


THIS IS EXHIBIT "R" TO
THE AFFIDAVIT OF W. JUDSON MARTIN
SWORN MARCH 30, 2012

A Commissioner, etc.


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

November 13, 2011

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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 plantations⁴

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.

Forestry Bureau Confirmations and Plantation Rights Certificates

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, 2010⁸ 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

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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

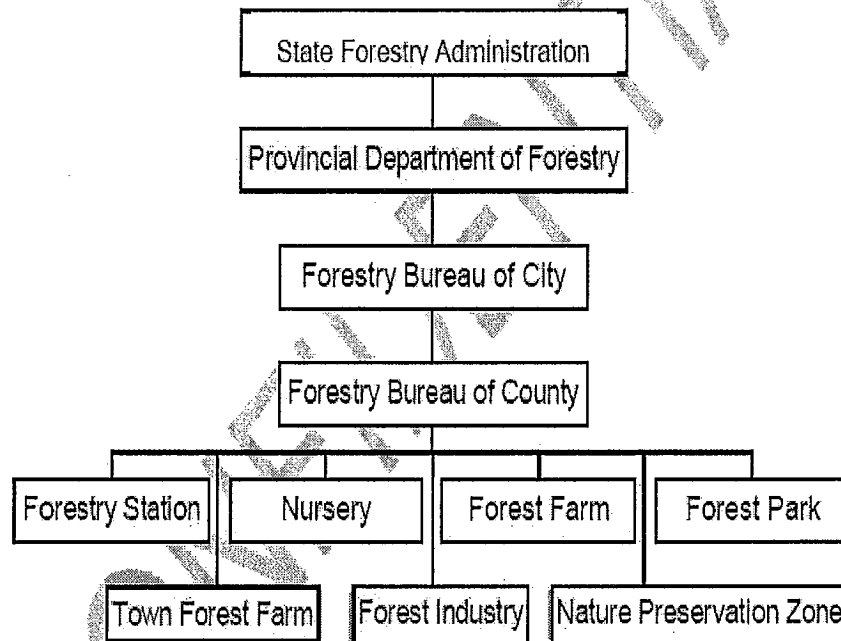
III. LEGAL REGIME

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) Forestry Administration - 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 hectareage 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 AI 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 previously 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 Partners [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, 2007 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.