

PRODUCT RULING - BR Prd 04/02

This is a product ruling made under section 91F of the Tax Administration Act 1994.

Name of the Person who applied for the Ruling

This Ruling has been applied for by Fletcher Challenge Forests Limited (“FCFL”).

Taxation Law

All legislative references are to the Income Tax Act 1994 unless otherwise stated.

This Ruling applies in respect of section CF 3(1)(b).

The Arrangement to which this Ruling applies

The Arrangement involves the payment by FCFL of a first return of approximately \$349 million of capital to shareholders (“the Return of Capital”) out of the proceeds of the sale by the FCFL group of its forest estate and related assets, and upon the cancellation of FCFL shares. The forest estate sale involves the sale of such assets held by FCFL wholly-owned subsidiaries, with the proceeds being repatriated to FCFL.

Further details of the Arrangement, and the background thereto, are as follows.

Sale of entire forest estate

1. On 16 June 2003 FCFL announced that it was seeking buyers for its entire forest estate. FCFL has now reached agreement to sell the forestry assets (excluding the interest held by the FCFL group in Tarawera Forests Limited: “the Tarawera interest”) for \$560 million to a group of three purchasers, namely, Kiwi Forests Group Limited, Viking Global New Zealand Limited and OTPP New Zealand Forests Limited (“the Purchasers”). The Purchasers will each purchase separate parts of the forestry assets.
2. Neither FCFL, nor any of its wholly-owned subsidiaries, are an “associated person” (as defined in section OB 1) with any of the Purchasers. At the time this Ruling was issued FCFL directors understood that the ownership of the Purchasers was as follows:
 - Kiwi Forests Group Limited was owned by four New Zealand resident investors, Messrs Trevor Farmer, Ross Green, Mark Wyborn and Adrian Burr;

- Viking Global New Zealand Limited was wholly-owned by a fund of institutional investors managed by Prudential Timber Investments, Inc of the United States of America;
 - OTPP New Zealand Forest Investments Limited was wholly-owned by The Ontario Teachers' Pension Plan of Canada.
3. On an initial settlement of the sale FCFL will receive \$351 million. The balance of \$209 million will be received as and when third party consents are granted to the transfer (to the Purchasers) of the interest of FCFL under various leases, forestry rights and joint venture arrangements that are part of the forestry assets. The consent process is expected to take seven months to complete.
 4. Receipt of proceeds from the sale of the Tarawera interest will depend upon when a buyer is located for that asset.
 5. The forest estate comprises approximately 80% of the total assets of FCFL. Following completion of the sale of the forest estate (including the Tarawera interest), the business of FCFL will comprise timber processing, marketing and distribution activities.

Return of sale proceeds

6. The Return of Capital is the first of two returns of capital planned for the sale proceeds. The Return of Capital is scheduled to occur in March 2004 and is expected to total approximately \$349 million. The second return of up to \$311 million (subject to determination of the sale price for the Tarawera interest) is planned to occur once all necessary third party consents have been granted and the outstanding purchase price payable by the Purchasers has been received together with receipt of the sale price of the Tarawera interest. Approximately \$65 million will be applied to meet transaction costs, working capital adjustments, repaying debt and forestry staff redundancies.
7. FCFL intends that the Return of Capital will be upon a pro rata cancellation of one out of every two current shares pursuant to an arrangement subject to the supervision of the High Court under Part XV of the Companies Act 1993. A payment of \$1.25 per share cancelled will be made and shares will be cancelled wholly and not in part.
8. FCFL will seek shareholder approval for the sale of the forestry assets and the first return of sale proceeds at a meeting of shareholders scheduled to be held on 20 February 2004. If shareholders approve, and if the High Court also approves, the first return of sale proceeds should be made some time in March 2004, with shares consequentially cancelled pursuant to the order of the High Court.
9. The funding for the Return of Capital will be derived from Fletcher Challenge Forests Industries Limited ("FCFIL") selling its shares in East Woodlands Ltd, Northwest Woodland Ltd and South Woodlands Ltd, as well as from FCFIL

selling some related forest plant and equipment. Each of these four companies are wholly-owned subsidiaries of FCFL. The funding will not reflect trading profits derived prior to the time of the Return of Capital.

10. The sale proceeds received by FCFIL will be used to repay debt owed to Fletcher Challenge Forests (Manufacturing) Limited (“FCFML”) of approximately \$351 million, which is another wholly-owned subsidiary of FCFL. These funds will then be used by other wholly-owned companies of the FCFL group to repay debt for the same amount owed within the FCFL group. Ultimately, the sale proceeds will be used by Fletcher Challenge Industries Limited (“FCIL”) to pay a dividend of approximately \$294 million to FCFL and to repay a debt to FCFL of approximately \$57 million.

Payment of dividends

11. FCFL has not paid a dividend since April 1998, as the financial position of the company has not allowed it. However, FCFL is now in a position where it could re-contemplate paying dividends. In this regard, FCFL management estimates that FCFL will be able to pay a dividend for the year ended 30 June 2005.

Level of reserves

12. FCFL’s reserves since 1998 were as follows:

Year	Total Reserves (\$m)
1998	211
1999	222
2000	481
2001	(44)
2002	(299)
2003	(579)

13. Any surplus cash accumulated before dividends are paid to FCFL shareholders will be applied as part of the capital expenditures on upgrading plant, repaying debt, and making investments to establish a suitable platform for FCFL’s processing and distribution activities.

Conditions stipulated by the Commissioner

This Ruling is made subject to the following conditions:

- a) None of the shares cancelled upon the Return of Capital are a “non-participating redeemable share” as defined in section CF 3(14).
- b) The share cancellation upon the Return of Capital constitutes a “pro rata cancellation”, as defined in section CF 3(14).

- c) The Return of Capital constitutes a “fifteen percent capital reduction”, as defined in section CF 3(14).
- d) At the time the Return of Capital is undertaken, it is not anticipated by the directors of FCFL that the associated returns to shareholders will affect the future dividend policy of FCFL.
- e) At the time the Return of Capital is undertaken it is not anticipated by the directors of FCFL that there will be a subsequent issue of shares.

How the Taxation Law applies to the Arrangement

Subject in all respects to any assumption or condition stated above, the Taxation Law applies to the Arrangement as follows:

- To the extent that it does not exceed the “available subscribed capital per share cancelled” (as defined in section OB 1), the Return of Capital will be excluded from the definition of “dividends” pursuant to section CF 3(1)(b).

The period or income year for which this Ruling applies

This Ruling will apply for the period from 13 February 2004 until 31 March 2006.

This Ruling is signed by me on the 13th day of February 2004.

Martin Smith

General Manager (Adjudication & Rulings)