the June 3, 2011 press release is marked and attached as **Exhibit "H"**.

75. On January 31, 2012, the SC released its final report to Sino's board of directors. The SC concluded that although there remain outstanding issues that have not been fully answered, the SC had reached the point of diminishing returns. Attached and marked as **Exhibit "I"** is a copy of the final report.

76. In an article dated February 13, 2012, William Ardell disclosed that Sino had then spent approximately $50 million on its internal investigation. Attached and marked as **Exhibit "J"** is a copy of that article.

Sino's Performance from its Listing on the TSX to 2012

77. From 1994, when Sino became a TSX-listed company, to 2010, Sino's reported annual revenues increased from US$20.5 million to US$1.9 billion, or 9,291%, and its year-over-year reported revenues decreased only once, in 2000. During that same period, Sino's reported net income increased from US$3.0 million to US$395.4 million, or

13,037%, and its year-over-year reported net annual income decreased only twice, in 2000 and 2001. Finally, from 1994 to 2010, Sino's reported total assets as at year-end increased from US$30.6 million to US$5.7 billion, or 18,616%. During that period, Sino's year-over-year reported assets never decreased.

78. For none of the sixty quarters compromising the years 1996 to 2010 did Sino report a net loss; rather, for 100% of all such quarters, Sino reported significant net income.

79. From the commencement of 1996 to the current time, Sino's first and only quarter in respect of which it reported a net loss was for the quarter ended March 31, 2011. For that quarter, Sino reported a net loss of $22.1 million on revenue of $338.9 million. However, for the subsequent quarter ended June 30, 2011, Sino reported a net profit of $447.1 million on revenue of $317.4 million.[1]

80. According to Sino's audited annual financial statements for the year ended December 31, 2010, Sino's revenues and net income for each of 2008, 2009 and 2010 were as follows:

Year	**Revenue**	**Net Income**
2008	$901,295,000	$228,593,000
2009	$1,238,185,000	$286,370,000
2010	$1,923,536,000	$395,426,000
TOTAL	$4,063,016,000	$910,389,000

81. Thus, for the period commencing on January 1, 2008 and ending on June 30, 2011, Sino reported total revenues of approximately $4.7 billion and total net income of approximately $1.3 billion.

1 Sino has filed no interim or annual financial statements on SEDAR for periods ending after June 30, 2011.

CLAIMS AGAINST THE MEMBERS OF SINO'S BOARD AND CERTAIN MEMBERS OF SINO'S MANAGEMENT

82. The following chart sets out the claims being asserted in the Ontario Class Action against the members of Sino's Board and certain members of Sino's senior management:

	OSA s. 130 (prospectus)	OSA s. 138.3 (offering memorandum)	Negligent Misrepresentation (secondary market)	Negligent Misrepresentation (prospectus/offering memo)	Negligence	Unjust Enrichment	CBCA Oppression	Conspiracy
Chan	X	X	X	X	X	X	X	X
Horsley	X	X	X	X	X	X	X	X
Poon	X	X	X	X	X	X	X	X
Wang	X	X	X	X	X		X	
Martin	X	X	X	X	X	X	X	
Mak	X	X	X	X	X	X	X	
Murray	X	X	X	X	X	X	X	
Hyde	X	X	X	X	X		X	
Ardell		X	X				X	
Bowland		X	X				X	
West		X	X				X	

Resignation of Sino-Forest's Auditor

83. On April 5, 2012, Sino issued a press release announcing that Ernst & Young had resigned as the company's auditors effective April 4, 2012. In its resignation letter to Sino, Ernst & Young noted that the company had not prepared December 31, 2011 consolidated financial statements for that audit. It also noted that in Sino's March 30, 2012 filing under the *CCAA*, Sino said that it remained unable to satisfactorily address outstanding issues in relation to its 2011 annual financial statements. Attached and marked as **Exhibit "K"** is a copy of the April 5, 2012 press release.

Actions of the Ontario Securities Commission Relating to Sino-Forest

84. On June 8, 2011 Sino announced that the OSC had commenced an investigation into the company. A copy of the June 8, 2011 press release is marked and attached as **Exhibit "L"**.

85. On August 26, 2011, the OSC issued temporary cease trade order against Sino's securities and in respect of certain members of Sino's management, including the defendant Allen Chan. In recitals to the temporary cease-trade order, the OSC stated that "Sino-Forest, through its subsidiaries, appears to have engaged in significant non-arm's length transactions which may have been contrary to Ontario securities law and the public interest", that "Sino-Forest and certain of its officers and directors appear to have misrepresented some of its revenue and/or exaggerated some of its timber holdings by providing information to the public in documents required to be filed or furnished under Ontario securities laws and which may have been false or misleading in a material respect contrary to section 122 or 126.2 of the [Ontario Securities] Act and contrary to the public

interest" and that "Sino-Forest and certain of its officers and directors including Chan appear to be engaging or participating in acts, practices, or a course of conduct related to its securities which it and/or they know or reasonably ought to know perpetuate a fraud on any person or company contrary to section 126.1 of the Act and contrary to the public interest." Attached and marked as **Exhibit "M"** is a copy of the OSC temporary cease trade order.

86. The temporary cease trade order made on August 26, 2011 was later extended and continues in force. On April 5, 2012, Sino received an Enforcement Notice from the OSC staff. Enforcement Notices were also received that day by Allen Chan, David Horsley, Alfred Hung, and George Ho, among others.

87. The Enforcement Notice against Sino alleges conduct contrary to ss.122 and 126.1 of the OSA. Section 126.1 prohibits activities resulting in an artificial price of a security, or which perpetuate a fraud on any person or company. Section 122 provides for a quasi-criminal offence and penalties on conviction of up to $5 million and imprisonment for a term of up to five years less a day.

88. Enforcement Notices are notices issued by OSC staff that usually identify issues revealed in an investigation, and advise that staff intend to commence a formal proceeding relating to those issues. Recipients of the notices are given the opportunity to make submissions before OSC staff make a final decision to commence formal proceedings.

89. I have reviewed the website of the OSC. It states that the OSC pursues cases in court under s. 122 "in order to seek sanctions and penalties that send a strong message of deterrence to those who try to exploit investors."

90. According to Sino's website, which I viewed on April 11, 2012:

(a) Allen Chan currently holds the position of Founding Chairman Emeritus;

(b) David Horsley currently holds the position of Senior Vice President and Chief Financial Officer;

(c) Alfred Hung currently holds the position of Vice President, Corporate Planning and Banking; and

(d) George Ho currently holds the position of Vice President, Finance (China).

Attached and marked as **Exhibit "N"** is a printout from Sino's website which describes these individuals and their positions.

MEDIA COVERAGE OF SINO-FOREST'S CCAA PROCEEDING

91. Attached and marked as **Exhibit "O"** is an article recently published by Reuters regarding Sino's CCAA proceeding.

THE DEFENDANTS' ABILITY TO PAY

92. The Plaintiffs understand that, given the financial position of Sino and the serious doubts as to the legitimacy of its business and, in particular, as to its title to its claimed assets, they are unlikely to obtain any significant recovery from Sino.

93. It appears, however, that all of the remaining defendants (with the possible exception of Pöyry) have the ability to pay significant damages arising out of the Ontario Class Action.

94. The objective of our clients, including Davis, is to pursue their claims against the individual defendants, the underwriter and Sino's former auditors.

Directors and Officers

95. According to Sino's proxy circular of May 30, 2011 (the last proxy circular that Sino filed on SEDAR):

> In 2010, the Corporation purchased, at its expense, directors' and officers' liability insurance in the aggregate amount of $60,000,000 for the protection of its directors and officers against liability incurred by them in their capacities as directors and officers of the Corporation and its subsidiaries. For the financial year ended December 31, 2010, the Corporation paid a premium of $230,823 (inclusive of applicable taxes) in respect of such insurance.

Auditors and Underwriters

96. The defendants, other than Sino and its directors and officers, are, or are controlled by, large business organizations each having hundreds of millions to billions of dollars in annual revenues:

(a) Ernst & Young reported US$22.9 billion in global revenue for the year ended June 30, 2011. Attached and marked as **Exhibit "P"** is a copy of Ernst & Young's Global Review 2011.

(b) Banc of America Corporation and Merrill Lynch Canada Inc are wholly owned subsidiaries of Bank of America Corporation. In 2011, Bank of America reported revenue of US$94.4 billion and net income (excluding goodwill impairment charges) of US$4.6 billion. Attached and marked as **Exhibit "Q"** is an excerpt from Bank of America's 2011 annual report.

(c) Canaccord Financial Ltd. (now Canaccord Genuity) is a subsidiary of Canaccord Financial Inc. In 2011, Canaccord Financial Inc. reported revenue of CAD$803 million and net income of CAD$98 million. Attached and marked as **Exhibit "R"** is an excerpt from Canaccord Financial Inc.'s 2011 annual report.

(d) CIBC World Markets Inc. is a subsidiary of CIBC. In 2011, CIBC reported revenue of CAD$12.25 billion and net income of CAD$3 billion. Attached and marked as **Exhibit "S"** is an excerpt from CIBC's 2011 annual report.

(e) Credit Suisse Securities (Canada) Inc. and Credit Suisse (USA) LLC are subsidiaries of Credit Suisse Group. In 2011, Credit Suisse Group reported revenue of CHF26.2 billion and net income of CHF 2.79 billion. One CHF is equal to approximately CAD 1.088. Attached and marked as **Exhibit "T"** is an excerpt from Credit Suisse Group's 2011 annual report.

(f) Dundee Securities Corp. (now DWM Securities Inc.) is a subsidiary of DundeeWealth Inc. On March 9, 2011, DundeeWealth Inc. became a wholly owned subsidiary of ScotiaBank. In 2010, DundeeWealth Inc. reported revenue of CAD$1.04 billion and net income of CAD$118.7 million. Attached and marked as **Exhibit "U"** is an excerpt from DundeeWealth Inc.'s 2010 financial statements.

(g) RBC Dominion Securities Inc. is a principal subsidiary of the Royal Bank of Canada. In 2011, the Royal Bank of Canada reported revenue of CAD$27.4 billion and net income of CAD$4.8 billion. Attached and marked as **Exhibit "V"** is an excerpt from Royal Bank of Canada's 2011 annual report.

(h) Scotia Capital Inc. is a principal subsidiary of Scotia Bank. In 2011, ScotiaBank reported revenue of CAD$17.3 billion and net income of CAD$5.26 billion. Attached and marked as **Exhibit "W"** is an excerpt from ScotiaBank's 2011 annual report.

(i) TD Securities Inc. is a principal subsidiary of the Toronto-Dominion Bank. In 2011, Toronto-Dominion Bank reported revenue of CAD$21.5 billion and net income of CAD$5.9 billion. Attached and marked as **Exhibit "X"** is an excerpt from Toronto-Dominion Bank's 2011 financial statements.

97. Attached and marked as **Exhibit "Y"** is a chart that sets out the claims against each of the defendants in the Ontario Class Action other than the individual defendants.

Pöyry

98. As indicated above, the plaintiffs have entered into a settlement agreement with Pöyry, which is to be reviewed by Justice Perell on April 17, 2012. The settlement agreement essentially provides that Pöyry will provide information and cooperation to the plaintiffs for the purposes of prosecuting the Ontario Class Action against the remaining defendants.

99. In exchange for information and cooperation, there would be a release of claims against Pöyry and a bar order preventing claims for contribution, indemnity and other claims over in respect of the released claims. If it is later determined that the non-settling defendants have such rights of contribution, indemnity, or claim over against Pöyry, then the class members would not be entitled to claim or recover from the non-settling

defendants the proportion of any judgment that the Ontario court would have apportioned to Pöyry.

100. The settlement agreement provides that the parties shall consent to certification for the purpose of settlement and that Pöyry will pay the first $100,000 of the costs of providing notice of certification and fairness hearing and half of any such costs over $100,000. A copy of the settlement agreement is marked and attached as **Exhibit "Z"**

Compensation and Proceeds of Stock Sales of Certain Individual Defendants

101. Over the course of their involvement with Sino, the defendants Allen Chan, Kai Kit Poon, and David Horsley received substantial compensation from Sino. The following information regarding these defendants' salary and bonus from Sino was compiled from the Management Information Circulars from 2007 to 2010, which are marked and attached as **Exhibits "AA"** to **"DD"**. Information regarding the net proceeds of these defendants' sale of Sino's securities was compiled from insider transaction detail reports retrieved from the System for Electronic Disclosure by Insiders ("SEDI"), which are marked and attached as **Exhibits "EE"** to **"GG"**

102. According to these documents, Allen Chan received

(a) $1,047,947 in net proceeds from his sale of Sino securities; and

(b) $22,698,775 in salary and bonuses between 2007 and 2010.

103. According to these documents, Kai Kit Poon received

(a) $48,522,642 in net proceeds from his sale of Sino securities; and

(b) $3,021,162 in salary and bonuses between 2007 and 2010

104. According to these documents, David Horsley received

(a) $5,842,303 in net proceeds from his sale of Sino securities; and

(b) $7,568,487 in salary and bonuses between 2007 and 2010.

SWORN before me at the City of Toronto, in the Province of Ontario, this 11th day of April, 2012.	
A Commissioner, etc. Serge Kalloghlian (LSUC #55557F)	Daniel E. H. Bach

TAB 3

FOR IMMEDIATE RELEASE

SINO-FOREST COMMENTS ON SHARE PRICE DECLINE

TORONTO, CANADA, June 3, 2011 – Sino-Forest Corporation (TSX: TRE) ("Sino-Forest" or the "Company"), a leading commercial forest plantation operator in China, today commented on the share price decline on June 2, 2011 as a result of the allegations made in a 'report' issued on a website by a short seller operating under the name Muddy Waters, LLC. The Company was not contacted by Muddy Waters for comment ahead of publication of its report.

The Board of Directors and management of Sino-Forest wish to state clearly that there is no material change in its business or inaccuracy contained in its corporate reports and filings that needs to be brought to the attention of the market. Further we recommend shareholders take extreme caution in responding to the Muddy Waters report.

As indicated in the report, Muddy Waters has a short position in the Company's shares and therefore stands to realize significant gains from a share price decline that it precipitated. Muddy Waters expressly admits that it makes no representation as to the accuracy, timeliness, or completeness of any information contained in its report. Further, its website discloses no address or ownership information, nor the credentials of any of the authors of the 'report'. Neither the Ontario Securities Commission nor the Securities Exchange Commission website lists Muddy Waters or its author as being registered as an advisor. Nevertheless, due to the substantial impact that the report has had on the prices of the Company's securities and the reputation of the Company, the Board has appointed an independent committee consisting of three of the Company's independent directors, William Ardell (Chair), James Bowland and James Hyde. All three of these directors are financially qualified professionals and two of the three are recent appointees to the Board. The independent committee's mandate is to thoroughly examine and review the allegations contained in Muddy Waters' report, and report back to the Board. The independent committee has appointed Osler Hoskin & Harcourt LLP as independent legal counsel and will retain the services of an independent accounting firm and such other independent advisors as it deems necessary to assist with its examination. During the course of the independent committee's examination, the Company will provide any updates as appropriate. Following conclusion of the report, the key findings of the independent committee will be released to shareholders.

Allen Chan, Chairman and CEO of Sino-Forest commented: "We are committed to a high level of corporate governance and stand by the integrity of our company, our 16-year operational track record and our financial statements. Our company has continuously retained the services of internationally recognized law firms, auditors and expert consultants from Canada, the US, Hong Kong and mainland China."

"It is important that our independent committee thoroughly address Muddy Waters' allegations, and they will have my full support and those of the management team in doing so. However, let me say clearly that the allegations contained in this report are inaccurate and unfounded. Muddy Waters' shock-jock approach is transparently self-interested and we look forward to providing our investors and other stakeholders with additional information to rebut these allegations."

David Horsley, Senior Vice President and CFO of Sino-Forest commented: "I am confident that the independent committee's examination will find these allegations to be demonstrably wrong, as for example:

(a) Muddy Waters fundamentally misunderstands and misrepresents the most basic items in our published Management's Discussion & Analysis with respect to revenue generated from Yunnan Province, which we report as being approximately 45.5% of the Company's standing timber revenue of approximately US$508 million. Muddy Waters alleges that it is impossible that such revenue existed because achieving such levels would greatly exceed allowable cutting quotas and it would be impossible to truck close to that volume in the period. However, that revenue was very clearly disclosed in our MD&A filed for Q1 and Q2 of 2010 as revenue resulting from the sale of the standing timber - there is no cutting or transport involved, as the trees were sold but not harvested and therefore are not considered part of the quota for the region until the harvesting is conducted by the buyers.

(b) Muddy Waters alleges that the Company overstated the assets in Yunnan Province, based on its erroneous and narrow assumption that our only purchases in Yunnan Province consisted of purchases of 20,574 ha of plantations in Gengma county in Yunnan. However, this allegation ignores the fact that in addition to the purchased plantations in Gengma county, (as disclosed in our 2010 annual MD&A of a total of approximately 193,000 ha purchased in Yunnan Province) we have purchased approximately 173,000 ha of plantations in approximately 25 other counties in Yunnan Province as of December 31, 2010."

As at December 31, 2010, the Company had approximately US$1.26 billion in cash, cash equivalents and short term deposits as reported in the audited consolidated balance sheet. As at March 31, 2011, the comparable amount was approximately US$1.09 billion. The Company continues to hold such cash, with the majority of it in banks in Hong Kong and offshore.

As previously announced, the Company intends to file its Q1 2011 results on June 14, 2011.

About Sino-Forest Corporation

Sino-Forest Corporation is a leading commercial forest plantation operator in China. Its principal businesses include the ownership and management of tree plantations, the sale of standing timber and wood logs, and the complementary manufacturing of downstream engineered-wood products. Sino-Forest also holds a majority interest in Greenheart Group Limited, a Hong Kong-listed investment holding company (HKSE: 00094) with operations based in Suriname, South America and New Zealand, which is involved in responsible and sustainable log harvesting, lumber processing and sales and marketing of logs and lumber products to China and other countries around the world. Sino-Forest's common shares have been listed on the Toronto Stock Exchange under the symbol TRE since 1995. Learn more at www.sinoforest.com.

FOR FURTHER INFORMATION PLEASE CONTACT:

SINO-FOREST CORPORATION
Dave Horsley
- Senior Vice President & Chief Financial Officer
Tel: +905 281 8889
Email: davehorsley@sinoforest.com

Please note: This press release contains projections and forward-looking statements regarding future events. Such forward-looking statements are not guarantees of future performance of the Company and are subject to risks and uncertainties that could cause actual results and company plans and objectives to differ materially from those expressed in the forward-looking statements. Such risks and uncertainties include, but are not limited to: changes in China's and international economies and in currency exchange rates; changes in market supply and demand for the Company's products, including global production capacity and wood product imports into China; changes in China's political and forestry policies; changes in climatic conditions affecting the growth of the Company's trees; competitive pricing pressures for the Company's products; and changes in wood acquisition and operating costs.

TAB 4

REDACTED VERSION FOR PUBLIC RELEASE

SECOND INTERIM REPORT OF THE INDEPENDENT COMMITTEE OF THE BOARD OF DIRECTORS OF SINO-FOREST CORPORATION

November 13, 2011

TABLE OF CONTENTS
(continued)

TABLE OF CONTENTS
(continued)

I. EXECUTIVE SUMMARY

I. EXECUTIVE SUMMARY

A. Introduction

The IC was established by the Board on June 2, 2011, immediately following the release by Muddy Waters of the MW Report regarding SF. The members of the IC are William Ardell (Chair), James Bowland, and James Hyde. At the invitation of the IC, Mr. Garry West, an independent director of SF, attends virtually all IC meetings and participates in its process. Following the delivery to the Board of the IC's draft of this Second Interim Report on November 3, 2011, Mr. James Bowland resigned as a director and therefore from the IC. The mandate of the IC, in general terms, is to independently examine and review the serious and wide-ranging allegations made in the MW Report and report back to and, if appropriate, make recommendations to the Board. To date, the IC has met approximately 48 times.

The IC Advisors' role is to support the IC in its mandate to review the allegations made in the MW Report and related matters. The IC Advisors have conducted various investigative and review processes, all at the direction of, and subject to such scope limitations as the IC, in its judgment, deemed appropriate. (See Part IV.) This Second Interim Report to the Board, while based on the work of such advisors, is the report of the IC and (other than Schedule IV) not the report of the IC Advisors.

The IC's First Interim Report to the Board dated August 10, 2011 outlined the nature and scope of the IC's activities (principally data collection) to that date and the planned next steps. The purpose of this Second Interim Report is to report to the Board on the activities undertaken by the IC since mid-August, the outcomes and findings from such activities and further next steps. The First Interim Report is attached as Schedule I.A.

While the MW Report took a scatter gun approach in its allegations, the IC determined to address the issues raised in three core areas: (i) timber asset verification; (ii) timber asset value; and (iii) revenue recognition. Overlaying the latter two areas are the issues raised by the MW allegations relating to related party transactions. The IC also determined to focus on the years 2006 to 2010. Using this framework for its review, the IC's focus since its last report has been principally on:

- the ownership structure of timber assets on SF's balance sheet;
- verifying the Company's holdings of standing timber ("purchased plantations" as referred to in the 2010 AIF) and plantation land use/lease rights ("planted plantations" as referred to in the 2010 AIF, though some plantation land use/lease rights, such as the Mandra holdings, are classified as "purchased plantations" in the 2010 AIF), held through BVIs and WFOEs and the nature of its interests in such assets (see Part V below);
- interviewing Suppliers and AIs with a view to verifying the existence and nature of SF's relationship with such third parties and seeking to obtain financial particulars about purchase and sale transactions between such third parties and SF (see Part VI below); and

- examining and assessing the relationship with Yuda Wood, historically one of the largest Suppliers of standing timber to SF supplying approximately 21.5% of BVI timber purchases from 2008 through 2011 (see Section VI.A below).

The IC's work has also included:

- examining a number of specific situations which are the subject of MW allegations or critical newspaper articles (see e.g. Sections IV.B.6, VI.B and VI.C and Part VII below);

- engaging with and assisting E&Y in its examination of various issues relevant to its reports on the Company's financial statements (see Schedule IV attached);

- responding to questions and requests for documents and information from the OSC, including enquiries made through the Hong Kong securities authorities, in connection with its publicly announced investigation (see Part IX below);

- meeting with and responding to requests for information from BJ and FTI;

- conducting interviews of certain members of Management;

- inspecting original versions of documents issued to the WFOEs and BVIs on letterheads with forestry bureau names and featuring Chops (the seal typically used in place of signatures) that indicate that they had been issued by the corresponding forestry bureau (the "**forestry bureau confirmations**"), and attending meetings with forestry bureaus in an attempt to verify the Company's holdings of standing timber;

- attending interviews of AIs and Suppliers, examining SF employee and other relationships with AIs and Suppliers (see Schedule IV attached); and

- meeting with and responding to requests for information from the RCMP (see Part XI).

In addition to the IC review, the MW Report has spawned various actions by public and private parties. These actions, which have affected the IC's activities and processes, include:

- an OSC investigation of matters related to SF;

- a review by E&Y of various matters relating to its 2010 and prior years' audits;

- three class action lawsuits in Ontario (one of which has a companion action in Quebec) by securities holders against the Company, its officers, E&Y and others;

- a threatened derivative claim against E&Y and certain officers and employees of the Company;

- extensive newspaper and analyst reporting of the Company, including several in-depth investigative reports; and

- an enquiry by the RCMP through IMET.

While the IC believes its work is substantially complete, there remain certain further steps which it intends to undertake as follows:

- review the information and analysis very recently provided by Management intended to respond to certain issues regarding relationships of the Company with AIs and Suppliers and between AIs and Suppliers identified in this Second Interim Report (see Part VI);

- engage an independent valuator (see Part VIII);

- such other steps as the IC, in its judgement, deems advisable in the discharge of its mandate; and

- submit its final report and recommendations to the Board.

The IC expects to be able to deliver its final report to the Board prior to the end of 2011.

B. Overview of Principal Findings

The following sets out a very high level overview of the IC's principal findings and should be read in conjunction with the balance of this report.

Timber Ownership

Based on its review and subject to its comments herein, the IC has confirmed to its satisfaction that the Company has:

- registered title to approximately 151,000 Ha. of SW and SP planted plantations and Mandra plantations. This constitutes approximately 17.9% of its timber holdings by area as at December 31, 2010;[1] and

- contractual or other rights to approximately 683,000 Ha. of plantations, being 81.3% of its timber holdings by area as at December 31, 2010 (of these, the Company holds original Plantation Rights Certificates, issued in the name of the Supplier, representing approximately 15,000 Ha., which the IC believes gives the Company a demonstrable chain of title). See Section III.B.

In connection with such confirmation, the IC has reviewed originals or copies of purchase contracts (and the corresponding set-off documentation confirming payment, in the case of the BVI purchased plantations) for the acquisition by the Company of:

- approximately 467,000 Ha. of BVIs purchased plantations;[2]

- approximately 237,000 Ha. of WFOE purchased plantations;[3] and

- approximately 129,000 Ha. of planted plantations[4]

representing approximately 106%[5] of SF's disclosed timber holdings of 788,700 Ha. as at December 31, 2010. With respect to these holdings, the IC has verified to its satisfaction that the Company has registered title:

---

1 Timber holdings by area as at December 31, 2010 have been calculated by adding approximately 51,000 Ha. of planted plantation land for which the Company has contracts but has yet to classify as plantations under management for the purposes of its annual disclosure, to the Company's disclosed plantation holdings in China of 788,700 Ha.

2 BVI purchased plantations are comprised of standing timber without underlying leases of land use rights.

3 The Company classifies this as being comprised of all WFOE (SP) standing timber and all Mandra leased plantations. Mandra leased plantations are considered to be "purchased" plantations in the Company's public disclosure because they were acquired through the 2010 acquisition of Mandra.

4 The Company classifies this as being comprised of all WFOE (SW and SP) leased plantations.

5 The Company's explanation for this figure being approximately 106% of its disclosed timber holdings as at December 31, 2010 is that the IC reviewed leases for approximately 51,000 Ha. of plantation land which were

- via original Plantation Rights Certificates in the Company's name, to approximately 86,000 Ha. of WFOE purchased plantations,[6] and approximately 43,000 Ha. of WFOE planted plantations;[7] and

- via copies of Plantation Rights Certificates in the Company's name, to approximately 9,000 Ha. of WFOE purchased plantations, and approximately 12,000 Ha. of WFOE planted plantations.

In addition, as at December 31, 2010, the IC has determined that the Company has original or copies of forestry bureau confirmations relating to the acquisition of:

- approximately 467,000 Ha. of BVIs purchased plantations;

- approximately 89,000 Ha. of WFOE (SP) purchased plantations; and

- approximately 50,000 Ha. of WFOE (SP only) planted plantations.

The Company does not obtain registered title to BVI purchased plantations. In the case of the BVIs' plantations, the IC has visited forestry bureaus, Suppliers and AIs to seek independent evidence to establish a chain of title or payment transactions to verify such acquisitions. The purchase contracts, set-off arrangement documentation and forestry bureau confirmations constitute the documentary evidence as to the Company's contractual or other rights. The IC has been advised that the Company's rights to such plantations could be open to challenge. However, Management has advised that, to date, it is unaware of any such challenges that have not been resolved with the Suppliers in a manner satisfactory to the Company.

<u>Forestry Bureau Confirmations and Plantation Rights Certificates</u>

Registered title, through Plantation Rights Certificates is not available in the jurisdictions (i.e. cities and counties) examined by the IC Advisors for standing timber that is held without land use/lease rights. Therefore the Company was not able to obtain Plantation Rights Certificates for its BVIs standing timber assets in those areas. In these circumstances, the Company sought confirmations from the relevant local forestry bureau acknowledging its rights to the standing timber.

The IC Advisors reviewed forestry bureau confirmations for virtually all BVIs assets and non-Mandra WFOE purchased plantations held as at December 31, 2010. The IC Advisors, in meetings organized by Management, met with a sample of forestry bureaus with a view to obtaining verification of the Company's rights to standing timber in those jurisdictions. The

---

not included in the disclosed total of planted plantations of 77,700 Ha. as of December 31, 2010, due to a number of reasons, primarily because these lands had not yet been planted.

[6] These 86,000 Ha. of WFOE purchased plantations are composed of approximately 84,000 Ha. of leases under Mandra and approximately 2,000 Ha. of standing timber under SP.

[7] These 43,000 Ha. of WFOE planted plantations are composed approximately of 31,000 Ha. of leases under SW and approximately 12,000 Ha. of leases under SP.

result of such meetings to date have concluded with the forestry bureaus or related entities having issued new confirmations as to the Company's contractual rights to the Company in respect of 111,177 Ha. as of December 31, 2010[8] and 133,040 Ha. as of March 31, 2011,[9] and have acknowledged the issuance of existing confirmations issued to the Company as to certain rights, among other things, in respect of 113,058 Ha. as of December 31, 2010.[10]

Forestry bureau confirmations are not officially recognized documents and are not issued pursuant to a legislative mandate or, to the knowledge of the IC, a published policy. It appears they were issued at the request of the Company or its Suppliers. The confirmations are not title documents, in the Western sense of that term, although the IC believes they should be viewed as comfort indicating the relevant forestry bureau does not dispute SF's claims to the standing timber to which they relate and might provide comfort in case of disputes. The purchase contracts are the primary evidence of the Company's interest in timber assets.

In the meetings with forestry bureaus, the IC Advisors did not obtain significant insight into the internal authorization or diligence processes undertaken by the forestry bureaus in issuing confirmations and, as reflected elsewhere in this report, the IC did not have visibility into or complete comfort regarding the methods by which those confirmations were obtained. It should be noted that several Suppliers observed that SF was more demanding than other buyers in requiring forestry bureau confirmations.

Book Value of Timber

Based on its review to date, the IC is satisfied that the book value of the BVIs timber assets of $2.476 billion reflected on its 2010 Financial Statements and of SP WFOE standing timber assets of $298.6 million reflected in its 2010 Financial Statements reflects the purchase prices for such assets as set out in the BVIs and WFOE standing timber purchase contracts reviewed by the IC Advisors. Further, the purchase prices for such BVIs timber assets have been reconciled to the Company's financial statements based on set-off documentation relating to such contracts that were reviewed by the IC. However, these comments are also subject to the conclusions set out above under "Timber Ownership" on title and other rights to plantation assets.

The IC Advisors reviewed documentation acknowledging the execution of the set-off arrangements between Suppliers, the Company and AIs for the 2006-2010 period. However, the IC Advisors were unable to review any documentation of AIs or Suppliers which independently verified movements of cash in connection with such set-off arrangements between Suppliers, the Company and the AIs used to settle purchase prices paid to Suppliers by AIs on behalf of SF. We

---

8 Composed of 106,446 Ha. of BVI plantations and 4,731 Ha. of WFOE planted plantations, of which 60,707 Ha. were confirmed in the Hunan Forestry Entity #1 Confirmation. This amount is, however, different from the total 60,696 Ha. shown on the confirmation, which appears to arise from an addition error.

9 Composed of 128,309 Ha. of BVI plantations and 4,731 Ha. of WFOE planted plantations, of which 60,707 Ha. were confirmed in the Hunan Forestry Entity #1 Confirmation. This amount is however different from the total hectare of 60,696 shown on the confirmation, which appears to arise from an addition error.

10 Composed of 90,905 Ha. of BVI plantations and 22,153 Ha. of WFOE planted plantations.

note also that the independent valuation referred to in Part VIII below has not yet been completed.

Revenue Reconciliation

As reported in its First Interim Report, the IC has reconciled reported 2010 total revenue to the sales prices in BVIs timber sales contracts, together with macro customer level data from other businesses. However, the IC was unable to review any documentation of AIs or Suppliers which independently verified movements of cash in connection with set-off arrangements used to settle purchase prices paid, or sale proceeds received by, or on behalf of SF.

Relationships

- Yuda Wood: The IC is satisfied that Mr. Huang Ran is not currently an employee of the Company and that Yuda Wood is not a subsidiary of the Company. However, there is evidence suggesting close cooperation (including administrative assistance, possible payment of capital at the time of establishment, joint control of certain of Yuda Wood's RMB bank accounts and the numerous emails indicating coordination of funding and other business activities). Management has explained these arrangements were mechanisms that allowed the Company to monitor its interest in the timber transactions. Further, Huang Ran (a Yuda Wood employee) has an ownership and/or directorship in a number of Suppliers (See Section VI.B). The IC Advisors have been introduced to persons identified as influential backers of Yuda Wood but were unable to determine the relationships, if any, of such persons with Yuda Wood, the Company or other Suppliers or AIs. Management explanations of a number of Yuda Wood-related emails and answers to E&Y's questions are being reviewed by the IC and may not be capable of independent verification.

- Other: The IC's review has identified other situations which require further review. These situations suggest that the Company may have close relationships with certain Suppliers, and certain Suppliers and AIs may have cross-ownership and other relationships with each other. The IC notes that in the interviews conducted by the IC with selected AIs and Suppliers, all such parties represented that they were independent of SF. Management has very recently provided information and analysis intended to explain these situations. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board. Some of such information and explanations may not be capable of independent verification.

- Accounting Considerations: To the extent that any of SF's purchase and sale transactions are with related parties for accounting purposes, the value of these transactions as recorded on the books and records of the Company may be impacted.

Cash

As reported in the IC's First Interim Report, as a precautionary measure, the IC requested that PwC confirm SF's cash balances. PwC did this as of June 13, 2011 for both China accounts and "offshore" accounts. A total of 293 accounts controlled by SF in Hong Kong were confirmed, representing 100% of the expected cash position. There are a very significant number of accounts held by SF in China (in excess of 260) and the logistics and requirements of in-person/in-branch verification in that country led the IC to confirm only a portion of the China accounts (28 accounts, representing approximately 81% of the expected China cash position). The IC was satisfied that SF's expected cash position existed as at the date of the confirmation. The Board should be aware that at the time of the cash confirmation process, SF only updated the details of its cash position quarterly, so the confirmation results must be considered in that context. The IC has instituted certain additional controls over cash movements in excess of $1 million held in SF Hong Kong bank accounts in order to provide the IC with some precautionary comfort during the examination process. Further, Management has advised that cash balances are now updated on a more frequent basis. See Part XII.

BVI Structure

The BVI structure used by SF to purchase and sell standing timber assets could be challenged by the relevant Chinese authorities as the undertaking of "business activities" within China by foreign companies, which may only be undertaken by entities established within China with the requisite approvals. However, there is no clear definition of what constitutes "business activities" under Chinese law and there are different views among the IC's Chinese counsel and the Company's Chinese counsel as to whether the purchase and sale of timber in China as undertaken by the BVIs could be considered to constitute "business activities" within China. In the event that the relevant Chinese authorities consider the BVIs to be undertaking "business activities" within China, they may be required to cease such activities and could be subject to other regulatory action. As regularization of foreign businesses in China is an ongoing process, the government has in the past tended to allow foreign companies time to restructure their operations in accordance with regulatory requirements (the cost of which is uncertain), rather than enforcing the laws strictly and imposing penalties without notice. See Section II.B.2.

C. Challenges

Throughout its process, the IC has encountered numerous challenges in its attempts to implement a robust independent process which would yield reliable results. Among those challenges are the following:

(a) Chinese Legal Regime for Forestry:

- national laws and policies appear not yet to be implemented at all local levels;
- in practice, none of the local jurisdictions tested in which BVIs hold standing timber appears to have instituted a government registry and documentation system for the ownership of standing timber as distinct from a government registry system for the ownership of plantation land use rights;
- the registration of plantation land use rights, the issue of Plantation Rights Certificates and the establishment of registries, is incomplete in some jurisdictions based on the information available to the IC;
- as a result, title to standing timber, when not held in conjunction with a land use right, cannot be definitively proven by reference to a government maintained register; and
- Sino-Forest has requested confirmations from forestry bureaus of its acquisition of timber holdings (excluding land leases) as additional evidence of ownership. Certain forestry bureaus and Suppliers have indicated the confirmation was beyond the typical diligence practice in China for acquisition of timber holdings.

(b) Obtaining Information from Third Parties: For a variety of reasons, all of them outside the control of the IC, it is very difficult to obtain information from third parties in China. These reasons include the following:

- many of the third parties from whom the IC wanted information (e.g., AIs, Suppliers and forestry bureaus) are not compellable by the Company or Canadian legal processes;
- third parties appeared to have concerns relating to disclosure of information regarding their operations that could become public or fall into the hands of Chinese government authorities: many third parties explained their reluctance to provide requested documentation and information as being "for tax reasons" but declined to elaborate; and
- awareness of MW allegations, investigations and information gathering by the OSC and other parties, and court proceedings; while not often

explicitly articulated, third parties had an awareness of the controversy surrounding SF and a reluctance to be associated with any of these allegations or drawn into any of these processes.

(c) Small Management Team: The Company has a very small executive management team and it is stretched by:

- demands from the IC, the OSC and E&Y;
- the placement on administrative leave in late August 2011 of certain members of Management by the Company, based upon the advice of BJ. These employees remained available to assist Management upon request on a supervised basis, which further stretched the remaining management;
- the appointment of a new Chief Executive Officer part way through the IC process; and
- the fact that Management is dispersed among Canada, Hong Kong and various parts of China.

(d) Cultural/Language/Geographic Issues:

- vast majority of operational documents are in Chinese;
- most Asia-based Management employees' first language is Chinese;
- business practices in China and the SF business model:
  - rely heavily on personal relationships; and
  - documentation of contractual arrangements is not as comprehensive as would be typical in Western jurisdictions, is often not done until after the transaction is agreed and is frequently incomplete;
- geographic and time distances for the North American-based teams;
- SF's operations in China are widely and remotely geographically dispersed, a number of plantations are close to sensitive border areas and some are accessible only by overland vehicle travel; and
- public records in China are more limited than in Western jurisdictions and are often not complete, accessible, up to date or accurate.

(e) Corporate Governance/Operational Weaknesses: Management has asserted that business in China is based upon relationships. The IC and the IC Advisors have observed this through their efforts to obtain meetings with forestry bureaus, Suppliers and AIs and their other experience in China. The importance of relationships appears to have resulted in dependence on a relatively small group of Management who are integral to maintaining customer relationships, negotiating and finalizing the purchase and sale of plantation fibre contracts and the settlement of accounts receivable and accounts payable associated with plantation fibre contracts. This concentration of authority or lack of segregation of duties has been previously disclosed by the Company as a control weakness. As a result and as disclosed in the 2010 MD&A, senior Management in their ongoing evaluation of disclosure controls and procedures and internal controls over financial reporting, recognizing the disclosed weakness, determined that the design and controls were ineffective. The Chairman and Chief Financial Officer provided annual and quarterly certifications of their regulatory filings. Related to this weakness the following challenges presented themselves in the examination by the IC and the IC Advisors:

- operational and administration systems that are generally not sophisticated having regard to the size and complexity of the Company's business and in relation to North American practices; including:
    - incomplete or inadequate record creation and retention practices;
    - contracts not maintained in a central location;
    - significant volumes of data maintained across multiple locations on decentralized servers;
    - data on some servers in China appearing to have been deleted on an irregular basis, and there is no back-up system;
    - no integrated accounting system: accounting data is not maintained on a single, consolidated application, which can require extensive manual procedures to produce reports; and
    - a treasury function that was centralized for certain major financial accounts, but was not actively involved in the control or management of numerous local operations bank accounts;
- no internal audit function although there is evidence the Company has undertaken and continues to assess its disclosure controls and procedures and internal controls over financial reporting using senior Management and independent control consultants;
- SF employees conduct Company affairs from time to time using personal devices and non-corporate email addresses which have been observed to be shared across groups of staff and changed on a periodic and organized basis; this complicated and delayed the examination of email data by the IC Advisors; and

- lack of full cooperation/openness in the ICs examination from certain members of Management.

(f) Complexity, Lack of Visibility into, and Limitations of BVIs Model: The use of AIs and Suppliers as an essential feature of the BVIs standing timber business model contributes to the lack of visibility into title documentation, cash movements and tax liability since cash settlement in respect of the BVIs standing timber transactions takes place outside of the Company's books.

(g) Cooperation and openness of the Company's executives throughout the process: From the outset, the IC Advisors sought the full cooperation and support of Allen Chan and the executive management team. Initially, the executive management team appeared ill-prepared to address the IC's concerns in an organized fashion and there was perhaps a degree of culture shock as Management adjusted to the IC Advisors' examination. In any event, significant amounts of material information, particularly with respect to the relationship with Yuda Wood, interrelationships between AIs and/or Suppliers, were not provided to the IC Advisors as requested. In late August 2011 on the instructions of the IC, interviews of Management were conducted by the IC Advisors in which documents evidencing these connections were put to the Management for explanation. As a result of these interviews (which were also attended by BJ) the Company placed certain members of Management on administrative leave upon the advice of Company counsel. At the same time the OSC made allegations in the CTO of Management misconduct.

Following the implementation of these administrative leaves and the subsequent appointment of Judson Martin as the new Chief Executive Officer of the company on August 26, 2011, the cooperation received by the IC Advisors from the Company improved significantly. As a result of Mr. Martin's direction, meetings have been arranged and held with Suppliers, AI's and additional forestry bureaus. In addition, as noted above, very recently, Management presented information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

(h) Independence of the IC Process: The cooperation and collaboration of the IC with Management (operating under the direction of the new Chief Executive Officer) and with Company counsel in completing certain aspects of the IC's mandate has been noted by the OSC and by E&Y. Both have questioned the degree of independence of the IC from Management as a result of this interaction. The IC has explained the practical impediments to its work in the context of the distinct business culture (and associated issues of privacy) in the forestry sector in China in which the Company operates. Cooperation of third parties in Hong Kong and China, including employees, depends heavily on relationships and trust. As noted above, the Company's placing certain members of Management on administrative leave, as well as the OSC's allegations in the CTO, further hampered the IC's ability to conduct its process. As a result, the work of the IC was frequently done with the assistance of, or in reliance on, the new Chief Executive Officer and his Management team and Company counsel. Given that Mr. Martin was, in effect, selected by the IC and BJ was appointed in late June 2011, the IC concluded that, while not ideal, this was a practical and appropriate way to proceed in the circumstances. As evidenced by the increased number of scheduled meetings with forestry bureaus, Suppliers and AIs, and, very recently, the delivery to the IC of information regarding AIs and Suppliers and relationships among the Company and such parties, it is acknowledged that Mr. Martin's involvement in the process has been beneficial. It is also acknowledged that in executing his role and assisting the IC he has had to rely on certain of the members of Management who had been placed on administrative leave.

II. BUSINESS MODEL AND CORPORATE STRUCTURE

II. BUSINESS MODEL AND CORPORATE STRUCTURE

A. Business Model

The IC's understanding of the Company's business model remains as described in its First Interim Report and reference should be made to that for an overall understanding of the business segments of the Company and their relative importance. The plantation fibre operations and, in particular, the core activity of purchasing and selling standing timber through the BVIs/AI structure is the central driver of asset value, revenue and income for SF. BVI entities within the BVI/AI structure represented as at December 31, 2010 $2.476 billion of book value (466,826 Ha.) and $1.326 billion in revenue, and approximately $622 million of Income for the year then ended before allocation of corporate overhead.

The plantation fibre operations use two principal business models, a "purchased plantation" model and a "planted plantation" model and disclose its timber assets in its AIF and other disclosure documents on that basis. The purchased plantation model operates through two legal structures: a BVI/AI legal structure and, to a lesser but growing extent, a China incorporated WFOE legal structure. The planted plantations model is operated exclusively through the WFOE legal structure (although the WFOEs themselves are typically held indirectly through a BVIs holding structure). Management advised that no new cash capital had been deployed by SF into the BVIs' standing timber operations since 2004. Recently identified e-mails suggest that payments may have been made from the WFOE structure into the BVIs structure, e.g., by an offshore customer of a WFOE to settle amounts due to a BVIs, and by WFOEs to establish BVIs Suppliers. Management has not yet provided a full explanation of all these emails. However, Management has advised that there have been transactions whereby SF subsidiaries sell imported logs offshore to a Chinese customer who then owes SF U.S. dollars or Hong Kong dollars. As a result of pressure to collect receivables and the fact that the customer does not have the required currency, SF accepts payment in RMB. The RMB is accepted as payment onshore and is used to buy trees in the BVI model.

The purchased plantation model involves the purchase of standing timber and sale of standing timber pursuant to standardized timber purchase agreements and Entrusted Sale Agreements. The standing timber purchased is generally on land owned by collectives or villages (i.e., not state-owned land). When conducted through the BVIs/AI legal structure, of which 20 BVIs hold all of the BVI timber assets, the timber purchases are arranged through Suppliers. The relationship between such Suppliers and SF has been the focus of much review by the IC. (see Part VI below.) The BVIs structure does not involve the BVIs concurrently purchasing land use rights or leases with the purchase of standing of timber. However, the BVIs supply contracts typically contain a right of first refusal for the BVIs to acquire, or nominate an affiliate to acquire the plantation land use rights after the timber has been harvested. Despite such common contractual provision, the IC Advisors did not identify any occasions when such rights have been exercised.

The BVIs do not sell standing timber directly to customers; they sell under contract to an entity referred to as an AI who usually resells to others. The BVIs timber sales accounts receivables are settled by the AI making payments to Suppliers (directly or indirectly to other parties on their behalf) on behalf of SF. These payments by way of set-off enable the BVIs to acquire further standing timber from Suppliers. As SF has publicly disclosed, no cash actually flows directly through the BVIs – all BVIs purchases are funded through the set-off mechanism using accounts receivable owed to SF. The particulars of the sales process between BVIs and AIs is set out in Section II.B and Section V.C.15.(b), below.

WFOEs are also engaged in the purchase and sale of standing timber through the SP group of entities with such activity classified as purchased plantations in the 2010 AIF disclosure. When conducted through a WFOE, purchases of standing timber are sometimes accompanied by concurrently obtaining plantation land use rights. The IC understands that WFOE standing timber transactions do not usually involve payments by way of set-off but are conducted on a direct fund transfer basis.

The planted plantation model is conducted by WFOEs through both SP and SW. It involves obtaining plantation land use rights, sometimes with standing timber but often as bare land suitable for planting. Management advises that sales from these planted plantations do not utilize the AI model but rather generally involve direct fund transfers by the WFOEs to the customer, some of whom are the same as or related to AIs under the BVIs/AI model. The IC understands that WFOEs, whether selling standing timber or selling logs from either planted plantations or purchased plantations, both buy and sell on a direct fund transfer basis; with all transactions settled in RMB.

What has become apparent throughout the examination process, is that important and integral elements of the business model are the relationships with business partners. Management had not been forthcoming in clarifying the parties behind the Suppliers and AIs or the relationships with the forestry bureaus that Management stresses are important to the ongoing business. However, as noted above, very recently, Management presented information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board. The extent of relationships, as discussed later in this report, are important to both the business model and to reporting requirements.

B. BVI Structure

The Company has established 58 companies in the British Virgin Islands. It uses these companies as both holding companies for subsidiaries in China and to engage in the purchase and sale of standing timber in China.

During the IC's review period of the first fiscal quarter of 2006 to the first fiscal quarter of 2011, a total of 20 BVIs entered into a total of 453 timber purchase contracts for the purchase of 823,153 Ha. of standing timber. The aggregate purchase price was RMB 28.654 billion. Of those purchases, 466,826 Ha. of standing timber from 310 timber purchase contracts remained in the Company's books as at December 31, 2010, with the balance being accounted for by sales between the first fiscal quarters of 2006 and 2011, and by purchases made in the first fiscal quarter of 2011.

Of those 20 BVIs, only Suri-Wood Inc. and Sino-Panel (Yunnan) Limited were incorporated prior to 2009. The remaining 18 BVIs are subsidiaries of Suri-Wood Inc. incorporated in 2009 or later and have company names not immediately associated with Sino-Forest, such as Brain Force

Limited, Glory Billion International and Trillion Edge Limited. A table summarising BVI corporate search results for all BVIs is found at Schedule V.A.1.

The BVI with the most purchases during the review period was Suri-Wood Inc., which had 131 purchase transactions amounting to a total of 325,697 Ha. and RMB 10.994 billion. However, its last purchase transaction was in 2008. Over the same period Sino-Panel (Yunnan) Limited had just two purchase transactions in 2007 amounting to 10,438 Ha. and RMB 670.5 million. Further, another BVI called Sino-Forest Resources Inc. had purchases prior to but not during the review period.

The remaining 18 BVIs account for all 320 BVI timber purchase contracts entered into from the first fiscal quarter of 2009 to the first fiscal quarter of 2011, amounting to 487,018 Ha. and RMB 16.989 billion.

During the IC's review period, Suri-Wood Inc., Sino-Panel (Yunnan) Limited and Sino-Forest Resources Inc. had a total of 582 sales transactions amounting to a total of 548,292 Ha. and RMB 27.465 billion. The BVI with the most sales during this period was Suri-Wood Inc. which had 509 sales transactions amounting to a total of 492,718 Ha. and RMB 24.099 billion. The 18 BVIs incorporated after 2009 are yet to have sales recorded as at the date of this report.

Despite criticism of the use of British Virgin Islands holding structures in the MW Report (which describes them on page 2 as an "unjustifiable black hole"), IC believes that there are proper commercial reasons for using British Virgin Islands holding structures for investing in China.

1. BVIs as Investment Vehicles

Many foreign investors, including well known multi-national companies, hold their investments in China in special purpose vehicles established overseas in jurisdictions with a familiar and internationally accepted system of corporate governance. By way of example, over 75% of blue chip companies listed on the Hong Kong Stock Exchange (Hang Seng Index constituent stocks excluding the Finance Sub-Index) utilise British Virgin Islands holding structures, including for their investments in China. This reduces the uncertainties of operating under relatively new and untested Chinese corporate structures, and enables investors to enter into shareholding arrangements under familiar Western structures, governed by a common law system.

The British Virgin Islands has been a particularly popular jurisdiction in which to establish such companies, because of the lack of corporate income tax, capital duty and stamp duty on profits or issue or sale of shares. The use of such special purpose companies, one for each investment, also facilitates raising capital offshore and restructuring such companies without the uncertainties and delays inherent in the domestic Chinese system which requires a host of government approvals for even minor changes to a company ownership or structure.

2. BVIs as Vehicles to Purchase and Sell Timber

The IC has been advised by its Chinese counsel that there is no express statutory prohibition that foreign companies such as the BVIs may not purchase, hold and sell assets including standing timber located in China. Foreign companies may, after obtaining necessary government approvals and clearances and going through the proper formalities relating to foreign exchange, remit foreign exchange into China and pay the purchase prices and repatriate the sale proceeds outside of China on the basis of proper documentary support, including evidence of payment of income tax and other taxes such as VAT (which is usually withheld by the domestic payer as withholding agent).

However, business operations in China conducted by foreign companies without an onshore presence is generally not allowed. Since 1992, SAIC regulations have required foreign companies to set up onshore entities within China before carrying out "business activities" within China. Chinese laws do not have any express definition of what activities carried out by foreign companies would constitute "business activities."

The Company has obtained Chinese legal opinions that state that the purchase of timber in China by certain BVIs and the sale of such timber by those BVIs are not prohibited by Chinese law,[11] and that "to the best of [local counsel's] knowledge after reasonable investigation and inquiry and as confirmed by the Company, each of the [BVIs listed] has the right to conduct business in China in the manner as presently conducted and as described in the Disclosure Package and the Final Offering Memorandum".[12] However, Chinese counsel to the IC has advised that, on the basis of the materials reviewed by it, interviews with Company officers and representatives of Suppliers, AIs and forestry bureaus, as well as its other investigations from June 2011 to the present, it cannot definitively conclude that the activities of the BVIs are not "business activities" carried on within China, and it is believed there is a risk that such activities, taken as a whole, might be considered carrying out "business activities", which requires a business to be registered in China. Chinese counsel to the Company and Chinese counsel to the IC met to consider these issues on November 11, 2011, and concluded that, given the lack of an express definition of "business activities" under Chinese law, and the uncertainty of the Chinese legal system, it was not possible to reach a definitive opinion on this issue.

Under the BVI structure, the BVIs do not sell standing timber directly to customers, they sell to AIs who, the IC are told, usually resell to others. Instead of receiving after-tax payment directly from the AIs, the BVI sales accounts receivables are settled in RMB by the AIs making payments to Suppliers on behalf of SF, which are usually by way of set-off (and some AIs and Suppliers stated to the IC Advisors during interviews that they sometimes directed the set-offs to be made to and from other parties), and thus enable the BVIs to acquire further standing timber from Suppliers without remitting the sale proceeds offshore and purchase monies back onshore again. This process avoids Chinese foreign exchange controls which must be complied with in a normal cross-border sale and purchase transaction, and this could present an obstacle to future repatriation of sales proceeds, and could have tax implications as well.

The Chinese authorities have demonstrated tolerance towards business activities that may be regarded as technically non-compliant or arguably non-compliant as business practices are gradually regularised over time, and tax laws are enforced more strictly year by year. While such practices by the BVIs and AIs have been going on for many years (since the 1990s according to

---

11 See Jingtian & Gongcheng legal opinions issued for the reference of the Company's auditors in 2007 and 2008.

12 Jingtian & Gongcheng legal opinion dated October 21, 2010 in respect of offering of 6.25% Guaranteed Senior Notes Due 2017.

Management), the Company has achieved large scale operations only in more recent years, which may result in more attention from the Chinese authorities. The BVIs are subject to withholding tax, stamp tax liabilities and VAT or business tax (as the case may be) and the AIs need to specifically record in their financial statements liabilities of those taxes to be paid on behalf of the BVIs. While AIs are responsible for paying tax on behalf of the BVIs according to the terms of the standard form entrusted sales contracts they enter into with BVIs, the IC has not been able to verify that any relevant income taxes and VAT have been paid by or on behalf of the BVIs in China.

The Company discloses potential Chinese tax liabilities as a risk factor in its AIF, and sets out the methodologies it uses for calculating such liabilities. The Company states that Management applies significant estimates and judgment to determine the appropriate amount of tax related liabilities, and contingencies for such liabilities, to be recognized and disclosed in the financial statements. The Company recognized a provision of approximately $160 million as at December 31, 2010 for contingent Chinese tax liabilities.

In the event that this business model is challenged by the relevant Chinese authorities as carrying on business activities in China by the BVIs, Chinese counsel to the IC has advised that, quite apart from the tax and foreign exchange compliance issues mentioned above, SF may be required to cease operations under this business model and could be subjected to administrative fines and other penalties.

However, as regularization of the practices of foreign businesses in China is an on-going process (as has happened in various industries since the early 1990s), the government has in the past tended to allow foreign companies a period to restructure their operations in accordance with regulatory requirements rather than enforcing the laws strictly and imposing penalties without notice.

3. WFOEs as Trading Vehicles since 2004

Chinese counsel to the IC has advised that, under Chinese law, the business of purchase and sale of standing timber could be categorized as a form of trading or commodity distribution business, which is an industry in which foreign investment in China has been subject to various restrictions and has been subject to change over the years.

In 1992, the State Council issued a notice to permit foreign-invested enterprises to be established in the commodity distribution industry in five trial cities, subject to relevant approval. However, in that notice, the State Council explicitly prohibited wholly foreign-owned enterprises from engaging in that industry.

In 2004, MOFCOM issued a notice that lifted both the prohibition on wholly foreign-owned enterprises from engaging in the commodity distribution industry and the limitation to certain cities. Since then, foreign investors have been permitted to, subject to relevant regulatory approval, establish trading companies (either as joint ventures or wholly foreign-owned enterprises) to participate in most areas of the commodity distribution industry, including the purchase and sale of standing timber, throughout China.

The Company established its first WFOE to engage in the purchase and sale of standing timber in 2004 in compliance with such regulatory requirements.

C. Corporate Structure

The Company's corporate structure is detailed in Schedule II.C. The organization has multiple subsidiary companies that have been formed over time to hold the different assets of the Company. There are, for example, about twenty BVIs holding different parcels of standing timber in China.

From a legal perspective, the vast majority of the subsidiaries are held through two holding companies: Sino-Wood and Sino-Panel.

Sino-Wood

SW holds, through many subsidiaries in the British Virgin Islands, Hong Kong and China, the Mandra assets, the BVIs' standing timber assets and a significant portion of non-Mandra WFOE assets. Management explained that functionally within SW, the domestic WFOE business and BVI business are operated quite separately. SW is also responsible for the flooring manufacturing operations, HOMIX, and the nursery business. SW is engaged in the buying and selling of imported logs.

In the SW WFOE domestic business (including Mandra), Albert Zhao is responsible for operations and Chen Hua is responsible for finance.

Sino-Panel

SP holds, through many subsidiaries in the British Virgin Islands and China, a significant portion of the non-Mandra WFOE assets. Management explained that Albert Ip was responsible for operations and George Ho was responsible for finance.

SP engages in both the purchased plantation business model and in the planted plantation business model. It also engages in the buying and selling of imported logs and, to a limited extent, in the buying and selling of domestic logs. We also understand it has some manufacturing operations.

For the BVI standing timber business, Albert Ip is responsible for purchases, Albert Zhao is responsible for sales, and Alfred Hung is responsible for finance.

III. LEGAL REGIME

III. LEGAL REGIME

A. Evidence of Ownership of Tree Plantations

The core activity of the Company's business is the purchase and sale of standing timber using the "purchased plantation" model, principally through BVIs, and to a lesser extent, through WFOEs. The BVI model is described more fully in Part II above. The BVIs (and sometimes WFOEs) acquire standing timber pursuant to timber purchase contracts from Suppliers without acquiring any land use rights. Forestry bureau "confirmation letters" are commonly obtained by the Supplier from the local forestry bureau at county level or above in respect of such contracts. One Supplier, in its interview with the IC, noted that SF is its only customer requiring confirmation letters for standing timber purchases in addition to a purchase agreement. It appears that issuing confirmations is not typical practice and that such confirmations have been provided as a "favour" at the request of the Company and its Suppliers. WFOEs acquire standing timber on a stand-alone basis or in conjunction with land use rights or land leases. When land use rights or land leases are acquired, Plantation Rights Certificates are often eventually obtained in the name of the contracting WFOE subsidiary evidencing registered title.

(a) <u>Forestry Administration</u> - China utilizes a top-down hierarchical system to govern its timber resources:

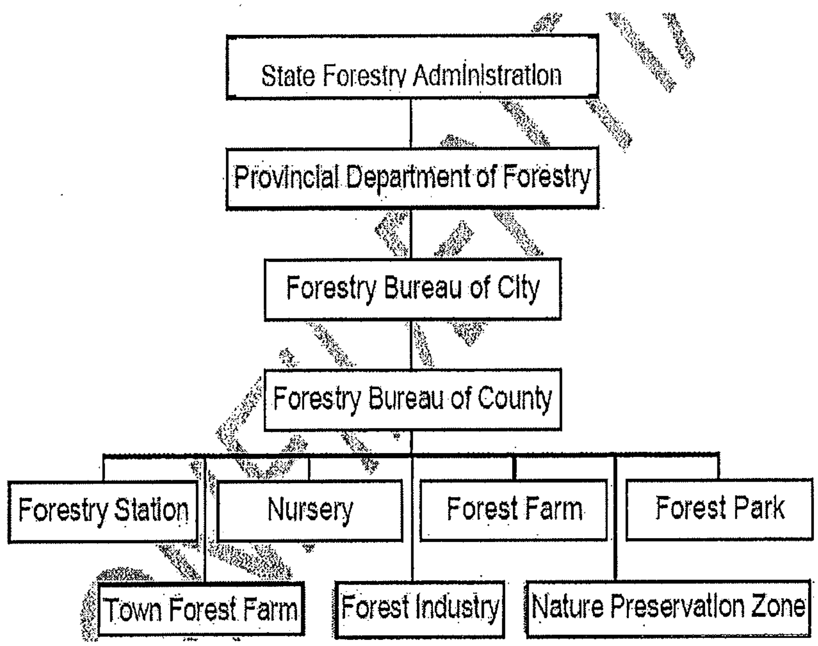
   (i) *State Forestry Administration* - the central level, responsible for national legislation, policy development, national strategic planning and key forestry programs;

   (ii) *provincial departments of forestry* - the regional level, responsible for forest regulation, by-laws and regional policy, short-term forestry and forest resource planning and organizing key programs;

   (iii) *city-level Forestry Bureaus* - primarily act as a bridge for county and provincial level communications; and

   (iv) *county Forestry Bureaus* - the local level, oversees the implementation of the central or provincial projects, resource management planning and land/forest title management.

This administrative structure is illustrated in the following figure:



(b) Regulatory Framework - The key legislation regulating the forestry industry in China is the Forestry Law (effective from January 1, 1985, as amended), and its Implementation Regulations (effective from January 29, 2000, as amended). These are supplemented by various provisions, notices and other administrative rules at the national and provincial level.

The transfer of timber and other plantation rights is permitted by the relevant legislation, in particular the "Opinions on Comprehensively Promoting the Reform of the Collectively Owned Plantation Right System" (promulgated by the State Council of China on July 14, 2008). Such Opinions provide that, among others, farmers with contractual rights over collectively-owned commercial plantations may, without change of the plantation usage, and in accordance with applicable laws and regulations, dispose of such rights relating to plantation operations and plantation tree ownership rights through sub-contracts, leases, transfers, mortgages, or as contributions in capital or under cooperative structures.

The Forestry Law and its Implementation Regulations implement a system of plantation rights registration and issuance of certificates as evidence of such registration. Pursuant to the Implementation Regulations, all entities must apply to the forestry bureau of the local government at the county level or above for plantation rights registration, and such forestry bureau is responsible for issuing Plantation Rights Certificates.

There are four types of rights associated with plantations in China, being:

(i) plantation land ownership,

(ii) plantation land use rights,

(iii) timber ownership and

(iv) timber use rights,

all of which are separate rights. Private enterprises cannot hold plantation land ownership but may hold plantation land use rights for a specified duration (up to 70 years), timber ownership and timber use rights. In certain provinces, foreign enterprises cannot acquire land use rights. The various rights are separate rights and can be separately owned by different parties.

(c) Plantation Rights Certificates and Confirmations - A Plantation Rights Certificate should reflect plantation rights as registered in the registration system and is the ultimate proof of ownership and sets out the parties that hold each of such rights. There is a nationally mandated registration system for Plantation Rights Certificates, though there appear to be some locations where Plantation Rights Certificates are not issued. In every visit with forestry bureaus conducted by the IC Advisors, they were told that Plantation Rights Certificates are not issued for timber ownership alone and that there is no forestry bureau record of the sale and purchase of standing timber alone. In these circumstances, the Company required their Suppliers to seek and they typically obtained from local forestry bureaus, "confirmation letters" (or "approvals") relating to the standing timber purchase contracts entered into by its BVIs and some WFOEs. These confirmation letters are not title documents as there appears to be no official regulatory basis for their issue. We understand that there is no registration system for such confirmation letters or approvals.

The forestry bureau confirmations are not a form of official documents contemplated by the applicable regulatory regime. Rather, we believe, based on meetings with certain forestry bureau officials or former officials and with certain Suppliers, and discussion with Management, that they are documents issued at the request of either the Company or, more commonly, its Suppliers as a "favour" and should not be disclosed outside the Company or relied upon legally. They have what purports to be the forestry bureau's Chop on them. We believe the forestry bureau confirmations should be viewed as comfort indicating that the relevant forestry bureaus do not dispute SF's claims to the standing timber to which they relate, but which are not documents of title that could be relied upon in event of a dispute or in a court of law. However as noted below, a number of the forestry bureaus have indicated that these have been issued at SF's request and that the confirmations are for SF internal use only and may not be shown to third parties. This could limit the usefulness of these documents in any legal dispute.

In two instances the IC Advisors have identified that forestry bureau officials were either concurrently or subsequently employees of, or consultants to, SF. One forestry bureau indicated that it assigned employees to SF and other companies to assist in the development of the forestry industry in its jurisdiction.

Attached as Schedule III.A is a chart prepared by the IC's independent Chinese counsel setting out the availability of Plantation Rights Certificates in various provinces in China.

B. Available Legal Opinions

Given the foregoing, the IC's independent Chinese counsel has advised that the available legal opinions regarding the Company's interests in its planted and purchased plantation standing timber, vary depending on the nature of the interest held. Schedule III.B sets out the form of opinion which JH has indicated it could provide to the IC. In summary, and subject in each case to the qualifications and assumptions set out in such form of opinion:

(a) **if the BVI or WFOE has entered into a timber purchase contract to acquire standing timber, has from the local forestry bureau a written confirmation letter and does not have a Plantation Rights Certificate registered in its name or been provided the relevant Plantation Rights Certificate registered in the name of the Supplier for such standing timber:** each such timber purchase contract entered into by such BVIs or WFOE is valid, effective and legally binding on the parties thereto subject to the authorization by (a) the *de facto* owner with the Plantation Rights Certificate for such standing timber, if any, or (b) the ultimate farmer or collective economic organization who has legally obtained the ownership of the standing timber during the reform of the collectively-owned plantation rights system, as the case may be. If the *de facto* owner or the ultimate farmer or collective economic organization, as the case may be, refuses to grant the authorization to any contract, the contract will be void and the Company will have no contractual rights. However, if the Company has paid consideration to the Supplier pursuant to the contract, the Company will have a cause of action against the Supplier for the return of the consideration based on the legal theory of unjust enrichment;

(b) **where the WFOE has entered into a timber purchase contract and a forest land use rights lease contract and has the relevant Plantation Rights Certificate registered in its name:** the WFOE has legally obtained the use right of the forest land and the ownership of the standing timber as recorded in the Plantation Rights Certificate;

(c) **where the WFOE has entered into a purchase contract and forest land use rights lease contract, has a forestry bureau confirmation letter and has not acquired the relevant Plantation Rights Certificate registered in its name but has been provided the relevant Plantation Rights Certificate registered in the name of the Supplier:** the forest land use lease contract and timber purchase contract are valid, effective and legally binding upon the parties thereto and are enforceable against the parties thereto; as a result, the WFOE has contractual rights to the forest land and standing timber as provided in such contracts;

(d) **where the WFOE has entered into a timber purchase contract and a forest land use rights lease contract and has obtained a forestry bureau confirmation letter but has not obtained relevant Plantation Rights**

Certificate registered in its name or been provided the relevant Plantation Rights Certificate registered in the name of the Supplier: such timber purchase contract and forest land use rights lease contract is valid, effective and legally binding subject to the authorization by (a) the *de facto* owner with the relevant Plantation Rights Certificate, if any, or (b) the ultimate farmer or collective economic organization who has legally obtained the ownership of the standing timber during the reform of the collectively-owned plantation rights systems, as the case may be. If the *de facto* owner or the ultimate farmer or collective economic organization, as the case may be, refuses to grant the authorization to any contract, the contract will be void and the Company will have no contractual rights. However, if the Company has paid consideration to the Supplier pursuant to the contract, the Company will have a cause of action against the Supplier for the return of the consideration based on the legal theory of unjust enrichment; and

(e) **where the WFOE has entered into a timber purchase contract, has obtained the forestry bureau confirmation letter and has not acquired the relevant Plantation Rights Certificate registered in its name but has been provided the relevant Plantation Rights Certificate registered in the Supplier's name:** the timber purchase contract is valid, effective and legally binding upon the parties thereto and is enforceable against the parties thereto pursuant to the terms and conditions thereof; as a result, the WFOE has contractual rights to the standing timber as provided in such contract.

JH's form of legal opinion also provides that, while a forestry bureau confirmation letter does not constitute definitive evidence of ownership of the standing timber referred to therein, such letters may provide certain comfort in respect of the BVIs or WFOE contractual or other rights over such standing timber. This is because under applicable Chinese law, in the event of any dispute in respect of the ownership of standing timber, the disputing party shall seek determination of such ownership from the government, namely the forestry bureau, before they may start litigation in the court.

We note that in prior years SF has obtained legal opinions from its Chinese counsel regarding its plantation rights assets and business in China. These opinions were issued in connection with its annual audit or offshore securities issues. It is not clear to the IC what level of due diligence was undertaken by Chinese counsel in connection with the issue of such opinion. In the context of the IC's review, JH's due diligence process has been rigorous and has included JH's visits with forestry bureaus, review of original contracts, Plantation Rights Certificates and forestry bureau confirmations, and participation in the investigation undertaken by the IC.

C. SAIC Filings

The SF transaction volumes with a number of AI and Suppliers do not match the revenue reported by such Suppliers in their SAIC filings. The AIs and Suppliers, which are private entities, make their own filings without input or review by SF. Attached as Schedule III.C is a chart setting out such differences. Both MW and the OSC have focused greatly on this differential.

IC Advisors made the following observations to the IC regarding the reliability of SAIC filings:

(a) Discrepancies between the information set forth in SAIC filings and the filer's books and records, as well as the filer's tax filings, can be expected in China. There are a number of reasons for this, such as the following:

- SAIC searches are not definitive - filings and searches are not of the same status as in many Western countries, and should not be relied upon as being up-to-date and wholly accurate; and
- the requirements for filing accounts with SAIC branches may be different from the requirements for statutory tax audits, resulting in different numbers.

(b) SAIC filings should not be relied upon exclusively. The unreliability of financial information in such filings is something that one should take into account in China.

(c) The way in which companies file with the SAIC / MOFCOM / SAFE / Finance Bureau / Tax Bureau / etc. would not usually be seen as a matter that concerns the counterparties that deal with such filers in China, with the possible exception of tax filings in the case of SF, as the AIs have an obligation under the Entrusted Sales Agreements to "pay relevant taxes on behalf of the Company".

(d) While information in such filings as to legal representations and shareholders is generally more accurate it is not uncommon practice in China that one or more registered shareholders may be a trustee or nominee holder for an underlying beneficial holder who is undisclosed.

(e) Legal and practical consequences of inaccurate SAIC filings could range from the draconian (on a literal interpretation of the legislation in the case of repeated, egregious breaches) to an expectation not to rely on filings (as a matter of common practice). The national government policy is that filings should be accurate, but the system of corporate filings / independent audits / imposition of tax / etc. is still at an early stage in China, and as a matter of practice, legislation reflecting such policy will only be enforced as and when the regulators choose to do so.

The conclusion that the IC has drawn from this advice is that information in SAIC filings, particularly financial filings, is one data point to consider but no conclusions can be drawn from that information alone, whether it be conclusions of a financial nature, ownership nature or otherwise based.

IV. PROCESS TO DATE

IV. PROCESS TO DATE

The IC Advisors' report on the process conducted on behalf of the IC is attached as Schedule IV. The scope of review and the processes undertaken by the IC Advisors to date were determined by the IC and have been subject to certain limitations. The IC, in its judgment, considers such limitations to be appropriate, having regard to the challenges discussed in Section I.C of this report, time constraints and cost/benefit considerations.

V. TIMBER ASSET VERIFICATION

V. TIMBER ASSET VERIFICATION

The principal objective of the asset verification process is to confirm SF's ownership of or contractual and other rights to standing timber in China, whether held by BVIs or WFOEs. In addition, steps were taken to verify the corporate existence of the subsidiary entities within the Company's corporate structure.

A central theme of the MW Report is that the Company does not own all the timber assets recorded on its books and that its reported revenue from timber is overstated. A principal task of the IC has been to examine the Company's rights to its timber assets and the revenue therefrom as reported in its 2010 Financial Statements. The chart attached as Schedule V sets out an overall summary of the Company's timber holdings as at December 31, 2010 broken down by organizational stream within the Company and showing the type of document held by the Company as evidence of title or contractual and other rights. Such documents include purchase contracts, Plantation Rights Certificates and forestry bureau confirmations.

A. Corporate Existence

The Company provided a list of the 149 entities comprising the SF group of companies: 58 BVI entities, 7 HK entities, 75 China entities, 2 Canadian entities, 1 Barbados entity, and 6 other entities (See Schedule V.A.) and a Chart showing the organization thereof (see Schedule II.C).

The existence of the Subsidiary BVIs and the WFOEs indicated on the Chart and the Company's ownership thereof has been confirmed as at the date of the searches. As noted below, the directors and officers of all such subsidiaries, with the exception of one,[13] were listed in SF records as being employees of the Company at the time of the searches. This included Mr. Allen Chan, who has subsequently resigned from his position. Management and its counsel have advised that they are undertaking changes to install current Management as directors and officers of such subsidiaries. The IC has not independently verified this process. Such searches do not assure that the Company does not own other subsidiaries or interests in other entities.

1. BVIs

To verify the incorporation and existence of the Subsidiary BVIs on the Chart, the IC:

- confirmed that the list provided by the Company included all of the BVIs listed as material subsidiaries in the 2010 AIF;
- obtained search results (including copies of charter documents) and original certificates of good standing through BVI counsel for all 58 BVIs listed;
- obtained original certificates of incumbency showing directors, officers and shareholders for the Subsidiary BVIs listed; and

---

[13] The authorized person to handle SAIC matters for Sino-Forest (Heyuan) Co., Ltd., He Qianghua, does not appear on the list of employees provided by the Company.

- summarized the search results in respect of each Subsidiary BVI listed, including verifying that the list accurately reflected the corporate name and shareholders of such Subsidiary BVI and that its directors and officers were employees of the Company at the date of the searches.

A table summarizing the BVI corporate search results is appended hereto as Schedule V.A.1.

2. WFOEs

To verify the incorporation and existence of the WFOEs on the Chart, the IC Advisors have:

- confirmed that the corporate list provided by the Company included all of the WFOEs listed as material subsidiaries in the 2010 AIF;
- obtained SAIC search results in China (including up to date basic company information sheets) for all WFOEs identified in the list; and
- summarized the search results in respect of each WFOE listed, including verifying that the list accurately reflected the name and shareholders of such WFOE Subsidiary and confirming its lawful incorporation, validity of business license and current scope of business.

A table summarizing the Chinese SAIC search results is appended hereto as Schedule V.A.2.

B. Master Framework Agreements

1. Overview of MFAs

Between September 2006 and the second fiscal quarter of 2011, through both BVIs and WFOEs, the Company entered into nine long-term MFAs with nine different Counterparties. These contracts address the supply to the Company of standing timber covering 1,667,667 Ha. in seven provinces over varying periods of three to fourteen years.

The MW Report questioned the legitimacy of certain of the MFAs. In its response to the MW Report, Management characterized the MFAs as framework agreements that are similar to a "Heads of Agreement" commonly used in Western business circles to outline the terms of a business deal. The MFAs provide the basis for subsequent specific purchase agreements for standing timber in the specific region.

2. MFA Review Process

The IC:

- reviewed the MW Report and Management's Response thereto;
- reviewed the Chinese texts and English translations of nine MFAs;

- reviewed certain public disclosure relating to the MFAs, including that set out in the 2010 AIF, 2010 MD&A and press releases issued by the Company concerning the MFAs;
- reviewed BVI and WFOE purchase contracts provided by the Company for standing timber held as at December 31, 2010, various BVI and WFOE contract spreadsheets, and BVI and WFOE asset listings as referred to elsewhere in this report;
- engaged in discussions with Management with respect to the business, including MFAs;
- performed corporate searches on each MFA Counterparty and potential related parties; and
- interviewed two of the MFA Counterparties (Supplier #3 and Supplier #19) in connection with its process interviewing certain Suppliers and AIs.

3. Muddy Waters MFA Allegations

The MW Report made a number of allegations with respect to the legitimacy of various Suppliers to the Company. Pages 16 to 29 of the MW Report focus on certain MFAs and the Counterparties thereto, particularly the MFAs with:

- Gengma Dai and Wa Tribes Autonomous Region Forestry Co., Ltd. (incorporated March 25, 1995, with registered capital of RMB 3 million, contract on March 23, 2007 for a 10 year term - approximately 200,000 Ha.);
- Zhanjiang Bohu Wood Co., Ltd. (incorporated on November 2, 2007, with registered capital of RMB 10 million (versus RMB 1 million disclosed in the MW Report), contract on December 10, 2007 for a 5 year term - approximately 150,000 Ha.);
- Zhangzhou Lu Sheng Forestry Development Co., Ltd. (incorporated November 19, 2007, with registered capital of RMB 2 million (versus RMB 550,000 disclosed in the MW Report), contract on August 11, 2008 for 10 year terms - approximately 200,000 Ha.); and
- Jiangxi Zhonggan Industrial Development Co., Ltd. (incorporated January 28, 2008 (versus January 28, 2009 as disclosed in the MW Report), with registered capital of USD 5 million (as disclosed in the MW Report), contract on June 11, 2009 for a 3 year term - approximately 150,000-300,000 Ha.).

The thrust of the Muddy Waters allegations is that the Company could not have made purchases from those Suppliers in the volume stated in those agreements. A number of reasons are put forth for that allegation which broadly can be summarized as follows:

- allegations that the Counterparties are generally newly created and thus cannot be credible Suppliers of the contracted supply volumes;

- allegations that based on SAIC filings the Counterparties have insufficient capital to support the contracted supply volumes;

- allegations that the Counterparties occupy simple offices or homes indicating that they are not sophisticated enough to be credible Suppliers of the contracted supply volumes; and

- allegations that the Counterparties' SAIC filings relating to their financial activity do not reflect SF's recorded contracted volume of business with such Counterparties; (including a detailed analysis of the Gengma Dai MFA by reference to Lincang City Forestry Bureau reports of forestry activity, reports on GDP and foreign investment levels for Lincang City in addition to SAIC financial filings).

There are a number of other specific allegations pertaining to each of the above-noted MFA Counterparties some of which are addressed in Part VI.

4. MFA Contract Terms

Each English translation of an MFA is 6-8 pages long. The MFAs are substantially similar although they have evolved over time to more closely reflect apparent actual practice. Key terms, and facts are summarized below:

- The SF subsidiary entering into an MFA was a BVI in the first 6 MFAs (2006-2008) and a WFOE subsidiary in the last 3 MFAs (2009-2011). The SF subsidiary may assign all its rights and obligations under the MFA to another SF subsidiary.

- Under each MFA, the SF subsidiary has first right of refusal to purchase very large volumes of standing timber (measured by mu/Ha. and cubic meters) in a designated area or region. Plantation land use rights are explicitly excluded from this first right of refusal.

- The MFA's do not contemplate the sale of the large volumes of standing timber through one transaction. Rather, the SF subsidiary is to exercise its rights by entering into a series of specific timber purchase agreements with the MFA Counterparty. Given the SF subsidiary may assign its rights and obligations under the MFA to any other SF subsidiary, both BVIs and WFOEs may ultimately enter into those specific timber purchase agreements.

- The MFAs stipulate that after a specific timber purchase agreement has been entered into, and the subject standing timber has been harvested, the SF subsidiary then has a preferential option to lease the underlying land.

- The MFA recitals state that the Counterparty has received, either directly or indirectly through an entrusted third party, the full commission of the original owner to enter into the MFA. Regarding the actual performance of the MFA, the actual contractual warranties are weaker, stipulating that the Counterparty has acquired or will acquire the necessary consent and approvals, including those of the original owners either directly or through a third party designated by it.

- The Counterparties' representations and warranties in the MFAs have become stronger over time. All of the MFAs contain a soft "authority" representation to the effect that the Counterparty has or will have authority to transfer the assets. In the case of MFAs signed with WFOEs, this has evolved to a representation that a third party designated by the Counterparty has or will have authority to transfer. In the case of MFAs signed with BVIs, the representation is to the effect that the forests assigned are subject to a Plantation Rights Certificate or other documents that evidence legal ownership. More recent MFAs include a title representation and a compliance with law representation and, in the case of the three most recent MFAs, a representation that the forests were commercial forest lands not subject to any restrictions on transfer.

Schedule V.B.4.1 sets out a detailed summary of the MFAs terms and Schedule V.B.4.2 provides an unofficial English translation of the Gengma Dai MFA.

5. MFA and BVI Timber Purchase Contract Pricing

The MFAs set maximum prices at which standing timber is to be purchased by the company SF subsidiary within areas covered by MFAs. While the MFAs contemplate the purchase of specified amounts of standing timber measured in mu/Ha. and cubic meters, with an estimated volume, the maximum contractual prices contemplated in the MFAs (generally in cubic meters) varying between 260 RMB per cubic metre and 380 RMB per cubic metre. See Schedule V.B.5.

The MFA maximum price per cubic metre of timber does not differentiate between species of trees. However, the MFAs identify the main species of trees that are to be the subject matter of the specific purchase contracts. All specific BVI timber purchase contracts for timber in that province or region signed after the relevant MFA, regardless of the identity of the Supplier, are generally priced almost exactly to the maximum price set out in the MFA for that province or region.

For example, in March 2007, SF signed an MFA with Gengma Dai setting a cap of RMB 260 per cubic metre. The IC Advisors found that most subsequent BVI timber purchase contracts for Yunnan, irrespective of the Supplier, are priced at exactly RMB 260 or to within several RMB of that. However, two contracts signed in September 2010 for pine and fir, as opposed to broadleaf, are priced at an average of RMB 510 and three contracts signed in the first fiscal quarter of 2011 are priced at an average of RMB 310. Some BVI timber purchase contracts signed before the March 2007 MFA for Yunnan were priced higher than RMB 260. A spot review revealed several contracts priced at around RMB 370.

Similarly, in December 2006, SF signed an MFA with the Hongjiang City Forestry Technology Integrated Development Services Company for Hunan timber, capping prices at RMB 260 per cubic metre. Again, most of the subsequent BVI timber purchase contracts the IC Advisors have seen for Hunan are priced at exactly that price or to within several RMB except for the five aforementioned contracts signed in September 2010 and in the first fiscal quarter of 2011.

Further, in December 2007, SF signed an MFA with Bohu Wood which priced timber in Guangxi at a cap of RMB 380 per cubic metre. All subsequent BVI timber purchase contracts for Guangxi for all Suppliers were priced either at that price or to within several RMB. In contrast, BVI timber purchases signed for Guangxi prior to the signing of the Bohu Wood MFA tended to have higher prices, sometimes as much as RMB 465 per cubic metre.

It appears that the MFAs establish a target price at which the subsequent specific BVI timber purchase. A chart summarising the pricing information for the MFAs from September 2006 onwards is attached as Schedule V.B.5. It is noted that there are some MFAs where the MFA Counterparty itself did not subsequently enter into any specific BVI timber purchase contracts. There are also MFAs under which the Company has not disclosed any subsequent purchases.

Very recently, Management provided the IC Advisors with information, which they indicate pertains to the market pricing of timber in each of the regions that are the subject matter of the MFAs at the time of entry into each of the MFAs. The IC has not yet reviewed or analyzed this information.

6. Summary of Findings on MW Allegations Regarding MFA

The MW Report seems to assume that the MFA Counterparties owned the standing timber that is the subject of the MFAs and that those Counterparties are directly supplying timber under the MFA itself. This assumption, together with the simplicity of the MFAs and the SAIC information on incorporation dates and capital, appears to have led MW to conclude that the contracts must be fraudulent.

In particular the MW Report alleges that the timber purchases under the Gengma Dai MFA were overstated by $800 million primarily based upon information from Lincang City public records about direct sales with associated land rights from Gengma Dai as the seller. The allegations appear to be based on several misconceptions:

- that Lincang City records show all forestry transactions.
- that Gengma Dai was the sole supplier under the Gengma Dai MFA.
- that the supply disclosed by the Company was all purchased in Gengma County.

In respect thereto the IC found as follows:

(a) Based on its interviews the IC does not believe trading in standing timber on a standalone basis is registered with the forestry bureaus. Accordingly, such trading volumes are not likely included in formal government statistics.

(b) Management provided a letter from Gengma Dai confirming that it had sold to SF 520,000 mu (approximately 34,670 Ha.) of standing timber and 190,000 mu (approximately 12,670 Ha.) of plantation land use rights combined with standing timber. The IC reviewed contracts covering such sales. In addition, Gengma Dai indicated it had also facilitated sales of some 3,040,000 mu (approximately 202,670 Ha.) of standing timber by third parties. The IC reviewed contracts for sales of standing timber in Yunnan that at least equalled the indicated volumes although those contracts did not reference Gengma Dai or the MFA. Management explained that the MFA Counterparties did not receive compensation for such arrangements. The IC received no other evidence of MFA Counterparties facilitating supply by other parties.

(c) MW ignores the fact that the MFA with Gengma Dai is to be fulfilled over as long as a ten year period. The various forestry and other economic statistics cited by MW are only for Gengma County and Lincang City whereas the underlying BVI timber purchase contracts disclosed by the Company are for plantations in 18 different counties within six different cities in Yunnan (not just Lincang City). For a table showing purchases of timber assets in Yunnan Province, please refer to Schedule V.B.6.(c).

The MW Report also indicated that SAIC filings by the MFA Counterparties did not reflect the values of the contracted supply in the MFA. The general issue of the accuracy of financial information in such filings is addressed under Section III.C. However, the point in this context reflects a misunderstanding by MW of the framework nature of the MFAs. In practice, only a small portion of the volume stated by the Company to be purchased under MFAs (with the exception of Supplier #3) has actually been supplied by the MFA Counterparty. As a result, the MFA Counterparty's SAIC records, even if accurate, would not be the basis by which to measure the Company's activity levels. As set out above, in the case of Gengma Dai, the role of the MFA Counterparty is explained by Management as also being a facilitator of supply through other parties. Further detailed analysis of the actual supply provided by MFA Counterparties is set out in Schedule V.B.6.

The MW Report suggests that the MFA Counterparties are generally newly incorporated entities. Four of the entities were incorporated more than two years prior to their entry into the MFAs. Three of the MFA Counterparties were incorporated within one year of their entry into the MFAs. The IC believes it is likely that at least some of the Suppliers are specifically incorporated for the purposes of acting as project companies to supply the Company. The MW Report also suggests (based on their SAIC filings) most MFA Counterparties have very modest offices and minimal capital.

Management's response to these points was as follows:

> "For foreign investors looking to invest in standing timber in the PRC, it is natural, and more likely, a necessity, to deal through local agents in a specific geographical area who are either a supplier and/or agent for the suppliers, or both, of standing timber. During the past several years, SF has worked with a small team of agents knowledgeable in their specialized geographical regions within the PRC, who work as intermediaries between SF and the local villagers and collectives, private owners and companies that own the standing timber....
>
> Under a typical "timber acquisition contract" used by SF in the acquisition of standing timber in the PRC, the buyer, a BVI company wholly owned by SF, will acquire standing timber from the suppliers/suppliers' agent who either has expressed authority from the original holder of timber rights to sell or is the holder of the timber rights....
>
> A good suppliers' agent does not need to have a large base nor a strong balance sheet nor a long history, but its key man needs to have extensive and in-depth local knowledge of the timber resources in the region, to have excellent

> relationship with the villages, their inhabitants and their respective elders, familiarity with their local practices and preferences; and a good knowledge and understanding of local rules and regulations, and the enforcement thereof, as well as good working connection with local regulators. None of them needs a posh, western office with high tech gears located in a class A office building at the centre of a major city (as stipulated by MW). In fact, by necessity, they should be located close to the villages, with humble and low cost set up for their offices.
>
> All SF suppliers' agents are selected on the basis mentioned above and are fully independent of and unrelated to SF in any way or form."

Schedule V.B.4.1 identifies the reported registered capital of each of the MFA Counterparties, where available in SAIC filings.

For the purposes of the IC's interviews of certain Suppliers, Management identified the key personnel at such Suppliers which included two MFA Counterparties. Interviews did not necessarily take place at the Supplier's place of business and little documentation was provided. The IC Advisors have observed that the business sophistication of these individuals and the apparent scope of the Suppliers' operations and related operations varied greatly. See Section V.C.12. The IC was unable to gain insight into the scope of capital necessary to act as a Supplier or whether the Suppliers are effectively funding their supply to the Company using deferred payments to underlying suppliers and the funds paid to it by the Company itself. The IC's analysis of BVI Suppliers activity generally is found at "BVI Suppliers General Observations" in Section V.C.13 below.

C. BVI Standing Timber Asset Review

1. BVI Asset Review Process

The BVI review process involved capturing, assembling and organizing into usable form massive amounts of documentation and data.

IC Advisors reviewed:

- 453 standing timber purchase contracts entered into by BVIs for the purchase of standing timber for the period January 1, 2006 to March 31, 2011, of which 337 were originals and 116 were copies. Of these, the timber acquired through 310 outstanding timber purchase contracts remained in the Company's books as at December 31, 2010 (consisting of 304 originals and 6 copies of contracts).

- 579 BVI Entrusted Sale Agreements by which BVIs sold standing timber for the period from January 1, 2006 to March 31, 2011, of which all were copies, see Section V.C.14.

- Documents among BVIs, AIs or parties related to AIs and BVI Suppliers recording set-off payments between the AI parties and BVI Suppliers on behalf of the BVIs for each timber purchase transaction. See Section V.C.14 below.

- 209 (196 originals and 13 copies) forestry bureau confirmations. The confirmations are on letterheads with forestry bureau names and feature Chops that indicate that they had been issued by the corresponding forestry bureau from 49 different forestry bureaus for BVI standing timber acquired from the third fiscal quarter of 2008 onward. 181 originals and 13 copies cover timber acquired before 2011 and the remaining cover timber acquired from January 1, 2011 until March 31, 2011.

- No originals or copies of Plantation Rights Certificates regarding BVI timber supply transactions, either in the name of the Company or other parties who previously owned the standing timber, were available to the IC Advisors. (Forestry bureaus visited generally advised that Plantation Rights Certificates are not available for standing timber only, and in one jurisdiction, are not available at all.)

- For the second fiscal quarter of 2011, 10 original BVI timber purchase contracts and set-off documents corresponding to each (set-off documents are discussed in Section V.C.15 below). No corresponding forestry bureau confirmations for these transactions were available. (Management advised that the Company has developed a new form of forestry bureau confirmation which it intends to obtain.)

The Company organized data including extensive spreadsheets listing:

- Detailed BVI timber assets spreadsheet tracking detailed information from 2006 to the first fiscal quarter of 2011 on BVI timber acquisitions and dispositions including information on contract number, buyer, seller, transaction dates and hectares moving;

- For the second fiscal quarter of 2011, BVI timber acquisitions and disposals including information on contract number, buyer, seller, transaction dates, hectares moving and set-off arrangements;

- Detailed BVI timber asset inventory information as of December 31, 2010 showing detailed flow chart of the asset inventory, a list of plantation timber holding amounts shown on the Company's balance sheet in the 2010 Financial Statements;

- Detailed BVI timber revenue information across a wide range of data points including contract tracking numbers, tree type, location, yield, margins by a number of measures, cost and maintenance costs;

- Email reviews, interviews with forestry bureaus, AIs/Suppliers and Management and other reviews as noted in Schedule IV; and

- The MW Report and the Management MW Response.

The IC observed that the Company possesses extensive and elaborate documentation with respect to its stated BVI standing timber purchases and standing timber sales.

2. BVI Standing Timber Purchase Contracts Reviewed

The IC has reviewed 337 original contracts and 116 copies of contracts for the purchase of standing timber by BVIs for the period of 2006 to the first fiscal quarter of 2011, of which 304 original contracts (452,959 Ha.) and 6 copies of contracts (13,667 Ha.) were for the standing timber held as at December 31, 2010.

Through timber purchase contracts, the BVIs acquire contractual and other rights from the Supplier or if the Supplier is properly acting as authorized agent of the underlying owner, then from such underlying owner, to standing timber purchased by them under such contracts. In the case of BVI standing timber purchases, the Company does not concurrently lease or obtain plantation land use rights.

3. Asset Reconciliation and Tie-in to 2010 Financial Statements

Management provided a detailed reconciliation of the contract purchase prices and amount of hectares shown in the BVI standing timber contracts to the BVI standing timber book value in the 2010 Financial Statements and the Ha. disclosure in the 2010 AIF. The IC reviewed and discussed this reconciliation (which was filed with the OSC) at length with Management. It contained a listing of BVI timber purchase contracts and purchase prices which the IC Advisors reviewed against the actual contracts. The IC is satisfied that the aggregate purchase prices shown in the BVI timber purchase contracts that SF indicated it held at December 31, 2010 reconcile to the book value of BVI standing timber assets of $2.476 billion as recorded as part of the total timber holding shown on the 2010 Financial Statements. The BVI holdings of 466,826 Ha. of standing timber disclosed by the Company as at December 31, 2010 also tied-in to the hectare amounts contained in the BVI timber purchase contracts reviewed by the IC.

This is consistent with the Company's public disclosure reviewed by the IC. Such management reconciliation also contained consolidated information for WFOE purchased plantation standing timber assets and WFOE planted plantation assets at a corporate level.

4. Form of BVI Timber Purchase Contract

The BVI timber purchase contracts are the previously discussed "specific purchase contracts". They are signed between the BVI and Counterparties (i.e. Suppliers). Not every BVI timber purchase contract is signed with a MFA Counterparty. All are written in Chinese and mostly follow a template format with standard wording, even though they may have varying titles. An English translation of an example contract, together with a summary of the terms, is attached as Schedule V.C.4.

5. BVI Supply Contract Payment Process

The BVI timber purchase contracts do not specify the manner in which Suppliers are paid. The Company discloses in Note 4 to its 2010 Financial Statements that as a result of the accounts receivable from the BVI timber purchase contracts being denominated in RMB (which is not freely remittable out of China and its conversion is restricted), the majority of accounts receivables arising from sales by BVIs of standing timber are realized by the Company instructing its AIs i.e., customers/debtors, to settle on behalf of the Company the amounts payable by it to Suppliers for further standing timber purchases and other liabilities denominated in RMB. For more discussion of set-off arrangements between BVIs and AI, see Section V.C.15.

Management advised that no new cash capital had been deployed by SF into the BVIs' standing timber operations since 2004. Rather the proceeds of disposition of BVI standing timber sales were generally redeployed to purchase further standing timber supply using the BVI/AI model. The IC email review indicated certain emails suggesting payment of certain BVI Supplier accounts payable were made by an offshore subsidiary of a customer and the IC has sought an explanation thereof from Management. Management's explanation is set out in Section VI.B.1, below.

6. Timber Rights Diligence Process

(a) Company Surveys

Each BVI timber purchase contract had an accompanying Forest Resource Survey Report ("**Survey Report**") which provides a general introduction of the county where the forest resources contemplated by the survey are located. The IC considered such surveys in connection with the asset verification process. The Survey Report also sets out the general geographic location of the county (including the longitude/latitude coordinates) and describes its natural conditions, total plantation land area, forest covering rate, timber reserves, tree types, tree details such as average height, diameter, density, transport conditions, and social and economic conditions. The Survey Report generally describes the verification method used and sets out the verification results of plantation area (mu), total number of compartments and sub-compartments that compose the plantation, and timber reserves (cubic meters). Although the reference numbers of compartments are included, no centralized system which connects compartments to the location of specific plantations is available to the IC and other location data that would be required to identify specific locations of the plantations is general in nature.

The Survey Reports for the BVI timber purchase contracts are almost exclusively produced by one survey company called Survey Co #1. The use of one company has raised concerns by the OSC. Management has provided an explanation as to its use of the surveys. See Section G of Schedule IX.

Management explained that the Survey Report was part of the due diligence process to determine suitability for acquisition and not a valuation or cash flow analysis. Management indicates in its diligence process summary that it also conducts an internal investment return analysis. The technical data, however, set out in the Survey Report were factors in the pricing of the timber. The most important factor is the volume of timber given that, on the basis of price per cubic metre of timber, the BVI timber purchase contracts are almost always priced in accordance with MFA pricing.

Management has explained that it reviews maps that allow them to locate the properties but does not retain them. The IC has not been able to verify this explanation and notes the Plantation Rights Certificates in the Company's possession in respect of WFOE timber transactions have detailed location descriptions. The IC Advisors were able to verify that most Mandra and SW purchase contracts have attached to them either a map or a description of boundaries or both. It is not clear to the IC Advisors how the Company would be able to identify the relevant areas of timber purchased by the BVIs at the time of sale or harvesting.

(b) Standing Timber Chain of Title Diligence

The IC initially considered and rejected a process of tracing the Company's title back through the chain of supply to the holder of a Plantation Rights Certificate in favour of a forestry bureau confirmation process. The issue was revisited in light of the delays related to obtaining new confirmations, information that emerged about the nature of the confirmations and the OSC request for BVI timber purchase contract attachments.

None of the BVI timber purchase contracts have as attachments either (i) Plantation Rights Certificates from either the Counterparty or original owner or (ii) villager resolutions, both of which are contemplated as attachments by the standard form of BVI timber purchase contract employed by the Company. The OSC expressed grave concerns as to such absence and surmised in its discussions with the IC that such absence is per se evidence of fraud. The IC disagrees with this proposition and has indicated that to the OSC. While there is little question possession of such documentation would provide significant evidentiary comfort that the representations of the Suppliers in the BVI timber purchase contracts were accurate, the IC believes that their absence is evidence of Chinese forestry practices, weak internal diligence practices and weak document retention practices rather than anything else.

The response of Management to the MW Report indicated as part of a comprehensive diligence review process for timber purchases that the Company reviewed underlying Plantation Rights Certificates if timber was purchased directly from the plantation right land owner. If the supply of the timber was through a Supplier who owned the rights, Management indicated the underlying contract by which such Supplier purchased the timber and, if available, the Plantation Rights Certificate of the underlying owner of that property, were reviewed. A complete set of the steps that Management indicated in its response that it followed is set out in Schedule V.C.6.(b).

Ms. Xu Ni (Head of Legal) relayed from Mr. Ip that the operations department reviewed Plantation Rights Certificates and village resolutions as part of the Company's diligence review process but that copies of such documents were not maintained. The reluctance by Suppliers to provide the underlying documents was confirmed during the various visits by the IC Advisors.

IC Advisors, in its e-mail review in August found a detailed SP diligence checklist from 2008. SP is a holding company for many non-Mandra SF WFOE companies that also purchase and sell standing timber. The diligence checklist stipulates that legal chain of title documentation is to be reviewed as part of the purchase of standing timber. Although the timber purchase process is conceptually the same for a WFOE as a BVI (although payment procedures are different), the document does not specify that the outlined diligence process is applicable to purchases by the BVI group. No similarly detailed document specifically addressed BVIs. An accounting flow diligence checklist for the BVI purchases indicates that Messrs. Chan and Ip were closely involved in BVI purchase planning and in approving individual purchases at several stages including selecting the BVI to make such purchases.

In response to a detailed OSC request, Management provided an updated report on its diligence process that evolved from prior explanations. Management indicated that when buying from a Supplier who was authorized by the original owner, it did not view Plantation Rights Certificates and may only view parts but not all of the underlying contract relevant to its purchase. Further, when buying from a Supplier who purchased from another Supplier, Management indicated that it relies upon Supplier representations without viewing underlying contracts or Plantation Rights Certificates. Management indicated that they may randomly check villagers' authorizations. No evidence was produced to support the Management explanation.

Management also indicated in its response to the OSC that it had visited certain forestry bureaus to view the history of the area in which timber is purchased and advised of SF's intention to purchase. It is unclear to the IC the extent and nature of the diligence that Management could have undertaken at forestry bureaus. The IC interviews with forestry bureaus indicate none maintained any records of standing timber-only transfer transactions, although most acknowledged they had issued Plantation Rights Certificates for land ownership.

In the course of assisting the Company to inspect specific transaction documents in connection with the 2011 second fiscal quarter report, it became apparent to the IC Advisors that the BVI timber purchase contracts and BVI timber sale contracts for the 2011 second fiscal quarter were only documented at quarter end. No forestry bureau confirmations were obtained in the second fiscal quarter of 2011. (Management advised that the Company has developed a new form of forestry bureau confirmation, which it intends to obtain.) Forestry bureau confirmations in respect of the 2011 first fiscal quarter purchases and the related BVI purchase contracts were provided to the IC Advisors in June 2011 for review.

The IC requested on a number of occasions commencing in late July that Management seek copies of the attachments to the BVI purchase contracts from the Suppliers. The Company provided copies of correspondence dated September 20, 2011 in which it made requests for the information but has advised that none has been forthcoming. In advance of and at each Supplier interview, requests for documentation including the attachments to BVI timber purchase contracts were made but no pertinent documents were produced by any BVI Supplier even though some BVI Suppliers undertook at various points to provide them.

7. Plantation Rights Certificates Not Generally Available for Standing Timber Alone

As noted above, under Chinese national forestry law (see Section III.A), Plantation Rights Certificates, a document evidencing ownership issued by governments in China (through local forestry bureaus), should theoretically be available for standing timber.

As noted above, the BVI standing timber contracts contemplate either a Plantation Rights Certificate or other valid ownership certification being held by the Counterparty or the original owner of the Counterparty in assisting the BVI in registering ownership of timber.

However, Management indicates that in practice it is not able to obtain Plantation Rights Certificates for standing timber purchases when no land transfer rights are transferred. Nine forestry bureaus visited by the IC generally advised that Plantation Rights Certificate's were not available to a holder of interests in standing timber only. Very recently, one official at one forestry bureau suggested that Plantation Rights Certificates may be available for standing timber alone. However, he advised that the forestry bureau had never issued such a certificate. This suggestion is also inconsistent with all of the other information received by the IC in respect of BVI standing timber and the availability of such Plantation Rights Certificates has not been tested.

While this is not definitive evidence that Plantation Rights Certificates are not available anywhere in China for standing timber alone, the IC has concluded that proof of ownership of standing timber through possession by SF of a Plantation Rights Certificate for standing timber interests alone is not currently available in the jurisdictions in which SF has been conducting business.

8. Forestry Bureau Confirmations

(a) Existing Confirmations

The IC is satisfied that it is not yet possible to obtain Plantation Rights Certificates for standing timber alone in most, if not all jurisdictions in which the Company is doing business.

Management indicated that, in the absence of Plantation Rights Certificates, it has sought further acknowledgements from relevant forestry bureaus in the form of "confirmations" that it has rights in the timber. The Company has previously obtained legal opinions from the Chinese law firm of Jingtian & Gongcheng regarding the issuance of such confirmations. According to the legal opinions, if in a particular locality the work of registering plantation rights and issuing the new format of Plantation Rights Certificates has been delayed, and it is not possible to obtain the old form of Plantation Rights Certificates, and the BVI needs to prove the legality of its plantation rights to a third party, the BVI may apply to the competent department in charge of forestry administration at county level or above where the timber is located for the issuance of a "certification letter or confirmation letter" to prove the lawful rights that the BVI holds over the timber, and in such a case, such a certification letter or confirmation letter may be seen as valid proof that the BVI has the right to own the timber. Management has advised that they relied upon such opinions and also believe that these confirmations provide additional comfort in the event of any dispute.

The Company provided and the IC reviewed 196 originals and 13 copies of existing confirmations for the period of 2006 to the first fiscal quarter of 2011 in the possession of the Company, of which 181 originals (452,958 Ha.) and 6 copies (13,868 Ha.) comprising all of the 466,826 Ha. of the Company's disclosed BVI standing timber holdings as at December 31, 2010.

The BVI confirmations were in the form prepared by SF outside counsel and all were printed on letterheads with forestry bureau names and featured Chops that indicate that they had been issued by the corresponding forestry bureau. The confirmations reviewed are substantially of the same standard form, which include the following key terms:

- forestry bureau confirms that it has reviewed the BVI timber purchase contract before issuing such confirmations;

- forestry bureau approves the contract arrangement under which timber is transferred to the BVIs;

- forestry bureau agrees to issue Plantation Rights Certificates to the BVIs and register its timber ownership according to the schedule of municipal or city government implementation for Plantation Rights Certificates; and

- forestry bureaus confirm that subject to applicable laws the BVI is entitled to harvest, transport and sell the timber once the timber grows to full size.

Attached to each confirmation is a chart setting out the timber stipulated in the corresponding BVI timber purchase contracts. Because SP WFOEs also obtain confirmations for both standing timber and leases, the wording of SP WFOE confirmations is different.

Further, it is apparent from documentation found in email searches that the Company, at least in some instances, prepared the actual forestry bureau confirmations on notional forestry bureau letterhead on which a forestry bureau Chop was then obtained. Management explained that it created the notional letterhead copies, as the issue of the confirmation was not a statutory or mandated action, but rather a favour to assist the activities of the Company. Accordingly, they had to arrange all the logistics to obtain the confirmation. The IC Advisors did not find any evidence, through its email searches or otherwise, of the Company having falsified the Chop on forestry bureau confirmations.

There are indications in emails and in interviews with Suppliers that gifts or cash payments are made to forestry bureaus and forestry bureau officials. The reasons are not clear although two Suppliers noted benefits were provided for the issuance of confirmations.

Affirmations of existing confirmations were not initially sought by the IC for the reasons set out below. Eventually certain affirmations were sought and the results are described under Section V.C.9 - "Summary Outcome of Forestry Bureau Visits" below.

(b) New Form of Forestry Bureau Confirmations sought by the IC

After input from Management, the IC concluded that it would be disruptive to SF's forestry bureau relations to reconfirm the existing confirmations. A new form of confirmation with a more limited scope (i.e. did not address issues such as transportation, harvesting, and sale, as SF did not have these rights) was agreed upon with Management and sought from forestry bureaus. It is attached as Schedule V.C.8.(b).

The IC Advisors determined that it was appropriate to initially focus on BVI forestry assets in Yunnan Province in its asset verification process because Yunnan was the focus of the Muddy Waters allegations pertaining to the Company's plantation assets, and the vast majority of the Company's book value and net income resides in the BVI standing timber business. Yunnan Province represented 186,700 Ha. of the Company's total plantation assets as at December 31, 2010 and 201,673 Ha. as at March 31, 2011. The IC Advisors conducted an analysis to select forestry bureaus at which new confirmations would be sought. Management arranged visits at each of the forestry bureaus, with the exception of Yunnan FB#8 which was originally selected by the IC Advisors but not yet visited. This focus was later broadened to include BVI forestry assets elsewhere and WFOE forestry assets both Mandra WFOEs and non-Mandra WFOEs.

9. Summary Outcome of Forestry Bureau Visits

The IC Advisors attended meetings with ten forestry bureaus or associated bodies between July 7 and November 12, 2011. The process by which meetings were arranged and the scheduling of those meetings took substantially longer than expected by the IC. Management explained that these delays were due to local holidays, changes in officials, personal holidays of officials, official forestry bureau requirement for background survey diligence and the adverse publicity surrounding SF, and conflicting demands on Management's time involved in both assisting the IC and conducting the Company's business.

The forestry bureaus responsible for Plantation Rights Certificates and from whom the Company has confirmations are located in the areas in which the Company assets are located, and visits to such locations involved significant time and travel, including multiple modes of transportation, often to somewhat remote locations in southern China.

The IC, on the advice of Management as to the importance of its forestry bureau relationships and on the advice of the IC Advisors that some form of introduction from the Company was a necessity, had Management arrange all of the visits and follow-up. The IC had little visibility into that process. Management attended and participated in all the forestry bureau meetings. There was sometimes disagreement with Management as to the tenor and findings of the meetings. The details of the IC process around the forestry bureau meetings is set out in Part IV. The status and results of these meetings to date are set out in narrative format below and a table in Schedule V.C.9.1. Summaries of the meetings with forestry bureau officials at the individual forestry bureaus are provided in Schedule V.C.9.2 and more complete notes of the interviews are available to the Board for its confidential review.

New confirmations representing a total of 54,781 Ha. of BVI standing timber were issued by two forestry bureaus from Yunnan selected by the IC Advisors (Yunnan FB#9 (14,433 Ha.) under Yunnan FB#6 (40,348 Ha.)). The visit to the Yunnan FB#2 resulted from the advice of the Yunnan FB#1 that it would not be able to issue a confirmation but that underlying county forestry bureaus may do so.

Two new confirmations representing a total of 75,892.71 Ha. of BVI standing timber were issued by two organizations related to forestry bureaus selected by Management. These were Hunan Forestry Entity #1 in Hunan Province (60,696.88 Ha.) and Yunnan Forestry Entity #1 in Yunnan Province (15,195.83 Ha.). The IC understands that these organizations are sponsored by the Hunan FB#2 and Yunnan FB#7, respectively.

Each of the four new confirmations varied from the form of confirmation agreed upon by SF's in-house counsel and the IC Advisors. Some of the material differences between the old confirmations and the new confirmations include the following:

- The new confirmations only state that SF BVIs have contractual rights and do not discuss other ownership characteristics.

- The Hunan Forestry Entity #1 issued a new confirmation (**"Hunan Forestry Entity #1 Confirmation"**) corresponding to 60,696.88 Ha.[14] which states that standing timber transactions comply with national and provincial laws, regulations and policies and such contracts are lawful and effective.

- The three Yunnan confirmations confirm the contract and Ha. information set out in the table of plantation rights as well as confirm that the BVI standing timber purchase contracts are lawful and effective.

There were indeterminate outcomes from several forestry bureau visits as follows:

- One forestry bureau in Yunnan Province (Yunnan FB#4) agreed to issue a new confirmation during the IC Advisors' visit subject to its completion of certain due diligence exercises, which it indicated would take approximately one month to complete from July 22, 2011. As of the date of this report, the new confirmation has not been received.

- Two forestry bureaus in Yunnan Province Yunnan FB#3 and Yunnan FB#5) declined to issue new confirmations relating to a total area of 95,550 Ha., as at December 31, 2010 or 121,062 Ha. as at March 31, 2011, referring the IC to the county level forestry bureau within that area. Management later advised that the forestry bureaus were willing to issue the confirmations after conducting some due diligence. As of the date of this report, new confirmations from these two forestry bureaus have not been received. In the case of the Yunnan FB#5, Management arranged for the issuance of the confirmation in relation to Yunnan Forestry Entity #1 as noted above.

Existing confirmations representing a total of 90,905 Ha. of BVI standing timber were acknowledged by two forestry bureaus as having been issued by that forestry bureau. The reconfirmation process was subject to certain caveats noted below, including that Management selected the forestry bureaus at which reconfirmations were sought. A brief description of the two visits follows below:

- One forestry bureau in Hunan Province (Hunan FB#1) affirmed the issuance of certain samples of confirmations prior to the MW Report corresponding to BVI plantations with a total area of 13,845 Ha. as at December 31, 2010. At the forestry bureau meeting, the party to whom Management introduced the IC Advisors affirmed the authenticity of the confirmation. Subsequent to the meeting, the IC Advisors determined that the person was a recently retired former vice-chief who had been briefly on the SF payroll after the announcement of his retirement, receiving a monthly consulting fee. Management provided evidence of the arrangement and of termination of employment.

- One forestry bureau in Guangxi Province (Guangxi FB#1) affirmed the issuance of certain confirmations corresponding to BVI plantations with a total area of 77,060 Ha. as at December 31, 2010. A single official attended the meeting.

---

[14] The hectarage of 60,696.88 Ha. differs from the total shown on the Hunan Forestry Entity #1 Confirmation, which shows 60,707 Ha. The difference appears to arise from an arithmetic error.

The new confirmations and acknowledged existing confirmations also cover certain WFOE standing timber assets and these are detailed under Section V.3.(d). Other information obtained from forestry bureaus:

- The level of transparency as to the nature of the diligence undertaken in issuing new confirmations or examining and reconfirming existing confirmations did vary, ranging from confirmation of an extensive review of underlying documentation (including confirmation of discussion of the underlying Suppliers and the review of such Suppliers' rights, including underlying Plantation Rights Certificates in the names of Suppliers) to no indication as to the methodology by which (or if) diligence was undertaken prior to the issuance of a confirmation.

- The interviews indicate that forestry bureaus have varying levels of completion in different Provinces with respect to the issuance of Plantation Rights Certificates to village collectives and other parties residing in the relevant area. All forestry bureaus visited by the IC Advisors in Yunnan Province and one in Hunan Province claimed to have issued Plantation Rights Certificates in respect of all plantations under their jurisdiction. In the case of the only forestry bureau visited in Guangxi, the IC Advisors were told that not many Plantation Rights Certificates (less than 3% in terms of plantation area) had been issued by it. The IC inquired about the ability to review Plantation Rights Certificate registries that are ostensibly available to the public. In some instances, it was indicated that no Plantation Rights Certificate registry exists. At other times, it was indicated that the Plantation Rights Certificate registry existed, but could not be reviewed or was kept at the county level rather than the city level. A variety of other reasons were provided as to why the Plantation Rights Certificate registry could not be seen at the time of the visit.

- All of the forestry bureaus acknowledge the activity of SF in their jurisdiction. A number expressly indicated that foreign offshore companies were not entitled to obtain Plantation Rights Certificates; but most expressly acknowledge that a foreign company was able to buy timber and sell timber.

- It was also clear that the forestry bureaus were of the view that the only means to establish legal rights with respect to the sale of standing timber alone was through contract.

- A number of the forestry bureaus indicated they had active relationships with SF and were aware of its activities as a buyer. In two instances the forestry bureau confirmed that SF was the largest owner of plantation forest areas within their jurisdiction.

- During the Hunan FB#2 visit, the party with whom the IC Advisors met advised that a specific vice-chief of the forestry bureau had been assigned to work closely with SF and that whilst he still drew a basic salary from the forestry bureau he also acted as a consultant to SF to assist SF in conducting its business. The IC Advisors were told that this arrangement had been in place for several years and a similar arrangement was in place between another forestry company and the forestry bureau at the direction of the local government. IC Advisors have confirmed that according to the Company's records the vice-chief has appeared on the payroll since January 2007 with a monthly payment of RMB 15,000 which is likely to be significant compared with his forestry bureau salary.

- The IC Advisors were informed by one of the forestry bureaus (Yunnan FB#2) that the harvest of plantations belonging to SF in that county is very difficult, if not impossible, to be approved since the forest of that county is located in the "Natural Forest Preservation Zone". The forestry bureau also indicated that there could be a few exceptions, namely the "Middle or Lower Output Forest Replanting Scheme". It is not apparent whether standing timber purchased by SF qualified as "Middle or Lower Output Forest".

10. Introduction to Supplier and AI Interviews

The IC Advisors have attended meetings with Suppliers and AIs between September 22, 2011 and October 25, 2011. The IC concluded that the only means by which Supplier and AI interviews could be arranged was through Management. Much delay was encountered in arranging such meetings; in part, Management advised, due to concerns about confidentiality and in part due to the notoriety of the matter, particularly after the OSC announced the CTO. Certain limited assurances were eventually provided by the OSC. All such meetings were also attended by Management with the concurrence of the IC. Apart from an initial meeting with Supplier #1 at the request of Management and the concurrence of the IC, the interviews were led by the Company's counsel, BJ.

The purpose of these meetings was to obtain information relevant to certain allegations made by Muddy Waters – specifically ownership of timber, the genuineness of the BVI purchase and sale transactions and allegations of related party relationships.

The IC Advisors established and provided an interview protocol, a detailed sample of transactions and a list of specific documents to SF which the IC Advisors understand were provided to Suppliers/AIs in advance of the meetings.

The IC Advisors created a detailed set of questions to be asked by BJ at these meetings. The IC Advisors were provided with additional questions from the OSC to be asked by BJ at these interviews. The IC Advisors posed some additional questions at the meeting.

The interviewees declined to show any evidence of financial transactions, notwithstanding the request provided to them. The reasons given for not producing financial documents included avoiding scrutiny regarding tax, media exposure, and that SF should have copies of certain of the same documents.

The limited sample documents provided by certain of the interviewees such as Plantation Rights Certificates and villager's resolutions were not the documents requested in the interview protocol and could not be tied back to the sample transactions.

Many of the responses of the interviewees were similar – for example, no financial records were given, no copies of documents presented could be taken and the interviewees were not prepared to discuss any aspect of any other companies that deal with SF that they control or that appear to be in the same corporate group or any transactions with other parties, including any other

Suppliers and AIs. The SAIC filings indicate a number of accounts payable and receivable as well some minority cross shareholdings amongst Suppliers and AIs.

Members of Management and Supplier/AI employees attended all meetings with the IC Advisors but one meet and greet with Supplier #1.

The IC and its Advisors are unable to compel the AIs and Suppliers to cooperate or to produce documents.

With the exception of the Supplier Supplier #20, none of the meetings took place at the business addresses of the AIs and Suppliers provided by SF or the registered addresses noted in the relevant SAIC filings.

With respect to Supplier #3, the meeting took place at substantial business premises of what the IC Advisors understand to be a Supplier #3-related entity.

11. Summary of Supplier Interviews

During September 2011 the IC Advisors interviewed four of nine selected Suppliers (Supplier #3, Supplier #1, Supplier #20 and Supplier #19). Summaries and detailed notes in respect of each visit are also available to the Board for its confidential review.

In preparation for the Supplier interviews the IC Advisors reviewed SAIC filings for the Suppliers and AIs and identified numerous potential relationships between AIs and BVI Suppliers such as payables and receivables amongst them, cross personnel appointments and cross minority shareholdings. This raised questions amongst the IC Advisors as Mr. Allen Chan had previously explicitly denied knowledge of any relationships between BVI Suppliers and AIs or between BVI Suppliers/AIs and the Company. Details of these relationships are discussed below at Section VI.B. Very recently, Management provided information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

Interviews were held with Supplier #1 and Supplier #3, which are Suppliers to BVIs and WFOEs, and Supplier #20 and Supplier #19, which are Suppliers to WFOEs only. Supplier #3 also purchases logs from the Company's log import trading business segment and is not an AI of the plantation fibre business as characterized by MW. All of the Suppliers interviewed indicated that they did business at arm's length with the Company and that there were no common employees or shareholders between them and the Company. However, three of the four Suppliers interviewed confirmed that they had personnel that were former SF employees. These relationships are discussed below at Part VI.

The Suppliers generally confirmed the levels of business activity between them and the Company but none of the Suppliers of BVI timber produced any documentation evidencing receipt of funds from the Company's AIs or any other parties or relevant chain of title documentation. A few sample documents such as contracts, villagers' resolutions, Plantation Rights Certificates and/or confirmations were provided by Supplier #1, Supplier #20 and Supplier #19. However, apart from the five Supplier/SF contracts provided by Supplier #20 and one contract provided by Supplier #1, none of the supporting documentation provided could be reconciled with transactions selected for review by the IC Advisors based on the information available on the documents. Nor could this documentation provide assistance in understanding movements of funds between these Suppliers and the relevant parties. Some interviewees did acknowledge doing business with other Suppliers and/or AIs.

The IC Advisors have also found additional information which suggests connections between former SF employees, Suppliers and AIs. (see Schedule VI.B.1.1). This information has been provided to SF Management for comment.

Supplier interviews indicated that the Supplier due diligence process for the purchase of timber is likely less rigorous than that of the Company. A number of the Suppliers advised that they used rotating project companies and under-reported revenue, all with the purpose of minimizing taxes payable. Additionally, some Suppliers indicated that they only traded in standing timber and avoided applying for Plantation Rights Certificates also in an effort to minimise tax payable. The table in Schedule V.C.11 sets out a summary of the outcome of Supplier and AI visits to date.

Very recently, Management provided information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

12. Suppliers Site Visits

In addition to the Supplier interviews, the IC instructed the IC Advisors to conduct unannounced site visits for a small sample of these companies to verify their existence at the addresses recorded in their SAIC filings, or at an address taken from the Company's records. Certain of these visits are described in more detail in Schedules V.C.11.

A selection of Suppliers was identified that would enable the IC Advisors, where applicable, to combine this manner of testing in conjunction with travel to various locations for planned Supplier visits, or to visit locations within a travel radius of two hours or less of an IC Advisor's office.

During the period from October 18, 2011 to October 20, 2011, the IC Advisors performed site visits to the following Suppliers offices based on addresses provided by SF and company information included in SAIC filings:

- Supplier #1 was a supplier to BVIs and WFOEs from 2007 to 2010. Four locations were identified in the surrounding area. Three of the locations were no longer occupied by Supplier #1 and the fourth address was incorrect. The IC Advisors were provided with a new address from individuals identifying themselves as Supplier #1 personnel. A sign at the site indicated that Supplier #1 had offices at this new location. One of the three Supplier #1 interviews took place at a business location in Chongqing, which appeared to involve newly planted forest plantations, although this location was not independently identified as being owned by Supplier #1.

- Supplier #10 was a supplier to BVIs in 2007 and 2008. Two locations were identified in the surrounding area. Offices belonging to Supplier #10 could not be found at either location.

- Supplier #11 was a supplier to BVIs in 2006 and 2009. Two locations were identified in the surrounding area. One address was not sufficiently specific to be located and the second address was not a corporate office.

Results of these site visits have been summarized in Schedule V.C.11.

13. BVI Suppliers General Observations

A chart showing the Suppliers to the BVIs from 2002 through 2011 by volume of transactions is attached as Schedule III.C. In that period the BVIs purchased from as few as four Suppliers to as many as eight Suppliers in any given year. The length of time the BVIs have dealt with any one Supplier has not exceeded four years despite large volumes of transaction.

(a) Suppliers as Project Companies

Management has suggested that the use of limited life project companies is not uncommon in China. The IC was advised that Mr. Chan undertook to identify the conglomerate structure behind these Suppliers in August, 2011. Such information was provided very recently. It identifies certain persons as supporting certain of the Suppliers and in many cases the same person supporting multiple Suppliers. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

Further, interviews with certain Suppliers have supported the notion that the Suppliers are part of a conglomerate. However, such Suppliers have declined to reveal the identity of such entities or their backers with a limited exception and that person is one of the people identified by Mr. Chan. The SAIC information on the shareholders of the various BVI Suppliers does not point to a consistent pattern of direct replacement of successive Suppliers with the same shareholders. However the use of nominee shareholders has been alluded to by many of those interviewed so the true beneficial ownership of the Suppliers may not be discernable through SAIC filings.

The MW Report noted in some instances the low capitalization based on SAIC filings and unsophisticated offices of some Suppliers. Management's general response to such allegations is reproduced in Section V.B.6, "Summary of Findings on MW Allegations on MFA". If certain Suppliers are part of a group of companies, the level of capitalization of Suppliers as project companies would be less of an issue as they would be supported by their respective parent company with greater capital resources. The timing of payments by the Suppliers to underlying landholders or other Suppliers and whether such Suppliers utilize SF payments to them in order to pay underlying owners or suppliers is not known to the IC.

(b) Local Knowledge

Management also suggested that the Company relies heavily on Suppliers due to their unique local knowledge on contacts necessary to aggregate and sell plantation assets in their respective provinces. That appears generally correct for the MFA Counterparties with one exception. Upon reviewing the timber purchase agreements, the IC Advisors observed that several of the Suppliers conduct business with the Company in multiple provinces rather than in one specific location that would require focused local knowledge. For instance, while Supplier #6 has its head office in Jiangsu Province, it has sold timber to the BVIs in five different provinces including Guangxi, Guizhou, Heilongjiang, Hunan and Yunnan.

(c) Payments to Suppliers

The IC Advisors found limited anecdotal evidence in an email in the Company records that suggested the Supplier mark-up on two contracts was in the range of 158% to 170%.

Payments to BVI Suppliers occur by way of set-off from Company customers. These are all documented by set-off documents although the Suppliers and AIs interviewed declined to provide the IC Advisors with any independent evidence of movement of funds evidencing payments. The basis for the price paid to Suppliers by the Company has not been determined although all the Suppliers interviewed and Management maintain the relationship between the Company and Suppliers is at arm's length and all pricing on market terms.

Very recently, Management provided the IC Advisors with information that it indicated supported that MFAs were priced at then market prices for the regions to which such MFAs applied. Such information has not been reviewed by the IC Advisors or independently verified.

14. BVI Standing Timber Sales Contract Reviewed

(a) Contract Review

The IC also reviewed 579 copies of contracts for the sale of BVI standing timber for the period of 2006 to the first quarter of 2011, of which 167 sales contracts with an aggregate sale price of approximately $1.327 billion related to sales in 2010. As described below, these 2010 sales contracts have been reconciled to the revenue of $1.327 billion in respect of the sale of BVI standing timber recorded on the 2010 Financial Statements.

(b) BVI Standing Timber Revenue Reconciliation

The IC Advisors established procedures to assist the IC in determining the facts related to revenue reconciliation issues. The IC Advisors have performed the following procedures to date:

- Obtained understanding of revenue streams and revenue recognition policies as applied by SF across its operating segments; and
- Obtained a listing of all transactions and, for standing timber, related purchase and sales agreements, and have tied revenue reported in the 2010 Financial Statements for BVI timber sales to the sales prices shown in the underlying BVI timber sales contracts.

15. Terms of BVI Timber Sale Agreements

As disclosed in the 2010 Annual Report, the BVIs sell standing timber through Entrusted Sale Agreements. These are contracts signed between the BVIs and the AIs. The IC reviewed 579

BVI Entrusted Sale Agreements by which BVIs sold standing timber for the period from January 1, 2006 to March 31, 2011, of which all were copies. All are written in Chinese and mostly follow a template format with standard wording. These agreements are also referred to as "AI Agreements". The IC Advisors observed the following regarding such contacts:

(a) Agency vs. Principal Transactions

The AIs are Chinese incorporated companies that engage in timber trading. In the preamble to the Entrusted Sale Agreements, it is stipulated that the BVI "entrusts" the AI to sell the standing timber on its behalf. AIs are sometimes described by SF as "selling agents".

Under a typical Entrusted Sale Agreement, the AI is entrusted by the BVI to sell the BVIs standing timber assets located in China on its behalf. Notwithstanding its stated role as an "agent", the Entrusted Sale Agreements stipulate that the AI is itself directly liable for paying SF. That is, the AI's obligation to make payment to SF is not conditional upon the AI on-selling the standing timber to its customers. The AI does not receive any commission or fee from SF. It appears in reality that the Entrusted Sale Agreements are principal-to-principal contracts and do not appear to involve an actual "agency" arrangement. During meetings with AIs in September and October 2011, representatives from the AIs confirmed to the IC Advisors that they do not act as "agents" for SF and are responsible for finding their own customers. The IC understands that Management has treated the BVI sales transactions as being complete upon the sale to the AIs for revenue recognition process.

(b) Payment through Set-Off

Payment terms may vary but typically involve payment of 20% of the total sale price within 60 days of signing the Entrusted Sale Agreement, an additional 40% within 150 days, and the balance within 270 days of signing. Upon signing, the AI has full powers and rights to dispose of and handle the standing timber, and simultaneously, all risks in the standing timber pass to the AI. This confirms that the Entrusted Sale Agreements do not involve an agency arrangement.

In practice, proceeds from the Entrusted Sale Agreements are not paid to SF but are held by the AIs as instructed by SF and subsequently used to pay for further purchases of standing timber by the same or other BVIs. The AIs will continue to hold these proceeds until the Company instructs the AIs to use these proceeds to pay for new BVI standing timber purchases. No proceeds are directly paid to the Company, either onshore or offshore.

When an AI makes payment for a new BVI standing timber purchase, the funds used to make payment may originate from the proceeds of multiple Entrusted Sale Agreements. However, the Company's accounting records show that any set-off payments made by an AI are deemed to contribute to either the partial or complete settlement of the account or accounts receivable from an AI in the books of a BVI that is earliest in time. That is, the accounts receivable from any one particular AI in the books of a BVI are always settled in chronological order while any one account receivable may be settled through one or more set-off payments by the AI for new BVI standing timber purchases. Examination of the accounting records of the Company indicate that most AIs with regular entrusted sales transactions with the Company will at any one time have multiple accounts payable to the Company.

Further, the BVI on whose behalf an AI holds proceeds from an Entrusted Sale Agreement may request that AI to use those held proceeds to pay for a new standing timber purchase by a different BVI. For example, the BVI Suri-Wood Inc. entered into 131 standing timber purchase transactions from 2006 to 2008 but has had none since. Proceeds from the sales of standing timber purchased through these 131 standing timber purchase transactions have been used to pay for new standing timber purchase transactions by 18 new BVIs established from 2009 onwards, including Amplemax Worldwide, Ace Supreme and Glory Billion International. The 18 new BVIs have yet to have any sales.

In this way, proceeds from the Company's BVI timber sales have been re-invested on behalf of SF to expand its asset base in China. This re-investment of the proceeds from standing timber sales by the BVI is confirmed in Note 4 to the Company's audited financial statements set out in the 2010 Annual Report. SF refers to such arrangements as "set-off arrangements".

(c) Set-off Documents

Set-off arrangements are not stipulated in the Entrusted Sale Agreements themselves but rather are stipulated in separate documents which SF refers to as "Set-off Documents". The set-off documents are organized into sets and use standard wording and formatting, with each set containing the following documents:

- written instructions from a BVI with accounts receivable from an AI for that AI to make payment to a particular Supplier as payment for a new timber purchase by that same BVI or another BVI. These written instructions feature the name of the BVI at the top and are dated, signed and stamped and set out the amount to be paid;
- written notification from SF to the Supplier that payment is being made through the AI via set-off on behalf of the purchasing BVI. This written notification features the name of the BVI at the top and is dated, signed and stamped and set out the amount to be paid;
- written confirmation from the AI that payment has been made to the Supplier as requested by the instructing BVI. This written confirmation features the name of the AI and is undated and stamped and sets out the amount and date of payment; and
- written confirmation from the Supplier to the instructing BVI and paying AI that payment has been received from the AI. This written confirmation features the name of the Supplier and is dated stamped and sets out the amount and date of payment received.

The set-off documents are only produced and stamped after the Company enters into a new BVI Timber Purchase Contract and therefore reflect the payment of the consideration for this new BVI Timber Purchase Contract using proceeds from earlier Entrusted Sale Contracts held by the AIs on behalf of the Company. The set-off documents do not explicitly relate to any particular Entrusted Sale Contract and are not a record of BVI sales transactions. Apart from the Entrusted Sale Contract itself, and until set-off documents are produced pursuant to a new BVI timber purchase, there is no other document produced dealing with payment or settlement of BVI timber sales.

The IC Advisors have received copies of the Set-off Documents related to all the BVI standing timber purchase transactions between the first fiscal quarter of 2006 and the first fiscal quarter of 2011. However, the IC Advisors have not been provided with any documents showing movement of money to confirm that such set-off arrangements have been carried out. During meetings of the IC Advisors with AIs and Suppliers, representatives from the AIs and Suppliers declined to produce such documents showing movements of money. Common reasons cited for declining to produce documents included "tax reasons" and sensitivity towards the MW allegations and the resultant publicity. Further, some AIs visited stated that they may not in fact make payment themselves as instructed by SF but would instead arrange for other parties (**"fourth parties"**) to make payment on their behalf. Those fourth parties may then instruct "fifth" or "sixth" parties to make payment.

In this situation, the Suppliers receiving payment will sometimes instruct its own "fourth" parties to receive payment on its behalf. All the AIs interviewed stated that these fourth parties are unrelated to SF. A common reason cited to explain the use of such expanding set-offs was for tax reasons but all AIs declined to discuss exactly how such use of fourth parties reduce taxes payable. During the meeting with Supplier #1, its legal representative explicitly stated that it would always instruct another party to receive payment from the AIs on its behalf. Reasons given for this arrangement included tax minimization and the fact that Supplier #1 did not have transactions with the AIs and therefore would be unable to account for the receipt of payment from the AIs.

(d) Tax Arrangements

The Entrusted Sale Agreement expressly provides that all taxes and fees that are to be borne by the BVI are to be withheld and paid by the AI to the appropriate tax bureau on behalf of the BVI. However, SF has not provided any documents to the IC Advisors showing that the AIs had in fact paid tax on behalf of any BVIs. Management has advised that they have not requested confirmations from the AIs with respect to payment of taxes. The AIs also declined to produce any such documents during meetings although several confirmed that they made such payments. Others either declined to discuss the issue of paying tax on behalf of SF or indicated that they were not aware of the details of whether tax is paid. The Company has recorded in its audited balance sheet as at December 31, 2010 a provision of approximately $160 million in respect of any contingent liability it may have with respect to these tax liabilities.

(e) Harvesting Timber

All the Entrusted Sale Agreements impose an obligation on the AI to return the plantation land within a stipulated period. Some additionally impose an explicit obligation on the AI to harvest the timber within a stipulated period. It should be noted that there are harvesting quotas imposed by forestry bureaus in many areas. Management are of the view that these quotas are subject to negotiation. Harvesting license requirements are also stipulated in Chinese laws. The IC Advisors have not received any information confirming that any standing timber sold through Entrusted Sale Agreements has been harvested. The AIs and Suppliers also could not confirm that any BVI standing timber has been so harvested. The ability of the Company to exercise its preferential option to lease such land for replanting is premised on the harvesting thereof.

Further, the IC Advisors have seen no evidence of SF exercising this right in respect of BVI standing timber holdings.

(f) Attachments

The Entrusted Sale Agreements do not include a schedule of attachments and therefore, provide no insight as to what underlying documents if any SF produces to the AI when the sale transactions occur. A number of AIs indicated that they did their own diligence investigations but the nature and extent of that investigation was not detailed; others have indicated that when the AIs purchase the timber, they usually review the purchase contracts between SF and the Suppliers.

16. Summary of AI Interviews

The IC Advisors conducted interviews with four of five selected AIs (AI #2, AI #4, AI #3 and AI #1). Summaries and detailed notes in respect of each visit are also available to the Board for its confidential review.

All of the AIs indicated in the interviews that they did business at arm's length with the Company and that there were no common employees between them and the Company. However, several AIs confirmed that they had personnel that were former SF employees. Further, several AIs admitted to having or to have had connections with Suppliers but denied that these connections affect the arm's length nature of transactions with SF. These connections are discussed in detail below at Section VI.B.

The AIs indicated that they bought standing timber from SF and sold it to their own customers. As noted above, they do not act under the direction of SF and are not in essence "agents". Accordingly, they are not paid any commission or agency fees.

The AIs generally confirmed the levels of business activity reported by the Company but none produced any documentation of fund transfers to the Company or its Suppliers. Common reasons cited for declining to produce documents was sensitivity towards the issues raised by MW and tax.

Like with the Suppliers, AI interviews suggested that the due diligence process undertaken by AIs is likely less rigorous than those of the Company. All AIs indicated that they only traded in standing timber and therefore did not rely on Plantation Rights Certificates. AIs reported that they instructed their personnel to perform site visits and inspect timber offered by SF and review contracts between SF and earlier suppliers but without keeping copies of such documents. It was not clear if any AIs visited forestry bureaus to make inquiries.

Most AIs indicated that they did not harvest any timber and were not aware if their customers applied for harvesting permits.

17. AI Site Visits

In addition to the AI interviews, the IC instructed the IC Advisors to conduct unannounced site visits for a small sample of these companies to verify their existence at the addresses recorded in their SAIC filings, or at an address taken from the Company's records. Certain of these visits are described in more detail in Schedule V.C.11.

A selection of AIs was identified that would enable the IC Advisors, where applicable, to combine this manner of testing in conjunction with travel to various locations for planned AI visits, or to visit locations within a travel radius of two hours or less of an IC Advisor's office.

During the period from October 18, 2011 to October 20, 2011, the IC Advisors performed site visits to the following AIs offices based on addresses provided by SF and company information included in SAIC filings:

- AI #2 has been an AI customer to BVIs from 2007 through to 2011. Three locations were identified in the Guangzhou area. AI #2 was found at one of the three sites, but had changed its name. Brochures at the location displayed the English name of Shareholder #10, a shareholder of the WFOE Supplier, Supplier #19.
- AI #3 has been an AI customer to BVIs from 2008 through to 2011. Two locations were identified in the Shanghai area. The company had recently vacated one site and could not be located at the other.
- AI #4 has been an AI customer to BVIs from 2008 through to 2011. One location was identified in the Shanghai area. The company could not be located at the site.

Results of these site visits have been summarized in Schedule V.C.11.

Representatives of AI #2 and AI #4 were included in the AIs interviewed. Those interviews took place at the offices of AI Conglomerate #1 ("**AI Conglomerate #1**"), an entity identified by Management as the conglomerate parent of these companies. The offices of AI Conglomerate #1 suggest the existence of a substantial business.

Representatives of AI #3 were included in the AIs interviewed. Those interviews took place at the offices of AI Conglomerate #2, an entity identified by Management as the conglomerate parent of this company. The offices of AI Conglomerate #2 suggest the existence of a substantial business.

18. AI General Observations

(a) Scale of Transactions with AIs

From the first fiscal quarter of 2006 to the first fiscal quarter of 2011, SF has dealt with approximately 14 different AIs, with no AI having dealings with SF spanning more than 4 years. Of those 14, 3 have been deregistered as of the date of this report, namely AI #8, AI #11 and AI #5. The total volume of transactions with the 14 AIs from the first fiscal quarter of 2006 to the first fiscal quarter of 2011 is approximately RMB 27 billion.

The volume of transactions with individual AIs can vary. The annual transaction sales volume with each AI from 2002-2011 is set on Schedule III.C. The five current AIs as at the first fiscal quarter of 2011 are AI #4, AI #1, AI #2, AI #6 and AI #3. From the first fiscal quarter of 2006 to the first fiscal quarter of 2011, they have had a combined approximately RMB 16.9 billion of transactions with SF.

(b) AIs as Project Companies

On August 19, 2011, Mr. Allen Chan provided an organizational diagram setting out the relationships between the five current AIs as at the first fiscal quarter of 2011 and their relationships with their holding companies ("**Holdcos**"[15]). He explained that the AIs were project companies which would change periodically but that the Holdcos remained the same. The diagram shows that AI #2 and AI #4 both fit under the one Holdco called AI Conglomerate #1 (or "**AI Holdco**") while the other 3 current AIs each have their own Holdcos. The SAIC filings received by the IC however did not indicate any relationship between these Holdcos and the 5 AIs.

This organizational diagram was presented to Mr. Albert Zhao during his interview on August 24, 2011. Mr. Zhao explained that during his tenure with SF, where he was in charge of liaising with AIs in relation to sales, he had only ever dealt with 5 AIs. He clarified that the individuals within the AIs with whom he liaises remain constant despite changes in the company with which they worked over time. Mr Zhao further indicated that the 5 AIs presented to him on the organizational chart were current as at the first fiscal quarter of 2011 and were comprised of the same main individuals as all other AIs he has dealt with.

D. WFOEs Contracts and Assets

1. Review Process Undertaken on WFOE Plantation Contracts and Assets

The primary focus of the asset verification has been the BVI standing timber assets. However, as the time frame and the difficulty of that process evolved, it was determined to also focus efforts on gathering, cataloguing and reviewing WFOE documentation. With respect to the WFOE timber assets, such documentation is not centralized and involved travelling to a number of offices and steps by the Company to centralize documentation within China. As in the case of the BVI assets, the review involved reviewing copies and originals of purchase contracts and land lease agreements, forestry bureau confirmations in the case of certain SP transactions and, in the case of SW and to a lesser extent SP, reviewing Plantation Rights Certificates.

Management has advised that WFOE standing timber assets as at December 31, 2010 represented approximately $298.6 million of book value (97,038 Ha.), $74 million in revenue and $10 million of Income for such year before allocation of corporate overhead; and that, SW and SP WFOE planted plantations represented approximately $103.8 million in book value as at December 31, 2010, but have not yet contributed materially to revenue.

[15] "Holdcos" refers to groupings which may not be legal groupings with cross shareholdings in the Western sense but rather groups of companies under common control or influence.

2. Review of Sino-Wood WFOE Plantation Assets

(a) Contract Review Results

All timber assets under SW are plantation land leases classified as planted plantations in the Company's public disclosure. The IC assembled and reviewed a total of 623 SW plantation land lease contracts (19 originals and 604 copies) covering 51,700 Ha. of planted plantations as at December 31, 2010. This is compared to the Company's disclosed total of 52,663 Ha. of planted plantations under SW as at December 31, 2010. Given its small size, the IC did not investigate this discrepancy. The plantation area of a typical SW plantation land lease contract is small compared to that of the BVI timber purchase contracts.

The IC Advisors selected and reviewed in more detail a sample of 19 original plantation land lease contracts covering the largest plantations of the four WFOEs under SW, representing approximately 8.89% of SW's total timber assets. Many more original plantation land lease contracts were made available for review at various SF offices in China but were not further inspected. This was due to the IC Advisors having previous reviewed copies of these and to the availability of Plantation Rights Certificates under SW for asset verification.

In contrast to the relative uniformity of BVI timber purchase contracts, the SW plantation land lease contracts are not in one standard form. SW contracts adopt a variety of forms and terminology, including land lease, land use right transfer, land contracting and plantation right/profit sharing structures. However, they generally involve the transfer of plantation land use rights, timber ownership and timber use rights at the same time. Plantation right/profit sharing structures refers to the arrangement whereby the villagers holding the plantation land ownership receive a percentage of the profits generated by the plantation in return for accepting reduced land lease fees from SF.

(b) Plantation Rights Certificates Reviewed

To the knowledge of the IC, the SW division does not ever purchase standing timber on a standalone basis and has not had a policy of seeking forestry bureau confirmations.

The IC Advisors reviewed a total of 418 copies of Plantation Rights Certificates provided by the Company representing approximately 42,979 Ha. of planted plantations held under the SW division.

The IC then reviewed 287 original Plantation Rights Certificates covering a total plantation area of 31,121 Ha. The details of this and a brief explanation regarding the Plantation Rights Certificates that were not available for review are set out below.

The IC inspected original Plantation Rights Certificates of (i) Gaoyao Jiayao Forestry Development Co., Ltd. in an office of Gaoyao Jiayao Forestry Development Co., Ltd. located in Zhaoqing city on October 18, 2011, (ii) Sino-Forest (Heyuan) Co., Ltd. and Zhangzhou Jiamin Forestry Development Co., Ltd. in an office of Sino-Forest (Heyuan) Co., Ltd. located in Heyuan city on October 19 and 20, 2011, and (iii) Guangxi Guijia Forestry Co., Ltd. in an office of Guangxi Guijia Forestry Co., Ltd. located in Nanning city on October 21, 2011, as arranged by SF.

The Company has advised that amongst the 418 copies of Plantation Rights Certificates which the IC Advisors initially reviewed, some had been superseded while others had been cancelled and reissued. Reasons for certain Plantation Rights Certificates being superseded or cancelled and reissued included that there were recalculations conducted for the area covered by the Plantation Rights Certificates. As a result, not all of the 287 original Plantation Rights Certificates later reviewed by the IC Advisors correspond exactly to copies amongst the 418 Plantation Rights Certificates that were initially reviewed.

Further, Management advised that a total of 136 Plantation Rights Certificates have been mortgaged as security for Plantation Rights Certificate loans and were therefore not available for review. Please refer to notes 5 and 8 of Schedule V.D.2.(f) for details. The IC Advisors reviewed a small sample of the mortgages.

Finally, certain SW WFOEs share their rights over the plantations with other parties on a 7:3 ratio and this is reflected in their Plantation Rights Certificates. A total of 54 Plantation Rights Certificates fall into this category. The Company has included 100% of the area covered by these 54 Plantation Rights Certificates in its calculations of proven ownership to the IC, covering 2,554 Ha., whereas the IC Advisors have only included 70% of the area for these assets in their calculations—a minor difference of 765 Ha. Please refer to notes 6, 9 and 10 of Schedule V.D.2(f) for details.

The IC has not visited any forestry bureaus to attempt to confirm the original Plantation Rights Certificates against registries, if any, maintained by such forestry bureaus.

3. Review of Sino Panel Timber Assets

(a) Contract Review Results

Unlike SW, SP does engage in the purchase and sale of standing timber as well as leasing plantation land so contracts reviewed for SP comprised of both timber purchase contracts and plantation land lease contracts. Accordingly, SP's standing timber and plantation land lease assets are divided into and respectively classified as purchased plantations and planted plantations.

The IC assembled and reviewed a total of 358 copies of SP WFOE contracts covering 173,424 Ha. as at December 31, 2010. These are comprised of 107 standing timber purchase contracts covering 96,169 Ha. of purchased plantations and 251 plantation land lease contracts covering 77,254 Ha. of planted plantations.

(b) Reconciliation of Surplus

The figures obtained from the IC's review of contracts are higher than the Company's recorded figures as at December 31, 2010 of 122,136 Ha., comprised of 97,038 Ha. of purchased plantations and 25,098 Ha. of planted plantations as shown in the asset reconciliation provided by Management to the IC and the OSC. Management has provided a reconciliation and explanation of this surplus of approximately 51,000 Ha. as well as the minor difference in its WFOE purchased plantation Ha. figure. The core of Management's reconciliation to disclosed figures as at December 31, 2010 was that such figures are lower primarily because they excluded bare land that had been leased but on which timber had not been replanted whereas the IC's contract review totals did include this bare land. The IC accepted this reconciliation and explanation and made no further investigations into this surplus.

(c) Plantation Rights Certificates Reviewed

(i) Purchased Plantations

The IC has reviewed a total of 383 original Plantation Rights Certificates which account for a total plantation area of 27,715 Ha. This Plantation Rights Certificate coverage amounts to a total of approximately 15.98% of SP's total timber assets of 173,424 Ha. based on contracts reviewed. These Plantation Rights Certificates are comprised of 301 Plantation Rights Certificates for 16,026 Ha. of standing timber and 82 Plantation Rights Certificates for 11,689 Ha. of plantation land leases.

The IC reviewed a total of 301 Plantation Rights Certificates for standing timber held under the SP division. Of these, 10 are in the name of SF covering 2,329 Ha. while 291 are in the name of Suppliers covering 13,697 Ha.

Regarding the 10 Plantation Rights Certificates in the name of SF, it is normally not possible to have Plantation Rights Certificates issued for standing timber only transactions. The Company explained that the standing timber purchase contracts corresponding to these 10 Plantation Rights Certificates were signed by Sino-Panel (China) but that the Plantation Rights Certificates were issued to Sino-Panel (Yunnan) Forest Management Co., Ltd. with the understanding that Sino-Panel (Yunnan) Forest Management Co., Ltd. would then purchase a lease over the same plantation land and would be assigned the rights over the standing timber from Sino-Panel (China). It was also explained that the Supplier in question agreed to delay the signing of the lease until after the issuance of the Plantation Rights Certificates and supported the application for those Plantation Rights Certificates. However, as at the date of this report, that lease is yet to be signed. Additionally, no documentation evidencing an assignment of the standing timber to Sino-Panel (Yunnan) Forest Management Co., Ltd. has been received. Nevertheless, for the purposes of this report, the IC has included these 2,392.2 Ha. of standing timber as being supported by original Plantation Rights Certificates.

Regarding the 291 Plantation Rights Certificates issued in the name of Suppliers, these are Plantation Rights Certificates issued to Suppliers that have sold the standing timber the subject of those Plantation Rights Certificates to SF WFOEs. As a form of security, these Suppliers allow the SF WFOEs to take possession of these Plantation Rights Certificates for the duration of the timber purchase contract, whose termination is usually deemed to occur when the timber is sold by SF or harvested. The SF WFOEs only have a contractual relationship with the Suppliers who remain the registered holders of the rights stipulated on the Plantation Rights Certificates. Nevertheless, in light of the contractual relationship between SF WFOEs and such Suppliers, and SF's possession of such Plantation Rights Certificates, for the purposes of this report, the IC has identified these 13,697 Ha. of standing timber as being supported by demonstrable chain of title to the original Plantation Rights Certificates.

(ii) Planted Plantations

The IC has reviewed a total of 82 Plantation Rights Certificates covering a total of 11,689 Ha. All of these 82 Plantation Rights Certificates are issued under SF's name.

The IC has not visited any forestry bureaus to attempt to confirm the original SP Plantation Rights Certificates against registries, if any, maintained by such forestry bureaus for purchased or planted plantations.

(d) Forestry Bureau Confirmations Reviewed

The IC has reviewed a total of 103 original forestry bureau confirmations covering a total of 138,914 Ha. which in turn represents approximately 80.1% of SP's total timber assets of 173,424 Ha. based on contracts reviewed. Of these, 42 confirmations covering 88,684 Ha. relate to standing timber while another 61 confirmations covering leases covering 50,230 Ha. relate to plantation land leases.

(e) Overlap between Plantation Rights Certificates and Forestry Bureau Confirmations

For the reasons outlined above, SP WFOEs sometimes have Plantation Rights Certificates and forestry bureau confirmations for the same plantation and therefore create an overlap between the totals of Plantation Rights Certificates and forestry bureau confirmations. The total amount of overlap between Plantation Rights Certificates and forestry bureau confirmations for SP is 26,333 Ha. which is comprised of overlaps of 15,264 Ha. for standing timber and 11,069 Ha. for plantation land leases. In some instances the forestry bureau confirmations were issued after the Plantation Rights Certificate had already been issued.[16]

(i) Purchased Plantations

Of the 96,169 Ha. of purchased plantations, approximately 88,684 Ha. are covered by forestry bureau confirmations. At the same time, approximately 16,026 Ha. are also covered by original Plantation Rights Certificates (13,697 Ha. in Suppliers' names and 2,329 Ha. in SF's name). Of the 16,026 Ha. covered by original Plantation Rights Certificates, only 762 Ha. (which originate from 2 transactions) are not concurrently covered by forestry bureau confirmations. Therefore, the overlap between forestry bureau confirmations and Plantation Rights Certificates is 15,264 Ha.

[16] Examples of forestry bureau confirmations being issued after the issuance of a PRC include those relating to SP plantation land lease contract JUW-RES-REN-002-07, whereby the PRC was issued under SF's name on November 27, 2007 while the confirmation was issued on July 28, 2008. Another example is the uncoded SP plantation land lease contract dated December 2, 2007 for 13,126.70 Mu (875.11 Ha) in the jurisdiction of Hunan FB#1 whereby two corresponding PRCs were issued on October 17 and November 6, 2007 while the confirmation was issued on August 8, 2008.

(ii) Planted Plantations

Of the 77,254 Ha. of planted plantations, approximately 50,230 Ha. are covered by forestry bureau confirmations. At the same time, approximately 11,689 Ha. are covered by original Plantation Rights Certificates in SF's name. Of these 11,689 covered by Plantation Rights Certificates, only 620 Ha. (which originate from 1 transaction) are not concurrently covered by forestry bureau confirmations. Therefore, the overlap between forestry bureau confirmation is 11,069 Ha.

(f) Forestry Bureau Visits

In conjunction with its visits to forestry bureaus to obtain BVI standing timber confirmations, the IC concurrently sought to acknowledge the issuance of old confirmations or to obtain new confirmations in respect of SP WFOE properties within the jurisdiction of the same forestry bureaus. A total of 15,980 Ha. of purchased plantation holdings and 10,904 Ha. of planted plantation holdings as at December 31, 2010 were so acknowledged or confirmed.

In respect of acknowledging the issuance of old confirmations, the Guangxi FB#1 confirmed that it had issued SP-related confirmations covering a total of 10,773 Ha. of purchased plantations and 9,518 Ha. of planted plantation holdings.

The person whom the IC Advisors met at the Hunan FB#1 acknowledged that it had issued SP-related confirmations covering a total of 476 Ha. of purchased plantations and 1,386 Ha. of planted plantations. This acknowledgment was given by the previous vice-chief, who had been appointed as a consultant to the Company.

The Hunan Forestry Entity #1 issued a new confirmation covering a total of 2,374 Ha.

The Yunnan FB#2 issued a new confirmation covering a total of 2,357 Ha. of SP purchased plantations.

See section V.C.9 for a further description of the various forestry bureau visits.

(g) SP Supplier Interviews

All of the Suppliers that were interviewed by the IC Advisors had contracts to supply timber to SP WFOEs. A summary of the IC's findings in respect of them is set out above under Part VI.

4. Review of Mandra Holdings

(a) Mandra - Executive Summary

The Company first became a shareholder of the Mandra group of companies in April 2005 with a 15% investment and completed the full acquisition of all of the Mandra group of companies in 2010.

The Company provided a chart of Mandra properties at the corporate subsidiary level that contained book values and hectare amounts that tied into the 2010 Financial Statements. It indicated a total of 147,144 Ha. held by Mandra subsidiaries which included 93,689 Ha. of plantations, 1,231 Ha. of bare land and 52,224 Ha. subject to long-term lease prepayments. The book value for the latter hectare amount was not included in timber holdings line item in the balance sheet included in 2010 Financial Statements but rather under the line item "Other Assets".

Approximately 853 contracts entered into by Mandra subsidiaries of the Company (as the buyer) covering plantation lands of 141,719 Ha. were reviewed. Management provided a reconciliation of the difference between that number and the publicly disclosed number of 147,144 Ha. held at December 31, 2010. Some 1,196 copies of Plantation Rights Certificates covering 95,420 Ha. were reviewed covering approximately 64.73% of the publicly disclosed total Ha. for Mandra and 1,115 original Plantation Rights Certificates related to Mandra assets have been sighted by the IC. These cover approximately 85,664 Ha. or 58.2% of the publicly disclosed total land holdings in the Mandra group of subsidiaries. Management explained that the balance of the properties were either subject to Plantation Rights Certificates under mortgage, under review for harvesting licensing or were properties for which Plantation Rights Certificates were in the process of being sought.

Underlying documentation relating to the purchases was also reviewed. As a general matter, documentation for Mandra properties was systematically more comprehensive than in other Company groups.

(b) Brief Mandra History Overview

The Company first made an investment by way of loan subscription to Mandra in April 2005. According to the minutes of the Company reviewed, Mandra became operational in 2006 prior to the issuance of bonds in a related public offering. There was extensive discussion in the Board minutes with respect to the Mandra investment throughout the period of time the Company held its investment, including recognition of a deteriorating financial condition. The Mandra bonds were publicly rated and Moody's issued a number of press releases concerning Mandra's financial status from 2006 through 2010, including a default situation in 2009 so Mandra cash flow situation was notorious. The Company took effective control of Mandra through a series of share acquisitions and bonds as addressed elsewhere in this report. The Globe made a series of accusations suggesting that the Company had bought Mandra while in a financially weakened state implying that Mandra's state was not public information. This is demonstrably wrong. A detailed review of the Globe report is set out in Schedule V.D.4.(b).

The IC reviewed Mandra diligence reports prepared in respect of legal matters pertaining to the Mandra companies at the time of its acquisition and a diligence report with respect to Plantation Rights Certificates held by its domestic subsidiaries.

(c) Mandra Review Process

(i) Number of contracts and Plantation Rights Certificates reviewed:

A. Approximately 853 copies of contracts have been assembled. The large majority of these transactions involve both purchasing timber and leasing underlying plantation land at the same time. The 853 contracts cover plantation land of 141,719 Ha.

B. The IC Advisors visited and inspected original Plantation Rights Certificates of Mandra in offices of Anqing Mandra Forestry Co., Ltd and Mandra Forestry (Jiangxi) Co., Ltd located in Anqing city and Nanchang city respectively as arranged by SF.

C. A total of 1,196 copies of Plantation Rights Certificates of Mandra have been reviewed covering plantation land of 95,240 Ha. representing 64.73% of the publicly disclosed total for Mandra of which 1,115 original Plantation Rights Certificates have been verified covering plantation land of 85,664 Ha. or 58.20% of the publicly disclosed totals for Mandra.

D. 17 original plantation land disposal contracts, under which all the 1,810 Ha. plantation of Huanggang Mandra Forestry Co., Ltd. and Wuhu Mandra Forestry Co., Ltd were disposed, have been reviewed.

E. The IC has reviewed two original mortgage certificates covering 6,982 Ha. plantation being mortgaged. The balance of the mortgaged Plantation Rights Certificates were not reviewed

(ii) Types of contracts – Planted Plantations

There were four primary types of contracts:

- Timber purchase with plantation land lease contract – Anqing Mandra Forestry Limited's contracts with total contract area of 95,535 Ha. are substantially of this type. The WFOE purchases standing timber and leases underneath plantation land at the same time. The WFOE is entitled to harvest the existing timber and replant trees thereafter. The consideration for the purchase of timber and for the annual plantation land rental are calculated separately at a fixed rate according to the reserves of timber (in cubic meters) and area of plantation land (in mu). A map indicating the boundaries of the plantation, Plantation Rights Certificates of the villagers, villagers' resolution and the WFOEs' internal survey report are usually attached to the contracts.

- Timber and plantation land contracting right transfer contract – the overwhelming majority of Xuancheng Mandra Forestry Limited's contracts with total contract area of 6,700 Ha. are of this type. The contracting rights of the timber and underlying plantation rights are transferred to the WFOE from the previous contracting party and consent is obtained from the plantation land owner. The consideration for the purchase of timber and plantation land is usually calculated together at a fixed rate per mu for the whole contracting term.

- Forestry resources transfer contract – the overwhelming majority of Mandra Forestry (Jiangxi) Limited, Yihuang Mandra Forestry Limited and Zixi Mandra Forestry Limited contracts with total contract area of 37,674 Ha. are of this type. Timber and underlying plantation land use rights are transferred together to the WFOE and consideration for timber and plantation land are usually calculated together at a fixed rate per mu.

- Plantation land use right transfer contract – The contracts for Wuhu Mandra Forestry Limited are of this type. Only the plantation land use right is transferred to the WFOE and the transferor is obliged to clear the timber thereon.

The IC has not visited any forestry bureaus to attempt to confirm the original Mandra Plantation Rights Certificates against registries, if any, maintained by such forestry bureaus.

(d) MW-HSBC Letter Timing and Issues

In reviewing the incorporation applications in the SAIC files of four Mandra entities, MW retrieved a letter from The Hongkong and Shanghai Banking Corporation Limited ("**HSBC**") dated February 1, 2005. The letter (which is a poor-quality copy) has a re. line referring to a Mandra company, but in fact comments on HSBC's banking relationship with "Sino-Wood Bartners [sic.]" ("the Company"), noting, for example, that it considers "the Company" "good" for "normal business engagement". MW characterizes the letter as "suspicious". The MW Report includes a photograph of the letter, the appearance of which could suggest that it has been tampered with (see Schedule V.D.4.(d).1).

The IC Advisors retrieved the HSBC letter in question from SAIC filings in connection with applications regarding the formation of three Mandra entities, Anqing Mandra Forestry Limited, Xuancheng Mandra Forestry Limited and Wuhu Mandra Forestry Limited. These three companies were formed on March 14, 2005, prior to the date SF initially became a shareholder of Mandra. The IC Advisors also found a Chinese version of the HSBC letter (see Schedule V.D.4.(d).3) in the SAIC filings of Anqing Mandra Forestry Limited. It is also dated February 1, 2005, and generally appears to be identical to the English version of the letter that appeared in the MW Report, speaking only to Mandra Forestry Anhui Limited without mention of Sino-Wood.

Management denied knowledge of the HSBC letter in its response to the MW Report, stating that, on the date of the letter, SF was not a shareholder of Mandra. BJ has retrieved an email subsequent to the MW Report attaching what the author, Ringo Yip, Senior Manager - Corporate Planning, SF, characterizes as "the true HSBC bank reference letter" (see Schedule V.D.4.(d).2). This letter, which is also dated February 1, 2005, generally appears to be identical to the letter in the MW Report, except that the subject and copy line properly refers to Sino-Wood, not Mandra Forestry Anhui Limited.

The IC's Chinese advisors have observed that, according to the Implementation Rules of Law of Wholly Foreign Owned Enterprises, a foreign investor is required to include evidence of credit in its application for forming a WFOE. Such evidence is normally issued by a bank in which the foreign investor maintains an active account, to certify to the regulatory authority that the foreign investor is of good credit and able to conduct business through the proposed WFOE. If this was the purpose of the HSBC letter, the letter should address Mandra Forestry Anhui Limited, a major investor in WFOEs, not Sino-Wood, which was not an investor in WFOEs at the time.

Management explained that they do not have any record of the forged version of the letter and do not know who forged such letter.

VI. RELATIONSHIPS

VI. RELATIONSHIPS

The MW report made a number of allegations regarding the relationships of the Company with AIs and Suppliers and between AIs and Suppliers, particularly with respect to Yuda Wood. The IC Advisors, in the course of their review, identified a number of possible relationships which warranted explanation. These are outlined below in this Part VI. Management has very recently provided to the IC information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board. Some of such information and analysis may not be capable of independent verification.

The objectives of the IC's examination of the Company's relationship with its AIs and Suppliers were to determine, in light of the MW allegations, if such relationships are arm's length and to obtain, if possible, independent verification of the cash flows underlying the set-off transactions described in Section II.A. That the Company's relationships with its AIs and Suppliers be arms length is relevant to SF's ability under GAAP to:

- book its timber assets at cost in its 2010 and prior years' audited financial statements; and
- recognize revenue from standing timber sales as currently reflected in its 2010 and prior years' audited financial statements.

A. Yuda Wood

1. Muddy Waters' Allegations

(a) In the MW Report, Muddy Waters alleged that Yuda Wood, a major Supplier based in Hunan Province, was a significant "undisclosed subsidiary" of SF, which has been receiving "massive amounts of money" from SF subsidiaries and which is "the nerve center for [SF's] illicit activities".

(b) In addition to the allegations in the MW Report, Muddy Waters published a short follow-up report on June 20, 2011, that focused on SF's relationship with Hong Kong's Sonic Jita, the holding company of Yuda Wood, which specifically alleged that:

(i) when Hong Kong Sonic Jita was owned by SF executives and SF itself, SF engaged in a major undisclosed related party transaction with Hong Kong Sonic Jita (in 1997); and

(ii) while Hong Kong Sonic Jita is currently nominally owned by parties unrelated to SF, SF and Hong Kong Sonic Jita shared "at least one key executive" (identified by the Chinese name of Albert Ip), who in 2005 entered into a contract with Hong Jiang City, Hunan Province on behalf of Hong Kong Sonic Jita.

(c) However, Hong Kong Companies Registry filings show a change of control and ownership of Hong Kong Sonic Jita on July 28, 1997 and July 28, 1998 respectively, prior to the occurrence of the alleged related party transactions cited in the MW Report. In particular, those filings show that:

(i) from November 13, 1993 to July 28, 1997, the directors of Hong Kong Sonic Jita were SF executives and associated parties, and that from November 13, 1993 to July 28, 1998, the shareholders of Hong Kong Sonic Jita were parties associated with SF.

(ii) parties associated with SF were replaced as directors and shareholders of Hong Kong Sonic Jita on July 28, 1997 and July 28, 1998, respectively by Jin Juemin and Li Haibao, who appear to have been associated with Beijing Sonic Jita, a forestry engineering contractor to SF's factories within China, and who renamed the company as "Sonic Jita Engineering Ltd." from August 1, 1997.

(d) In his statutory declaration dated August 15, 2011 (see Section VI.A.2(d) below), Allen Chan stated that up to July 28, 1998, SF did not engage in any transactions with Hong Kong Sonic Jita, and that, up until this date, the Company (under all its registered names) had not engaged in any business and remained a dormant company, and that after this date, Hong Kong Sonic Jita was no longer a related party to SF.

(e) Nevertheless, in the course of the IC Advisors' Yuda Wood review, they identified information that suggested that SF had a close relationship with Yuda Wood, may have been involved in its establishment and exercised an influence over certain of its RMB bank accounts, funding and tax payments.

2. Review Conducted

(a) Evidence Brief

To address the MW allegations, and to gain a better understanding of the connections between SF and Yuda Wood, the IC Advisors prepared an interim evidence brief plan (draft dated August 23, 2011) that included an electronic data review as described above in Schedule IV, relationship mapping and meetings with Management and with E&Y. Relationship mapping findings are set out in Schedule VI.A.2(a).

(b) BJ's Interviews with Management

The IC Advisors attended interviews conducted by BJ with Management between July 26 to August 11, 2011. Information concerning the Yuda Wood relationship was presented to members of Management. The members of Management interviewed were Allen Chan, KK Poon, Alfred Hung, Albert Zhao, George Ho and Chen Hua.

(c) Review for Associated Parties

(i) During the IC Advisors' review of the SAIC filings for Yuda Wood and other companies identified during the process, a document was found within the Yuda Wood SAIC search results which linked Simon Yeung to the purchase of a manufacturing facility in Hunan in Yuda Wood's name prior to when Yuda Wood had yet to be officially incorporated. Mr. Yeung's Chinese signature appeared on an offer, and ultimately an executed purchase contract, for Yuda Wood to acquire the factory facility.

(ii) This document was presented to Mr. Yeung for an explanation at his interview by the IC Advisors. On August 25, 2011, Mr. Yeung responded that he was performing a favour for Mr. Huang Ran as he was absent from the region at the time the facility became available for sale and that he did not act on behalf of Yuda Wood in any capacity.

(d) Statutory Declarations

The issues of SF's relationship with Yuda Wood were still being examined by the IC Advisors in the middle of August, 2011, at a time when the Company's quarterly report for the period ending June 30, 2011 ("**Q2s**") were being prepared. To address certain issues relating to Yuda Wood pending completion of the IC's review, statutory declarations were obtained by the IC and the Audit Committee from the following members of Management at the IC's request:

- Allen Chan;
- Albert Ip; and
- Chen Jun.

The declarations were prepared with assistance from the Company's counsel and were sworn on August 15, 2011.

In his statutory declaration, Allen Chan declared that:

(i) he did not hold a direct or indirect or beneficial shareholding interest in Yuda Wood, Beijing Sonic Jita or Hong Kong Sonic Jita or their affiliates, and was not involved in their operations and that he did not have other personal arrangements with or entitlements from these entities; and

(ii) to his knowledge, no officer, director or employee of SF held a direct or indirect or beneficial shareholding interest in Yuda Wood, Beijing Sonic Jita or Hong Kong Sonic Jita or their affiliates or was involved in their operations, and that to his knowledge, no other officer, director or employee of SF had any other personal arrangements with or entitlements from these entities.

In his statutory declaration, Albert Ip:

(i) denied having ever been an executive of Hong Kong Sonic Jita, held himself out to be a representative of Hong Kong Sonic Jita or entered into a contract in 2005 with Hong Jiang City, Hunan Province, on behalf of Hong Kong Sonic Jita; and

(ii) further declared that Zhan Xiaokun and Chen Jun did not become employees of SF until after resigning as directors from, and selling their shares in, Hong Kong Sonic Jita.

However, searches at Hong Kong's Companies Registry in August 2011 indicated that Chen Jun remained a director and shareholder of Hong Kong Sonic Jita since joining SF in July 2010. In response to this finding, SF counsel arranged for Chen Jun to make a statutory declaration in which he declared that he had been only a nominee shareholder in Hong Kong Sonic Jita, and had submitted a letter to the other shareholder and director of Hong Kong Sonic Jita, Huang Ran, on June 26, 2010, tendering his resignation as director and asking to transfer his shares to Huang Ran. Huang Ran appears, from the documents exhibited to Chen Jun's statutory declaration, to have only filed documents implementing such requests with Hong Kong's Companies Registry and Stamp Duty office one year later, on June 10, 2011. Those documents were dated July 30, 2010, and included minutes of a shareholders' meeting allegedly held in Hong Kong on July 30, 2010, and attended by Chen Jun, at which his resignation as director and sale of his shares was approved. Chen Jun stated in his declaration that he did not attend any such meeting.

(e) IC Advisors' Interviews with Management

As the IC Advisors' Yuda Wood review proceeded subsequent to the release of the Q2s, they identified additional information relevant to SF's relationship to Yuda Wood.

The IC Advisors presented to the IC on August 23, 2011 a draft Yuda Wood interim evidence brief memo which set out certain matters of concern that warranted further investigation. (This memo was subsequently presented to the Board on August 23, 2011, and delivered to the OSC under summons.)

The IC Advisors recommended that certain members of Management be interviewed about the subject matter raised in certain emails identified by the IC Advisors, and about the Yuda Wood relationship generally; these emails suggested a close relationship between SF, its past and current employees, and past and current shareholders of Yuda Wood and/or its holding company.

The interviews conducted by the IC Advisors took place in Hong Kong from August 24, 2011 to August 26, 2011 and were also attended by BJ who occasionally participated. The members of Management interviewed were: Allen Chan, Albert Ip, George Ho, Eric Chan, Alfred Hung, Simon Yeung, Albert Zhao, Chen Hua and KK Poon. The IC Advisors have delivered completed notes of such interviews to the IC, which delivered them to E&Y and to the OSC under summons. The IC authorized Osler to provide such notes to BJ so it could provide copies of the relevant interview notes to each interviewee and his or her respective counsel.

Following their respective interviews, Mr. Martin put Messrs. Ho, Hung and Yeung on administrative leave and Mr. Ip on limited duties.

The IC Advisors subsequently conducted interviews on September 8, 2011 with Messrs. Chen Jun, and Zhan Xiaokun. Both are current employees of SF and both are former 50% shareholders of Hong Kong Sonic Jita, the holding company of Yuda Wood.

(f) Interviews and Meetings with Yuda Wood

Further to the steps set out in their Yuda Wood evidence brief plan, the IC Advisors requested a meeting with Yuda Wood for the purposes of interviewing Yuda Wood's sole shareholder, Huang Ran.

On September 1, 2011 a meeting was held in Shenzhen. The nature of the meeting was a "meet and greet" between Huang Ran and SF's new Chief Executive Officer, Judson Martin. Huang Ran was accompanied by Supporter #2 who appears to be a shareholder and supervisor of Jiangxi Tianyao which is also a supplier to SF and Supporter #1. BJ and JH were also present. The IC Advisors were told by Management and BJ not to take any notes or ask any questions during the meeting as a condition of participation.

The key items noted during the September 1, 2011 meeting with Huang Ran are as follows:

- Huang Ran stated that he was in charge of running Yuda Wood's daily business. He denied that Yuda Wood is obligated by SF's instructions and stated that no one from SF has any interest in Yuda Wood.
- Huang Ran declined to disclose the names of the supporters behind Yuda Wood.
- Huang Ran stated that the only company to which Yuda Wood sold standing timber was SF.
- Huang Ran advised that he owns three other companies in China, namely Supplier #26, Supplier #9 and Supplier #25, which also act as Suppliers to SF. The SAIC filings indicate that Huang Ran holds a majority shareholding interest in those companies.

Following the meeting in Shenzhen, the IC Advisors were advised by BJ that Huang Ran would meet them again the next day in Chongqing, a five hour journey from Hong Kong and Shenzhen. The IC Advisors were also told that such meeting the next day would be another "meet and greet", and that it was unlikely that they would be able to review any documentation.

The second meeting with Huang Ran took place in Chongqing on September 2 2011. The meeting was conducted in accordance with the Interview Protocol for Suppliers and AIs prepared by the IC Advisors and sent to Allen Chan, Judson Martin and BJ on August 4, 2011. (See Schedule VI.A.2.(f).)

The key items noted during the second meeting with Huang Ran are as follows:

- The meeting was a "meet and greet" and consisted of a meeting over lunch and a subsequent meeting at Huang Ran's premises.
- Huang Ran confirmed he is the legal representative of Yuda Wood.
- Huang Ran declined to talk about any companies he is associated with other than Yuda Wood.
- Huang Ran advised that transactions with SF account for over 50% of Yuda Wood's business.
- Huang Ran advised that Yuda Wood acquires plantations from aggregators, not directly from farmers.
- Huang Ran advised that Yuda Wood obtains confirmations from forestry bureaus at the request of SF; the forestry bureaus have no obligation to issue them.
- Huang Ran advised that Yuda Wood sometimes directs payments to it from AIs to other parties, so there may be no evidence of Yuda Wood having received funds.
- Huang Ran agreed to try to collect documents for the IC Advisors' review.

A third meeting with Huang Ran was scheduled and took place at SP's Guangzhou office on September 28, 2011.

The key items noted during the third meeting with Huang Ran are as follows:

- Huang Ran was cooperative and gave responses to all questions.
- The IC Advisors were shown copies of four contracts with two farmers' resolutions attached, and two contracts between Yuda Wood and its suppliers. With the exception of one contract for approximately 4,000 Ha., matched on the basis of the city and county of the plantation alone, the sample contracts provided between Yuda Wood and its suppliers could not be directly reconciled with transactions selected for review by the IC

Advisors, as specific location data was not available. No copies of these documents were allowed to be made.

- Huang Ran stated that Yuda Wood's business is trading and planting plantations and that SF represents approximately 40% - 50% of Yuda Wood's business.

- Huang Ran advised that in cases where SF directs a third party AI to settle its transactions with Yuda Wood (i.e. all BVIs transactions), Yuda Wood would always nominate a fourth party (which may in turn nominate a fifth or sixth party) to receive the payment "for tax reasons".

- Huang Ran declined to discuss tax related matters and when asked if Yuda Wood has ever issued VAT receipts to SF, he stated he was uncertain if that was the case, but if so, Yuda Wood should have records of any VAT receipts issued to SF.

- During the interview, Huang Ran was shown two emails by Rebecca Huang of BJ, which she identified as being the two emails resulting from the email review that were of concern to E&Y.

- In response to the two emails, Huang Ran denied that SF controlled Yuda Wood. He acknowledged that SF, through George Ho, Vice-President, Finance, monitored and was a joint operator of one of Yuda Wood's bank accounts (each of Yuda Wood and SF had knowledge of one of two passwords which were jointly required to release funds from the account).

- When shown the lists of SF Suppliers/AIs provided to the OSC and companies identified through relationship mapping or SAIC filings, Huang Ran acknowledged only that he has an interest in Supplier #9. When asked about other companies, he declined to discuss them. He did state that Yuda Wood "may have done one or two transactions" with Supplier #3 a few years ago.

- According to SF's records, the total volume of transactions between SF and Yuda Wood from 2007-2010 was RMB 4.56 billion. The IC Advisors were not provided access to the Yuda Wood books and records in order to confirm this volume during any of the three meetings.

(g) Management Responses

The IC Advisors completed additional electronic review for Yuda Wood related emails and the IC and E&Y requested a response from Management. The final version of such response was delivered to the IC, the audit committee and E&Y on October 22, 2011. The IC Advisors provided comment to the IC on Management's response to the emails in that such response was determined to be incomplete.

3. Findings Relating to Yuda Wood

(a) The IC is satisfied that Mr. Huang Ran is not currently an employee of the Company and that Yuda Wood is not a subsidiary of the Company. However, there is evidence suggesting close cooperation (including possible payment of capital at the time of establishment, joint control of certain of Yuda Wood's bank accounts and the numerous emails indicating coordination of funding, and other business activities). Management has advised, based on its own inquiries, that they believe that no such payment of capital has occurred. Management explanations of a number of Yuda Wood-related emails and answers to E&Y's questions are being reviewed by the IC but may not be capable of independent verification.

(b) Considerations Relevant to Yuda Wood Review:

(i) The meetings with Huang Ran occurred at a location related to a separate project company that Huang Ran is associated with and the second meeting occurred at the Guangzhou offices of SP.

(ii) The IC Advisors were not given access to certain of Yuda Wood's books and records in order to trace the flow of funds related to a selected sample of transactions (which sample was provided to Yuda Wood in advance).

(iii) Huang Ran declined to provide the names of other individuals or companies that control or have an interest in Yuda Wood.

Please see Schedule V.C.11 for a summary of Supplier site visits.

B. Other Relationships

1. Relationships Identified in Preparation for Suppliers/AIs Interviews

In preparation for the Supplier and AI interviews the IC Advisors performed reviews of SAIC filings for the Suppliers and AIs and identified numerous potential relationships between AIs and BVI Suppliers. Relationships identified to date for the key Suppliers and AIs are summarised in Schedule VI.B.1.1. In light of the potential relationships identified, the IC Advisors further reviewed BVI timber purchase contracts, Entrusted Sale Agreements and summary charts of BVI transactions. As a result of this review, the IC Advisors identified transactions which require explanations.

Observations included that SF's top Supplier from 2007-2010, Supplier #1, had no transactions with any SF BVIs in the Company's first and second fiscal quarters of 2011. In this same period, three new Suppliers, owned partly by recently departed SF employees, appeared and conducted several billions of RMB of business in the Company's first and second fiscal quarters of 2011.

Other observations included a number of payments to Suppliers in 2011 being made by an offshore customer that appears to be related to AI Conglomerate #1 / Supplier #3, suggesting that there may be funds held offshore on behalf of SF BVIs or offshore payment obligations owed to SF BVIs.

Further observations included set-off arrangements between AIs and Suppliers with potential relationships as well as the sale of BVI standing timber to AIs that are potentially connected to the Suppliers that supplied the same standing timber.

These observations are summarized below. Some of these observations were raised with Mr. Judson Martin via email on October 19, 2011. A copy of the correspondence to Mr. Martin is attached as Schedule VI.B.1.2. As noted above, very recently, Management provided to the IC information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

(a) Suppliers with Former SF Employees

In addition to Yuda Wood, to date, the IC Advisors have identified 13 Suppliers where former SF employees, consultants or secondees are or have been directors, officers and/or shareholders. Including Yuda Wood, these suppliers account for 43% of SF plantation purchases between 2006 and the first quarter of 2011. Very recently, in Management's explanation of relationships, a number of additional relationships were identified. These have not yet been reviewed by the IC Advisors.

(i) Supplier #2

Supplier #2 was established in 2010 and acts as a major Supplier to BVIs, taking up much of the slack in supply of timber left by the absence of Supplier #1 as a Supplier in 2011. It appears to be partly owned by an individual who was a SF employee from 2007 to 2010.

According to SAIC search results, Supplier #2 was incorporated on May 27, 2010, and has 2 shareholders. The first is Shareholder #11, who holds 80% of the shares and contributed RMB 800,000 of the registered capital. The second is Shareholder #12, who holds 20% of the shares and contributed RMB 200,000 of the registered capital. The total registered capital is just RMB 1 million.

According to the first SF employee lists obtained through electronic data searches, Shareholder #12 was an employee of the SF WFOE Hunan Jiayu Wood Products Co., Ltd. from March 1, 2007 to March 1, 2008, as a manager in the resources department. He was also employed at Sino-Panel (Luzhai) Co., Ltd. from March 1, 2007 to March 31, 2010, as a manager in the operations department. These positions appear to be intermediate positions.

In the third and fourth quarters of 2010 Supplier #2 had over RMB 1.8 billion worth of standing timber transactions with the BVI companies. In the first quarter of 2011 Supplier #2 had over RMB 1.76 billion worth of standing timber transactions with BVI Companies.

According to a scan of his Chinese ID card found in the SAIC filings, Shareholder #11, the 80% shareholder of Supplier #2, was born on June 9, 1987. This means that he was 23 years old when Supplier #2 engaged in transactions worth RMB 3.56 billion with SF from the third quarter of 2010 to the first quarter of 2011.

(ii) Supplier #21

Supplier #21 has been acting as a Supplier to BVIs since the Company's second fiscal quarter of 2011. According to SAIC search results, Supplier #21 was incorporated on March 11, 2011. It has registered capital of RMB 5 million and its legal representative is the previously mentioned Shareholder #12, the former employee of SF until March 31, 2010, and the 20% shareholder of Supplier #2. Shareholder #12 holds 70% of the shares while Shareholder #13 holds the other 30%.

An email located in the Company's records suggested that senior management personnel knew of Shareholder #12 using proceeds paid from Sino-Panel Luzhai and Jianghua WFOEs to Supplier #2 for timber purchases to pay the registered capital of Supplier #21.

In the second fiscal quarter of 2011, Supplier #21 had over RMB 1 billion in transactions with the SF BVIs. The first such transaction was for RMB 432 million and was dated April 7, 2011.

(iii) Supplier #7

Supplier #7 has been acting as a Supplier to BVIs - since the first fiscal quarter of 2009. In 2009, Supplier #7 had over RMB 1.8 billion of standing timber transactions with the BVIs. In all of 2010 and the first fiscal quarter of 2011 it had no transactions with the BVIs. In the second fiscal quarter of 2011 it had over RMB 435 million of transactions with the BVIs.

According to SAIC search results, it was registered on January 20, 2009, with a registered capital of RMB 500,000. Its 60% shareholder is Shareholder #14, who was an employee of the SF Jiamu WFOE from May 1, 2007 to October 31, 2007, as a project assistant in the logistics department. He was also employed by the SF Hezhou WFOE from November 1, 2007 to October 31, 2008, as a manager in the projects department. During his interview, Mr. Allen Chan described Shareholder #14 having been a junior employee and the IC's findings appear to confirm this.

(iv) Other Suppliers and AIs with Former SF Personnel

Other observations regarding SF Suppliers with former SF personnel as summarised in the table below. A more detailed discussion of these Suppliers is contained in Schedule VI.B.1.1.

Name of Company	Role	Transactions with SF (RMB)	Date of Registration	Registered Capital (RMB)	Former SF Personnel, their shareholding or role and SF employment dates
Supplier #2	BVI and WFOE Supplier	3.59 billion (BVI) (Aug 2010 to Mar 2011) 72 million (WFOE) (Oct 2010	May 27, 2010	1 million	Shareholder #12 (20%) (SF Mar 1, 2007 to Mar 31, 2010)
Supplier #21	BVI Supplier	1 billion (Q2 2011)	Mar 11, 2011	5 million	Shareholder #12 (70%)(SF Mar 1, 2007 to Mar 31, 2010)
Supplier #7	BVI and WFOE Supplier	1.8 billion (BVI) (Jan to Dec 2009), 205 million (WFOE) (Aug 2010), 435 million (Q2 2011)	Jan 20, 2009	500,000	Shareholder #14 (60%) (SF May 1, 2007 to Oct 31, 2008)
Supplier #22	WFOE Supplier	39 million (Mar 2011)	Dec 10, 2010	2 million	Shareholder #14 (30%)(SF May 1, 20 07 to Oct 31, 2008) Shareholder #19 (70%) (SF Sep 24, 2007 to Aug 6, 2010)
Supplier #18	BVI Supplier	49 million (Dec 20, 2007)	Sep 12, 2006	500,000	Shareholder #14 (director and GM Aug 2007 to Apr 2008) (SF May 1, 2007 to Oct 31, 2008) Officer #1 (supervisor Aug 2007 to Apr 2008) (SF 2005 to present)
Supplier #12	BVI and WFOE Supplier	837.6 million (BVI) (Q3 and 4 2009) 31 million (WFOE) (10 Jan 2010)	Aug 7, 2009	500,000	Shareholder #14 (shareholder Aug 7, 2009 to Oct 15, 2009) (SF May 1, 2007 to Oct 31, 2008)
Supplier #23	WFOE Supplier	3.3 million (Oct 3, 2007)	Jun 15, 2005 (deregistered Mar 5, 2008)	500,000	Shareholder #20 (70%) (SF April 1, 2004 to present)
Supplier #24	WFOE Supplier	182 million (Oct 2009)	Apr 28, 2008	20 million	Shareholder #1 (39%)
Supplier #25	WFOE Supplier	99 million (Oct 2007 to Apr 2010)	Oct 31, 2005	500,000	Shareholder #1 (100%)
Supplier #9	WFOE Supplier	1.1 billion (Apr 10 to Mar 11)	Aug 19, 2009	2 million	Shareholder #1 (80%)
Supplier #26	WFOE Supplier	170 million (Aug 21, 2010)	Jan 5, 2010	2 million	Shareholder #1 (80%) Shareholder #21 (20%) (SF Luzhai Jan 1, 2008 to Mar 31, 2010, Gaoyao Jiayao left May 30, 2003, join date unknown)
Supplier #20	WFOE Supplier and customer	61 million (sale to SF) (2010) 65 million (purchase from SF) (2009)	Dec 2, 2008	1 million	Shareholder #21 (70%) (SF Luzhai Jan 1, 2008 to Mar 31, 2010, Gaoyao Jiayao May 30, 2003 to present) Shareholder #17 (30%) (SF 2000 to 2008)
Supplier #19	WFOE Supplier	478 million (Mar to Nov 2009)	Jan 28, 2008	USD 5 million	Shareholder #9 (SF 2001 to 2007)

(b) AIs with Former SF Employees

(i) AI #2

AI #2 is a current AI that was registered on February 15, 2002 with a registered capital of RMB 500,000. From the third quarter of 2007 to the first quarter of 2011, it purchased approximately RMB 4.093 billion of standing timber from BVIs.

During the interview with AI #2, the IC Advisors were introduced to Officer #3 as the person in charge. Officer #3 was an employee of the Company from 2004 to 2007.[17]

(c) Potential Relationships between AIs and Suppliers

(i) Supplier #13 and Supplier #1

Supplier #13 is a supplier to BVIs WFOEs. It was registered on June 5, 2009, with registered capital of RMB 5 million. In September 2010 it sold approximately RMB 796 million of timber to the BVIs over two transactions. From October to December 2009 it completed approximately RMB 179 million of transactions with the WFOEs.

According to SAIC filings, the 60% shareholder is Shareholder #15 while the 40% shareholder is Supporter #2. On September 1, 2011, Supporter #2 was introduced to Mr. Judson Martin in the presence of Mr. Robert Staley and Ms Rebecca Huang of BJ as a supporter behind Yuda Wood.

(ii) Supplier #4, Supplier #5 and AI #6.

There are two Suppliers and an AI that have a common person as their "supervisor". The practical role of "supervisor" varies within different Chinese companies and it is not known what the role of this person is within each of these companies.

Supplier #4 is a supplier to BVIs that was registered on December 15, 2005, with a registered capital of RMB 500,000 and was deregistered on July 16, 2009. Its 100% shareholder was Shareholder #16. Its supervisor is Officer #2. From 2006 to 2009, it sold RMB 3.28 billion of standing timber to the BVIs.

Supplier #4 is a supplier to BVIs that was registered on April 16, 2009, with a registered capital of RMB 300,000. Its 100% shareholder was the

17 According to SAIC search results, Officer #3 is not listed as a shareholder or officer of AI #2. Similarly, the SAIC search results do not indicate any shareholding by AI Conglomerate #1. However, during the interview with AI Conglomerate #1, its chief Shareholder #5 introduced Officer #3 as the person in charge of AI #2 and stated that AI #2 was his investment. For details of the interview, please refer to Schedule V.C.11.

same Shareholder #16. Its supervisor is the same Officer #2. From 2009 to the first quarter of 2011, it sold RMB 2.64 billion of standing timber to the BVIs.

AI #6 is an AI that was registered on January 13, 2010 with a registered capital of RMB 200,000. From 2010 to the first quarter of 2011 it purchased RMB 2.15 billion of standing timber from the BVIs. According to SAIC filings, its supervisor is the same Officer #2. From January to November its 100% shareholder was Shareholder #18.

(d) Payments for BVI Standing Timber Purchases Made by Companies that are Not AIs

(i) Trading Co. #1

According to emails located in the Company's records, Trading Co. #1 is incorporated in the BVI and is owned by Shareholder #4, the brother of Shareholder #3 of Supplier #3. That email was sent to SF personnel and also contains the Hong Kong HSBC bank details of the company. A search seeking the identity of shareholders of Trading Co. #1 was denied (shareholding information in the BVI is only available with the consent of the shareholder).

According to the SAIC search results, and confirmed at the AI interview with AI #4 and AI #2, Shareholder #4 is a former shareholder of AI Conglomerate #1, the Holdco of these two AIs.

In the first fiscal quarter of 2011, in four different BVI standing timber purchases with Supplier #2, payment was made partially by Trading Co #1. This is unusual as payments for BVI standing timber purchases are normally made by SF's AIs as set-offs against SF's standing timber sales to those AIs. It is not clear on what basis Trading Co. #1 owed money to SF and made those payments to Supplier #2. The SAIC search results for Supplier #2 do not indicate that Shareholder #4 is involved in Supplier #2.

These payment records suggest that there may be funds held offshore by Trading Co. #1 (or others) on behalf of SF, or accounts payable to SF BVIs by Trading Co. #1 (or others).

Management advises that Trading Co. #1 is owned by Shareholder #4 and is a customer of both SP and SW Trading that purchases imported logs from the Company. Supplier #2 is a supplier of plantations that Shareholder #4 is not involved with. The Company sold imported logs to Trading Co. #1 and by the end of 2010, Trading Co. #1 owed the Company $39 million. The Company had purchased plantations from Supplier #2 and owed it for these purchases. The Company's finance department pressured Trading Co. #1 to pay its account after year end, but it did not have the U.S. dollars to pay the amounts owing. Trading Co. #1 was directed to pay its liability using RMB and it was directed to pay it to Supplier #2 in partial settlement of the plantation purchases. Management very recently provided the IC with information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

(ii) Other Set-off Arrangements Involving Non-AI Companies

The IC Advisors have also identified other instances where Suppliers of BVI standing timber purchases have received payment from companies other than AIs. The companies identified appear to be domestic import/export companies.

Payments by these companies in RMB to Suppliers of the BVIs in China may suggest that they have accounts payable to the BVIs. If this is the case, BVI funds outside China (or accounts receivable offshore in foreign exchange) are being transferred by way of set-off into China for purchase of standing timber that become part of the BVI assets in China.

Specific examples include payments in 2010, where Supplier #3 received payment from non-AI companies, including Trading Co. #2 and Trading Co. #3. Similarly, in 2010 the Supplier #5 received payment from Trading Co. #4.

It is again unclear on what basis these non-AI companies are making set-off payments on behalf of SF.

(e) Payments to Potentially Connected Suppliers

(i) AIs AI #4 and AI #2 Paying Potentially Connected Supplier #3

SF charts of BVI purchase and sale transactions indicate that from 2009 to 2011, the AIs AI #4 and AI #2 made over RMB 604 million in set-off payments on behalf of SF for BVI timber purchases from the Supplier.

At the Supplier #3 supplier interview in Schedule V.C.11, Shareholder #3, the chief of Supplier #3, confirmed that he founded AI Conglomerate #1, the holding company which owns AI #4.

Based on the SAIC search results, it appears that 40% of the shares of AI Conglomerate #1 are held by a Hong Kong company called Shareholder #22 that is 100% owned by a company called Shareholder #23, which is a BVI company. Emails located in the Company records indicate that Shareholder #23 is controlled by Shareholder #3 and that it is through this BVI structure that Shareholder #3 maintains his shareholding in AI Conglomerate #1 and therefore the two AIs. A search seeking the identity of shareholders of Shareholder #23 was denied (shareholding information in the BVI is only available with the consent of the shareholder). The most current SAIC search results show that Shareholder #3 is currently the vice chairman of AI Conglomerate #1. During the interview with Shareholder #5, the IC Advisors were told that the information was out of date and that Shareholder #3 had transferred his shares to Shareholder #5 and his brother Shareholder #6 in 2009. However, SAIC search results showed that Shareholder #3 participated in a board resolution of AI Conglomerate #1 in 2010. The holding structure is illustrated in a chart attached to such emails.

(ii) AIs AI #6 and AI #5 Paying Potentially Connected Suppliers Supplier #4 and Supplier #5.

SF charts of BVI purchase and sale transactions indicate that in 2010, the AI AI #6 made over RMB 313 million in set-off payments on behalf of SF for BVI timber purchases from the Supplier #5 both of whom have a common supervisor as noted above. In 2009, AI #5, which is an AI identified by Management as also controlled by the same entity which controls AI #6, made over RMB 170 million in set-off payments on behalf of SF for BVI timber purchases from the Supplier #5. From 2007 to 2008, AI #5 made over RMB 499 million in set-off payments on behalf of SF for BVI timber purchases from Supplier #4. The IC intends to assess the implications of these potential relationships.

(f) Sale of Standing Timber to AI Potentially Connected to Supplier of that Timber

(i) Timber Bought from Supplier #3 and Sold to AI #4 and AI #2.

SF charts of BVI purchase and sale transactions indicate that from October 2008 to March 2011, SF sold a total of approximately RMB 145 million of standing timber to the AIs AI #2 and AI #4 that was purchased from Supplier #3. During the interview with Shareholder #5, the IC Advisors were told that the information was out of date and that Shareholder #3 had transferred his shares to Shareholder #5 and his brother Shareholder #6 in 2009. For further details about the relationship between AI #2, AI #4 and Supplier #3, please refer to Schedule VI.B.1.1.

(ii) Timber Bought from Supplier #8 and Sold to AI #3

SF charts of BVI purchase and sale transactions indicate that from July 2006 to December 2009, SF sold a total of approximately RMB 456 million of standing timber to AI #3 that was purchased from the connected Supplier #8. For details about the relationship between AI #3 and Supplier #8, please refer to Schedule VI.B.1.1.

(g) Lam Hon Chiu – Jiangxi Zhonggan

Certain of the related-party allegations in the MW Report concerned Lam Hon Chiu, who was characterized in the MW Report as an "executive" of the Company. The MW Report alleged, among other things, that Lam Hon Chiu was also the manager of two of the Company's "agents" (which agents were unnamed), as well as the legal representative and President of Supplier Jiangxi Zhonggan.

Management responded that Lam Hon Chiu, also known as Marco Lam, had once held the position of Vice-President, Business Development and Logistics, with the Company, but left Sino-Forest on July 22, 2007.

Management provided the IC with a letter of Sino-Panel (Asia) Inc. dated July 17, 2007, confirming the termination of Lam Hon Chiu's employment, effective July 23, 2007. The letter was acknowledged by Lam Hon Chiu on July 17, 2007. In addition, Management provided a copy of an Employee Termination Checklist dated July 22, 2007, acknowledged by Lam Hon Chiu on July 17, 2007, and an MPF Member Termination Statement for Employer in respect of Lam Hon Chiu issued by HSBC Life (International) Limited on November 7, 2007. These materials are attached as Schedule VI.B.1(g).

During the interview with Supplier Jiangxi Zhonggan on September 22, 2011 Lam Hon Chiu confirmed his previous employment with the Company. He further stated that Jiangxi Zhonggan, the Supplier of which he is legal representative, did not have any transactions with Sino-Forest until after his employment with it had ended.

(h) Relationship Mapping

The IC Advisors identified other possible relationships between SF, its parent and current employees and AIs and Suppliers.

To date numerous interrelationships and linkages between SF's current/former employees, and AIs, Suppliers, forestry bureaus and their current/former employees have been identified and further potential relationships continue to be identified as enquiries continue.

On the instructions of the IC, the IC Advisors have passed the details of possible relationships identified to date to Management for further follow up and explanation. As noted above, very recently, Management provided information regarding AIs and Suppliers and relationships among the Company and such parties. The IC is reviewing this material from Management and intends to report its findings in this regard in its final report to the Board.

2. E&Y Directors

Muddy Waters alleged that the Board appears to be a retirement plan for partners of E&Y. In particular, Muddy Waters suggested that there are currently five retired E&Y partners on the Board.

In fact, there are only two current directors of the Company who were formerly partners of E&Y, Mr. James Hyde and Mr. Garry West. Mr. Hyde left E&Y in 2002 to take a position in industry, and became a director of the Company in 2004. Mr. West retired from E&Y in June 2007 and became a director of the Company in February 2011. No other persons on the current Board have been E&Y partners.

It would appear that Muddy Waters confused Mr. Jamie Bowland, a recently departed director with a long career at BMO Capital Markets, with a "James Boland" - an American who sits on a public company board. While Mr. Jamie Bowland had advised that he worked briefly for a predecessor to E&Y in the 1970s, he was not a partner thereof.

Muddy Waters may also have confused Mr. W. Judson Martin, the Chief Executive Officer, with a "J. W. Martin" - a former E&Y partner who is not associated with the Company. Mr. W. Judson Martin has never been an E&Y partner or employee.

Finally, the Company has been advised by E&Y that Mr. Peter D.W. Wang has a similar name to an E&Y partner, although he, too, has not been an E&Y partner.

C. Globe and Mail Allegations re: Homix and Chen Hua

Homix is currently an indirect wholly owned subsidiary of the Company. Dayang is currently a wholly owned subsidiary of Homix. The Globe, in a story printed September 3, 2011, claimed that SAIC corporate filings for Dayang indicate Chen Hua, a Vice-President of SF, was also a shareholder in Dayang at the time of the sale of Homix to SF in 2010 for $7.1 million. The Globe characterized Dayang as a "unit of Homix" and stated that SF closed the purchase of Homix in June 2010. Muddy Waters says that SF paid Ms. Chen $7 million (without relating such payment to any particular transaction). Based on SF public disclosures at the time, the transaction was closed in January 2010.

Based on the Dayang SAIC filings that have been reviewed by the IC Advisors, the IC was able confirm that the SAIC filings do not show Chen Hua as holding an interest or a position in Dayang after January 28, 2008. The Homix sale is recorded in the SAIC filing and disclosed by SF as occurring on January 4, 2010. The SAIC searches show Chen Hua was a 30% shareholder (and Chair) from August 2003 to November 2004. She was again shown as a 30% shareholder for three days in January 2008. BJ advised the IC Advisors that Ms. Chen has stated to them that she was a nominee holder who held for the owner who was a friend. She further indicated to BJ that she acted as Chair in the initial stages as she had good relationships that were relevant to the business.

VII. OTHER MUDDY WATER ITEMS

VII. OTHER MUDDY WATERS ITEMS

The IC has not attempted to address every allegation made by MW but rather has focussed its review as previously described. Set out below are two additional of allegations of MW, which the IC also believes warrant comment.

A. Logging Versus Sale of Trees

One of the allegations in the MW Report was that, given logistics and operational realities, SF's Yunnan Province timber sales are largely fabricated. For example, Muddy Waters noted that Yunnan is a remote, rugged, mountainous province, making the prospect of harvesting any sizeable quantity of logs, even by hand, daunting. Moreover, even if the Company were able to harvest the logs claimed, the roads through the mountains are dangerous, with switchbacks and steep precipices. Roads leading into the agricultural areas are of an even lower quality and often unpaved. During the rainy season (from May to October), travel by road would be further complicated by mud and occasional landslides. According to the MW Report, the value of purchases made under the Yunnan MFA was overstated by approximately $800 million.

In response to these allegations, Management explained that, in fact, its revenue from Yunnan Province was solely the result of the sale of standing timber. No cutting or transport was involved, as the trees were sold as living trees and not harvested as logs.

The IC Advisors reviewed the Company's 2010 MD&A, the MD&A for the three months ended March 31, 2011, and the Q2s, and determined that this particular element did not require further investigation, as the Company's public disclosure supported Management's assertion that the revenue generated by the Company in Yunnan Province resulted from the sale of standing timber. For example, the 2010 MD&A stated that the revenue from broadleaf in Yunnan accounted for approximately 45.5% of standing timber revenue in the year ended December 31, 2010. The MD&A for the three months ended March 31, 2011 disclosed that during the three months ended March 31, 2011, the Company sold approximately 9,868 Ha. of plantations which were acquired under MFAs, mainly in the provinces of Guangxi, Yunnan and Hunan. Finally, the Q2s indicated that in the six months ended June 30, 2010, 92.9% of standing timber sales were of broadleaf from Yunnan Province.

B. Capital Hole

The MW report raises an allegation it refers to as the "Capital Hole". The essence of this allegation is that there is a gap between the capital available to SF in China which it could access through equity injections, debt and asset dispositions, and the capital SF reports to have spent in China on acquisitions.

Management was asked to address this allegation in its overall response to the MW allegations. Management's primary response is as follows:

> "MW's premise is that SF's business generated $3.5 billion of cash flow (after change in working capital components and changes in short term borrowings) but that SF purchased $5.0 billion worth of trees, thereby SF has a cash shortfall of $1.5 billion. Since Chinese government records only show between $0.7

> billion and $1.2 billion of investment by SF into the PRC, SF in China must be short of cash of between $0.3 billion and $0.8 billion. MW then argued that SF must not have been acquiring all of the trees that SF publicly discussed. In reality, the alleged cash short fall has been made up by fund raising exercises undertaken at the parent level outside of China. And not all of this cash raised has gone into China to fund trees acquisitions. In fact, the operating cash flow figures that MW used are taken from our financial statements and include expenses in the income statement and investments in working capital assets in Hong Kong that have been funded by capital raised at the parent level and kept in Hong Kong. The expenses have not been funded by operating cash flow in China. The expenses made in Hong Kong should not be included as deduction against the operating cash flow in China. For example, SF's selling, general and administrative expense and Interest for the period of time referred to the MW Report has been in excess of $0.7 billion. This amount has been wrongly deducted by MW from the China operating cash flow to arrive at the incorrect operating cash flow used in the MW report. This $0.7 billion has been funded by cash raised at the parent level and paid outside of China, and therefore this amount needs to be added back to the operating cash flow within China. The remaining of the alleged excess/shortfall in the MW Report is caused by MW wrongly lumping together the change in working capital components. Some of the change relates to onshore WFOE's and is funded by their operating cash flow in China, some of the change is related to the BVI plantation purchases and is funded by this model and some of the change is related to Hong Kong log trading business which is funded off shore by capital raised by the parent. For example, SF funded the Imported log trading business in Hong Kong (the investment in this business is included in the change in non-cash working capital components when determining operating cash flow) to the extent of $220 million. This amount needs to be added back to the operating cash flow. When one adjusts for these two amounts and includes the actual investment in China, one arrives at an excess funding scenario – there is no cash hole as MW so sensationally alleged."

The IC did not ask the IC Advisors to examine the capital hole allegation in favour of focusing on the primary issues described in Part I above.

VIII. VALUATION

VIII. VALUATION

Key allegations in the MW Report relate to the valuation of SF's standing timber holdings being overstated. The MW Report suggests that Poyry, the company retained by SF to provide certain valuation services, had been provided manipulated data and had its scope of work restricted by SF. The MW Report also suggests that timber holdings are overstated by way of alleging purchase transactions are fabricated.

Initially, the IC instructed the IC Advisors to focus on verifying existence and ownership of the assets, with a subsequent step being the valuation of those assets. The IC determined in August 2011 that the valuation exercise would need to run concurrently with the other efforts.

At the request of the IC, the IC Advisors pursued the engagement of an independent valuator with appropriate forestry expertise in China. The scoping of this project with a prospective valuator was completed. However, through the course of its own review, the IC determined it had material concerns with respect to such valuator's independence and did not proceed with it further. At the same time, SF was giving consideration to a course of action which would require a valuation of its own and, in order to avoid duplication of costs and effort, the IC determined it would combine its needs with those of the Company and proceed with a new process.

A key concern identified by the IC Advisors was the information from SF that longitude/latitude coordinates of standing timber plantations cannot be obtained from the Surveyor Reports. Such reports show GPS coordinates for the village/general area rather than detailed coordinates that would facilitate specific identification and a site-walk/examination.

The IC and Management are currently negotiating an engagement letter with an independent valuator pursuant to which it would conduct a valuation process in respect of a sample of SF's standing timber.

IX. OSC

IX. OSC

On June 8, 2011, the OSC announced it was investigating matters related to SF. A discussion of the OSC's investigation and the work of the IC in that regard is attached as Schedule IX, which is privileged and confidential.

X. E&Y

X. E&Y

As auditor, E&Y is entitled to inspect the books and records of the Company. The IC agreed and instructed the IC Advisors to keep E&Y informed as to the status of the IC's review process and have addressed questions of particular interest to E&Y in relation to the scope and progress of the review.

At the outset the IC provided E&Y with the first draft of the proposed work plan of PwC as submitted to the IC. The IC has continued to discuss the work plan with E&Y as it has developed. The IC also has given E&Y access to the Sino-Forest data captured by PwC on behalf of the IC.

A particular area of interest for the IC and E&Y has been Sino-Forest's relationships with AIs and Suppliers, particularly, the Hong Kong Sonic Jita and Yuda Wood relationships.

The IC has briefed E&Y regularly on the nature and progress of the IC's review in relation to the following topics:

- Cash;
- Fact Gathering;
- Management Response;
- Revenue Mapping;
- Relationship Mapping;
- Alleged Non-Arm's Length Relationships;
- Forestry Bureau Visits and Confirmations;
- Customer/Supplier Visits;
- Current Activities/Next Steps; and
- Timing.

XI. ROYAL CANADIAN MOUNTED POLICE (IMET)

XI. ROYAL CANADIAN MOUNTED POLICE (IMET)

The RCMP has advised the IC that it has commenced a preliminary investigation into the allegations of fraud asserted in the MW Report. Particulars of the IC's discussion with the RCMP to date are set out in Schedule XI, which is privileged and confidential.

XII. CASH

XII. CASH

As reported in the IC's First Interim Report, as a precautionary measure, the IC requested that PwC confirm SF's cash balances. PwC did this as of June 13, 2011 for both PRC accounts and "offshore" accounts. A total of 293 accounts controlled by SF in Hong Kong were confirmed, representing 100% of the expected cash position. There are a very significant number of accounts held by SF in China and the logistics and requirements of in person/in branch verification in that country led the IC to confirm only a portion of the China accounts (28 accounts, representing approximately 81% of the expected China cash position). The IC was satisfied that SF's expected cash position existed as at the date of the confirmation. The Board should be aware that SF only updates the details of its own cash position quarterly, so the confirmation results must be considered in this context. The IC has instituted certain additional controls over cash movements in excess of $1 million held in SF Hong Kong bank accounts in order to provide the IC with some precautionary comfort during the examination process.

XIII. NEXT STEPS

XIII. NEXT STEPS

Subject to the direction of the Board, the IC expects to complete its review prior to the end of 2011 and intends to:

(a) review the information and analysis recently received from Management relating to certain relationship issues;

(b) in cooperation with Management, engage an independent valuator to conduct a valuation process with a scope and parameters acceptable to the IC;

(c) such other steps as the IC, in its judgement, deems advisable in the discharge of its mandate; and

(d) submit its final report and recommendations to the Board.

The IC expects to be able to deliver its final report to the Board prior to the end of 2011.

GLOSSARY

GLOSSARY

"$" means, unless otherwise specified, U.S. dollars;

"**2010 Acquisition**" means the Company's acquisition of substantially all of the outstanding common shares of Mandra (not already owned by the Company) on February 5, 2010;

"**2010 AIF**" or "**AIF**" means the Company's annual information form for the year ending December 31, 2010;

"**2010 Annual Report**" means the Company's annual report for the 2010 calendar year;

"**2010 Financial Statements**" means the Company's audited consolidated financial statements and the notes thereto as at and for the year ended December 31, 2010;

"**2010 MD&A**" means the Company's management discussion and analysis for the year ending December 31, 2010;

"**AI**" means an authorized intermediary, an entity through which a BVI conducts its sales;

"**AIC**" or "**SAIC**" means China's State Administration for Industry and Commerce, the national authority responsible for administering industry and commerce;

"**AI HoldCo**" or "**AI Conglomerate #1**" means AI Conglomerate #1, a holding company that controls several AIs;

"**Audit Committee**" means the Audit Committee of the Board;

"**BJ**" means Bennett Jones LLP, Canadian counsel to the Company;

"**Board**" means the Board of Directors of SF;

"**BVI**" means a subsidiary of the Company incorporated in the British Virgin Islands;

"**Chart**" means the corporate structure chart provided to the IC Advisors by the Company and attached as Schedule II.C;

"**China**" means The People's Republic of China;

"**Chop**" means the seal typically used in place of signatures in China;

"**Company**" or "**SF**" or "**Sino-Forest**" means Sino-Forest Corporation and, where the context requires, its consolidated subsidiaries;

"**Counterparty**" means a party to an agreement with SF that is not a subsidiary of the Company;

"**CTO**" means the cease trade order of the OSC dated August 26, 2010;

"**Dayang**" means Jiango Dayang Timber Co. Ltd., a wholly-owned subsidiary of Homix;

"**E&Y**" means Ernst & Young LLP, the auditor of the Company;

"**Entrusted Sale Agreements**" has the meaning set forth in Section V.C.15;

"**forestry bureau confirmations**" or "**confirmations**" means documents issued to the WFOEs and BVIs on letterheads with forestry bureau names and featuring Chops (the seal typically used in place of signatures) that indicate that they had been issued by the corresponding forestry bureau, but does not include new confirmations;

"**FTI**" means FTI Consulting, a consulting firm advising the Company;

"**GAAP**" means the Generally Accepted Accounting Principles;

"**Gengma Dai**" means Gengma Dai and Wa Tribes Autonomous Region Forestry Company Ltd., an agent through which the Company purchases timber assets in the Yunnan region of China;

"**Globe**" means *The Globe and Mail*, a Canadian national newspaper;

"**Ha.**" means hectares, which is equivalent to 15 mu (statements of Ha. herein are approximate, given the rounding associated with the conversion of mu to Ha.);

"**Homix**" means Homix Limited, a company acquired by SF in June 2010;

"**Hong Kong Sonic Jita**" means Sonic Jita Engineering Co. Ltd., the Hong Kong incorporated parent company of Yuda Wood;

"**Hunan Forestry Entity #1 Confirmation**" means the new forestry bureau confirmation issued by Hunan Forestry Entity #1 (see Section V.C.9);

"**IC**" means the Independent Committee to the Board;

"**IC Advisors**" means one or more of PwC, Osler, Mallesons and JH;

"**IMET**" means an Integrated Market Enforcement Team of the RCMP;

"**Income**" means income from continuing operations before interest, other income, exchange losses and changes in fair value of financial instruments;

"**JH**" or "**Chinese counsel to the IC**" means Jun He Law Offices, independent Chinese IC counsel;

"**Jiangxi Zhonggan**" means Jiangxi Zhonggan Industrial Development Company Ltd.;

"**Mallesons**" means Mallesons Stephen Jaques, independent Hong Kong counsel to the IC;

"**Management**" means, at any time, the management of SF at that time;

"**Mandra**" means Mandra Forestry Holdings Limited, a wholly-owned subsidiary of SF;

"**Mandra Bonds**" means aggregate principal amount of $194,470,000 of 12% Guaranteed Senior Notes due May 2013 issued by Mandra Finance;

"**Mandra Finance**" means Mandra Forestry Finance Limited;

"**MD&A**" means management discussion and analysis;

"**MFAs**" means master framework agreements between various BVIs or WFOEs, on the one hand, and various Chinese entities, on the other, which establish a framework for the supply of standing timber to the Company in specified areas;

"**MOFCOM**" means China's Ministry of Commerce;

"**mu**" means a Chinese unit of measure for area, which is equivalent to 0.067 Ha;

"**Muddy Waters**" or "**MW**" means Muddy Waters, L.L.C.;

"**MW Report**" means the initial "research report" issued by Muddy Waters dated June 2, 2011;

"**OSC**" means Ontario Securities Commission;

"**Osler**" means Osler, Hoskin & Harcourt LLP, independent Canadian counsel to the IC;

"**Plantation Rights Certificate**" means a governmental registered certification of ownership issued by a forestry bureau in China to evidence certain forestry-related rights;

"**PwC**" means PricewaterhouseCoopers LLP, forensic accounting advisors to the IC;

"**Q2s**" means, collectively, the financial statements of the Company for the six months ended June 30, 2011 and the related MD&A;

"**RCMP**" means Royal Canadian Mounted Police;

"**RMB**" means Renminbi, the official currency of China;

"**SAFE**" means China's State Administration for Foreign Exchange;

"**SAIC**" means China's State Administration for Industry and Commerce, the national authority responsible for administering industry and commerce;

"**Sino-Panel (China)**" means Sino-Panel (China) Investments Ltd., a WFOE;

"**SP**" or "**Sino-Panel**" means Sino-Panel (Asia) Inc. (BVI), a BVI;

"**Staff**" means Staff of the OSC;

"**Subsidiary BVIs**" means, as of the date hereof, all BVIs, other than Greenheart Resources Holdings Limited;

"**Supplier**" means a supplier to the Company of plantation assets, either rights to standing timber or plantation/land use rights or both;

"**Survey Company #1**" means Survey Company #1, a survey company engaged by SF to provide it with surveyor services in connection with its plantation assets;

"**Survey Report**" means a Forest Resource Survey Report that accompanies BVI timber purchase contracts;

"**SW**" or "**Sino-Wood**" means Sino-Wood Partners, Limited, a Hong Kong incorporated subsidiary of SF;

"**TSX**" means Toronto Stock Exchange;

"**VAT**" means valued-added tax;

"**WFOE**" means a subsidiary of the Company incorporated in China as a "Wholly Foreign Owned Enterprise";

"**WFOE MFAs**" means the four MFAs entered into between WFOEs and vendor Counterparties from 2009 to 2011, described further in Section V.B; and

"**Yuda Wood**" means Huaihua City Yuda Wood Co. Ltd, a Supplier.