



Annual Report  
2011

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## **Forward-Looking Statements**

There are statements in this document that are “forward-looking statements”. As these forward-looking statements are predictive in nature, they are subject to a number of risks and uncertainties relating to Tenon, its operations, the markets in which it competes and other factors (some of which are beyond the control of Tenon). As a result of the foregoing, actual results and conditions may differ materially from those expressed or implied by such statements. In particular Tenon’s operations and results are significantly influenced by the level of activity in the various sectors of the economies in which it competes. Fluctuations in industrial output, commercial and residential construction activity, changes in availability of capital, declining housing turnover and pricing, declining levels of repairs, remodelling and additions to existing homes in North America, relative exchange rates, interest rates in each market, and profitability of customers, can have a substantial impact on Tenon’s results of operations and financial condition. Other risks include competitor product development and demand and pricing and customer concentration risk.

All references in this document to \$ or “dollars” are references to United States dollars unless otherwise stated.

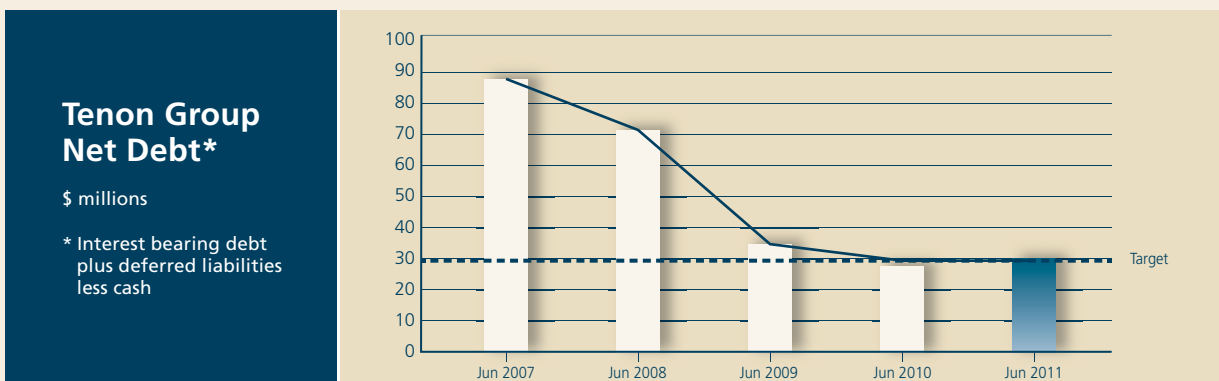
# Tenon Annual Review – 2011 Fiscal Year

## Tenon's Strategy and Progress

Over the past five years Tenon has undergone a major business transformation that has advanced the Company in almost all aspects of its operating activities. From both an earnings and share price perspective, the significant gains realised from this transformation process have, unfortunately, been 'swamped' by an extremely depressed US housing market, the likes of which have not been seen for over seventy five years. It is important, therefore, when looking at the progress that has been made, that we do so in the light of the operating environment that has prevailed over this period.

By way of review, the beginning of this five-year transformation saw us complete a series of growth orientated acquisitions, which included the purchase of Southwest Mouldings (a leading millwork distribution position in the large Texas market) for \$32 million, and the swap of our American Wood Mouldings joint venture holding for 100% ownership of Ornamental Mouldings (\$38 million in equivalent 100% value terms). As events transpired, the end of this acquisition phase coincided with the beginning of the deepest recession that has been seen in the US housing market since the 1930s depression. So, we then immediately set about significantly reducing our balance sheet debt as quickly as possible, whilst at the same time continuing to invest in our core business activities to ensure we maintained and grew our industry-leading position – with the aim of both actions being to secure the long-term future value of the Company.

As the chart below shows, through a tight focus on cash generation in each of our core activities, our balance sheet goal was reached quickly. Total net debt has reduced 65%, from a peak of almost \$90 million down to a target level of around \$30 million, despite the extremely difficult macro-environment over this period.



Our strategic positioning also advanced significantly over this same period, through a number of key initiatives, including our 'One-Company programme'. The first phase of this programme saw the elimination of \$5 million per annum in administrative and back-office costs through the implementation of a Group-wide shared services and back-office platform. The second phase involved a fundamental restructuring of the way in which Tenon services its core customers. Each customer would have a single interface at Tenon, no matter from where in the world, or in which Tenon manufacturing entity, their products were produced. This change resulted in a higher level of service delivery and product innovation, tighter customer relationships, and as a result the emergence of new business and product opportunities with our key customers. These opportunities ranged from new product introductions, to entering into completely new market segments, to organically growing our traditional business with existing customers.

This latter category, organic growth, has played a large role in our overall growth platform over the market downturn period. The achievement in this regard can be seen best in our US full service distribution businesses which now service some 40% more retail stores today than they did at the cycle peak in 2006-7. We now have six major distribution hubs in North America, directly servicing well over 1,100 separate North American locations, with our products now appearing in over 2,000 stores.

We believe Tenon has now built a unique industry position.

We have 100%-owned manufacturing operations in both New Zealand and North America. These operations are not only an important source of innovation for us in our product offerings to our customers, but they also offer certainty of supply needed when industry supply chains face serious circumstances outside their control (for example, the Chile earthquake which disrupted manufactured product supply out of that country only a year ago). In addition, our New Zealand manufacturing site located at Taupo is well placed to supply FSC certified wood product to meet the specific needs of the US market – particularly high value clear lumber, boards and mouldings from New Zealand's high quality pruned radiata forest resource. This offers us a strong competitive advantage over lumber sourced from other markets.

Our logistics platform combines this internally manufactured product together with extensive third-party sourcing across three continents, to bring a total portfolio of select millwork products to our customers. This mix of owned manufacturing and third-party global sourcing allows us to arrive at critical 'make or buy' decisions that maximise Group earnings under constantly changing market supply and demand, fibre supply, and currency conditions, whilst at the same time maintaining a full inventory of products in every store we supply. In our full service distribution operations, a fleet of trucks on programmed destination 'runs' make daily deliveries of products that have originated not only from Tenon's owned manufacturing sites in New Zealand, the United States and Canada, but also from third-party production facilities in other countries – for example, from China, Brazil and Chile. The logistics capability required to satisfy our customers' product and service needs is substantial, as by both necessity and design our product-to-customer supply chain reaches half way around the world. In some cases product orders can be met simply by accessing stock already residing in our US distribution hubs, whilst in other cases it may need to come from orders that we processed with offshore manufacturers three months ago for delivery into the US today. This aspect of the business has become more complex as the third-party sourced volume sold through our distribution businesses has grown over time. To put some numbers to this third-party sourcing growth, today Taupo (New Zealand) manufactured product represents less than 10% of our total US distribution sales.

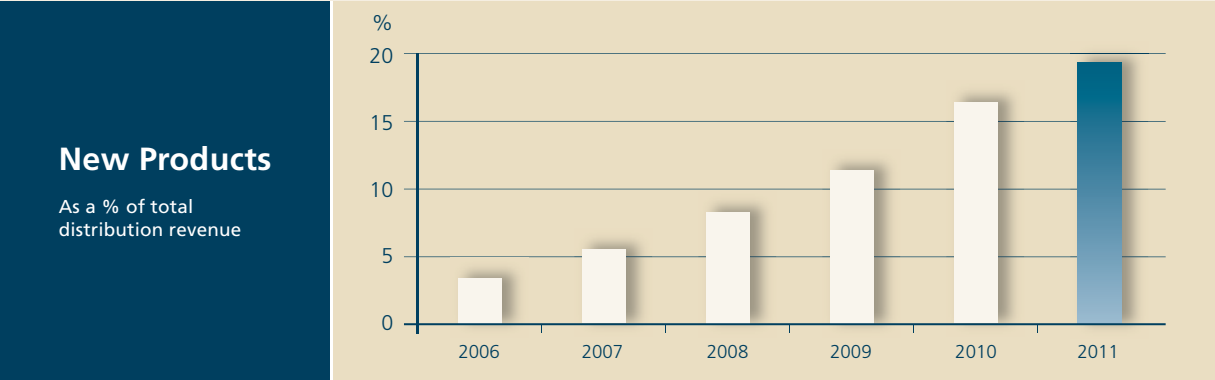
Whilst this logistics capability delivers the core products our customers need on a daily basis, and does so to their demanding quality and fill-rate requirements, traditional product delivery represents only one aspect of

our customer value proposition. So, for example, with our retail customers, innovation in new products and improving in-store service are also critical factors, as both can significantly improve their sales growth and overall store performance. We have advanced our offerings in both these areas.

In new product introductions, as previously reported, we have launched the National Trust Mouldings range which is already present in nearly 500 retail stores, the innovative RapidFit® moulding collection which can be installed over existing mouldings in situ, untreated primed finger-jointed boards, and (through a strategic partnership) Royal PVC synthetic boards. Our ArmourWood® range of treated trim board products represents product innovation in a new market segment. The relevance of the outdoor segment to us is the significant growth potential it offers, given that the total market size is approximately ten times that of our traditional indoor mouldings segment.



The chart below shows the positive impact that new product launches (including in the outdoor segment) have had on our US distribution activities. As you can see, almost 20% of our US distribution revenues today are represented by new products that we have introduced over the past 5-6 years.

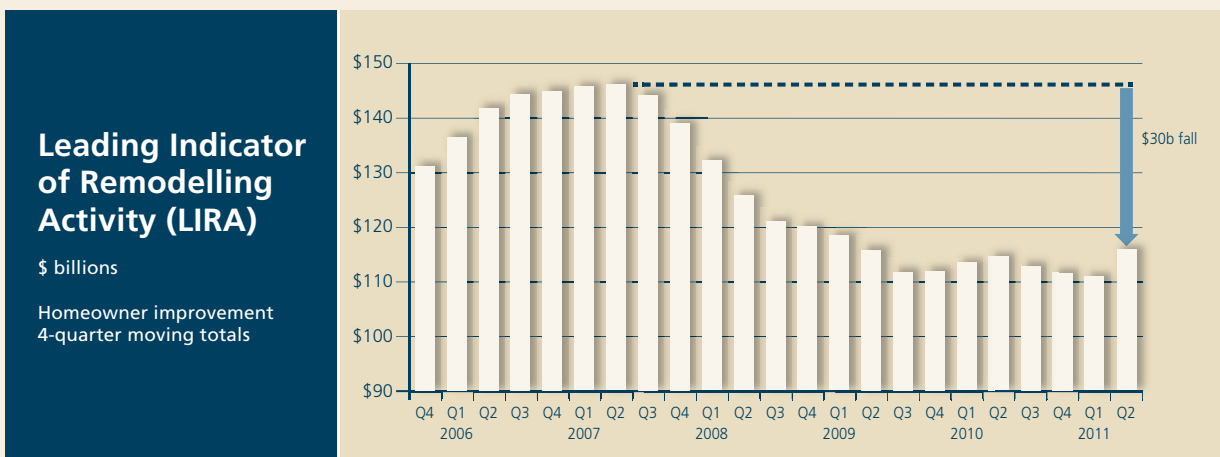
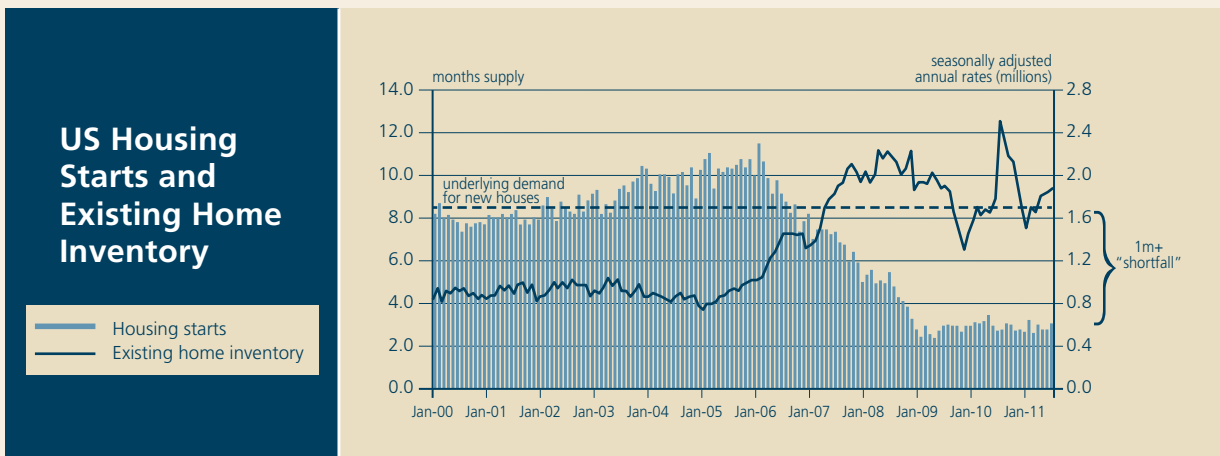


In terms of innovative service offerings, we can use the retail customer again as an example. Once our product reaches the stores, our full service distribution businesses stock the aisles, use proprietary IT systems we have developed internally to manage store SKUs and inventory replenishment, and through our analytics team apply the knowledge gained from this SKU management to develop targeted customer product offerings on both a regional and store-by-store basis. We believe that the incremental value that these performance management services generate for our customers differentiates our business model from others, and has helped to solidify our key customer relationships.

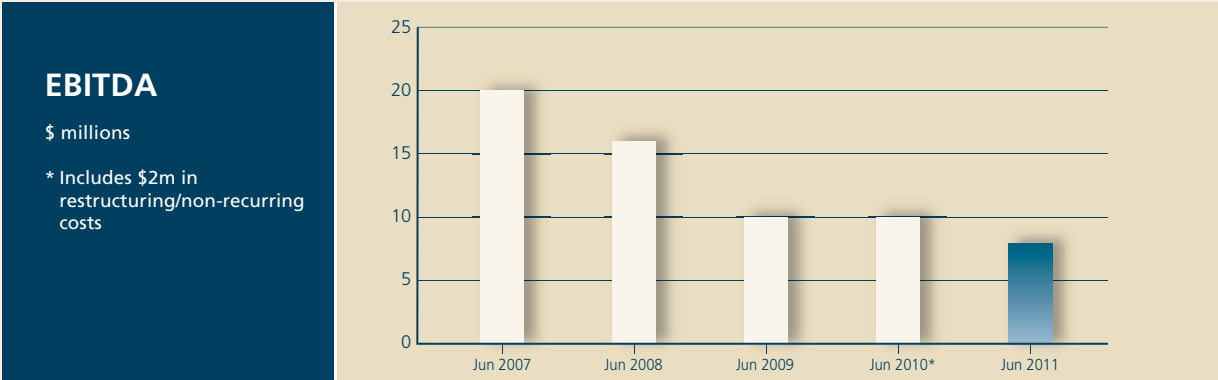
Our existing customer relationships, and the value we can deliver to those customers, offer us the opportunity to leverage our market position by expanding the range of products we can supply through these established channels, as well as providing us the opportunity to grow organically with our key customers as they expand their own market reach. These relationships have been built up over decades, and we constantly remind ourselves that we exist only as long as we continue to add significant value to our customers' customers. This can only come from a culture of 'customer-first', and this is transparent and fundamental to everything we do. Only by improving our customers' performance, can we continue to be successful and grow.

So, it is our unique mix of owned manufacturing facilities, a world-class logistics platform with extensive third-party global sourcing, a proprietary customer performance management programme, established relationships in the leading market channels, and a focus on innovation and the customer in everything that we do, that has allowed us to build a leading industry position – whether that be (for example) our number one position in interior mouldings sold through our full service distribution business, or our number one position in stair parts distribution in the large Texas pro-dealer market, or our number two position in imported clear and finger jointed mouldings sold through our US wholesale operation, or our position in decorative mouldings sold to the large format home improvement retailers.

As previously noted, this enviable position has been built in an operating environment that the US housing sector has not seen since the 1930s depression era. Shareholders will have read (in our previous Annual Reports) and heard a lot about this, so there is no need to repeat it again here in detail, other than to briefly comment upon the extent of the decline that has occurred by way of a few macro-driver comments.



The first chart, on the previous page, shows that new housing starts have declined quite dramatically, from a peak of 2.3 million houses per annum in 2006 down to only circa 600,000 per annum today – a fall of almost 75% - and today's unsustainably low level of activity has prevailed for the last three years. At the same time, the inventory of homes available for sale as measured in months of supply, has risen from a long-run level of 5-6 months to the current figure of 9.4 months. The second chart shows the decline in remodelling spend in the US that has occurred over a similar period – a reduction of some \$30 billion since 2007. While these macro drivers have obviously had a major and noticeable impact on our retail distribution activities in the US, our manufacturing operations at Taupo have, in addition, suffered significant cost pressures from increasing pruned log prices (a result of the strong China demand for wood fibre to meet China's domestic growth needs) and an oppressively high NZD:USD foreign exchange rate.



Given this environment, it is no surprise that Tenon's earnings have reduced over this period. Despite all of the profit improvement initiatives we have put in place, it has been impossible to offset the full extent of the market decline in the macro-operating environment given its magnitude. Indeed, with the level of demand drop-off that has been seen and the cost pressure from the rising NZD:USD exchange rate, the positive has been the extent to which our earnings have held up to date. The reason for that is as just discussed – i.e. through a combination of cost-out and rationalisation initiatives, organic growth with existing customers, new customer acquisition, and new product launches, we have been able to mitigate the full effect of the housing downturn.

We have further moved to lessen the impact on us of the US macro-environment by accessing opportunities outside of the North American market. By way of example, from its beginnings only a couple of years ago, the volume of manufactured product out of our Taupo site being sold into the China market already represents over 15% of all of our third-party sales from New Zealand.

Shareholders will know that while our prime focus is, naturally, on Tenon's absolute performance, we also keep a very close eye on the progress of our competitors, and on how Tenon's performance compares relatively. While the comparable universe is not large, we are comfortable that on most key metrics we have out-performed. One statistic may be enough to show this – i.e. the extent of decline in operating earnings over this down-cycle period. Tenon's earnings have dropped 60% across the five-year downturn, while the average of our peer group has dropped more than 100% over this same period. Clearly neither result is acceptable, but it is still worth acknowledging that in a very tough environment we are still doing better than 'the pack'.

When making these comparisons, it is true that we have been quite fiscally prudent over the course of the US housing downturn. As discussed, rather than being aggressively speculative, we have operated an FX strategy specifically designed to protect the earnings of our Taupo operation by mitigating the impact of the rising NZ dollar on our cost base – and in this past year that strategy added \$2 million to operating earnings. In recent years we have also chosen to expend financial resources on organically growing our business with our existing customers (in order to establish greater earnings leverage to the cyclical market recovery when it occurs), rather than to grow through acquisition, which to date we have considered carries a far greater risk profile and greater debt burden than organic growth. There will again come a time for acquisition through debt financing, but that time has certainly not been over the past 3-4 years, and we believe our decision in that regard has proved to be the right one. We have been aggressively focused on debt reduction, and we have avoided the temptation to re-leverage our balance sheet given that market conditions continued to be very uncertain.

We have not made dividend payments over this period, instead focusing on debt reduction and organic growth. While we understand that this policy may have been unpopular with some shareholders in the short-term, the longer-term pay-off from the use of these funds on organic growth and on building a stronger balance sheet will come with buoyant share price gain when the market recovery begins.

It is important to recall that our fiscal conservativeness allowed us to pass through the global credit crisis without needing to go back to our shareholders and ask for a fresh capital injection. It also allowed us to operate within our bank ratios when others struggled to do so. In this regard, we have always consciously moved early to refinance the Group's debt facilities when the opportunity has arisen to do so, in order to deliver the best possible outcome, rather than take the risk that volatility in debt markets might return again when our facilities are closer to their natural expiry dates. We did exactly this again in June this year, when, 12 months ahead of the then existing facility expiry we put in place a new \$57.5 million syndicated debt facility (with an additional \$12.5 million 'accordion' feature) under an asset-based lending structure. The term of the facility is five years, with an expiry date of June 2016. Being able to secure this new facility at this time, and on favourable terms that do not require us to meet fixed charge (e.g. interest) or leverage coverage requirements, is a reflection of the excellent market positioning that we have created and also of the strong banking relationships that have been established in recent years.

With an industry-leading position firmly established, Tenon is now very well positioned to take advantage of future growth opportunities in our home markets of North America and Australasia, and also in new geographies where we can earn superior margins through the application of our value-added product and service model.

## Fiscal 2011 Highlights

Overall, 2011 saw no respite from the difficult operating environment that has been with us for the past 3-4 years. The fiscal year began reasonably, but then US economic growth faltered in the second half, due to a combination of extreme weather conditions, high gasoline prices, global industrial supply chain disruptions following the earthquake in Japan, and most recently, the US federal budget debacle. These factors were reflected in lower consumer confidence, with many preferring debt reduction as a better use of discretionary income than investment in housing – whether that be house purchasing or home remodelling. Expenditure on housing was constrained further by the removal of the home buyer tax credit incentive, tightening access to credit, and falling house prices – important factors which slowed new buyers entering the market.

The latter part of the second half of the year saw a lower level of demand than the first, as uncertainty as to the strength of the US economic recovery grew. This can be seen in US GDP growth, which recorded average growth of 2.4% for the first six months of fiscal 2011 but only 0.8% for the second six months. These factors all flowed directly through to a lower demand level in the US housing sector, and ultimately also through to industry earnings, with operating revenues among US publicly traded wood products companies being down approximately 12% in the last quarter of the fiscal year compared with the corresponding quarter in 2010.

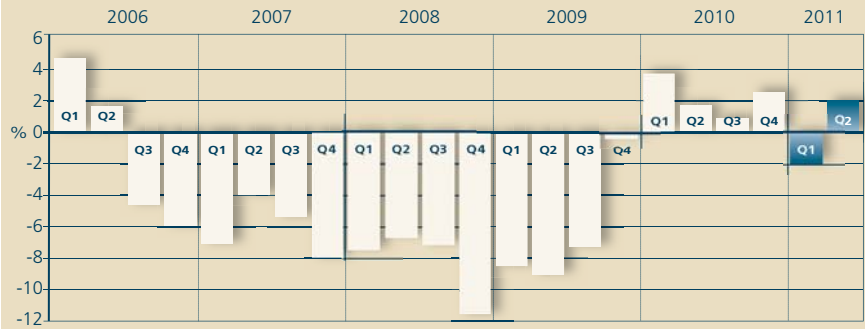
In summary, the charts on the next page show that almost all the key sector value drivers either remained flat or showed deterioration year-on-year.

Although the large home centre stores did begin to show some life in terms of their year-on-year store sales comparisons, unfortunately the millwork component in these numbers continued to lag the overall store performance, remaining in negative territory for the full period. New housing starts, although ending the year slightly up, were on average lower across the year than they were in 2010. Existing homes available for sale rose from 8.9 months of supply at the beginning of the year, to peak at 12.5 months during the year, before ending fiscal 2011 at 9.2 months.

The movement in each of the macro-drivers is reflective of the high current unemployment level in the US, declining equity in homes resulting from falling house prices, the high level of property foreclosures, and a lack of consumer confidence – issues that still remain to be addressed. Whilst it is clear that the current US economic woes may largely have stemmed from a debt-fuelled housing bubble, it must be equally clear that the answer to the economic problem also rests with the housing sector. Until house prices begin to rise, consumer confidence is unlikely to be restored – and neither of those two things can occur until credit availability for house lending is once again freed up to allow home sales (particularly the existing home inventory on the market) to return to healthier levels. The US home buyer tax credit incentive was removed during the year, making year-on-year operating comparisons difficult, however looking forward it is largely accepted by the US administration that support for the sector (hopefully by way of improved credit availability) will need to be put in place to assist the immediate short-term outlook. Added to the difficult US operating environment was the strengthening of the NZD:USD exchange rate, which moved from an opening level of 69 cents to close the fiscal year at just over 82 cents, averaging 76 cents for the year.

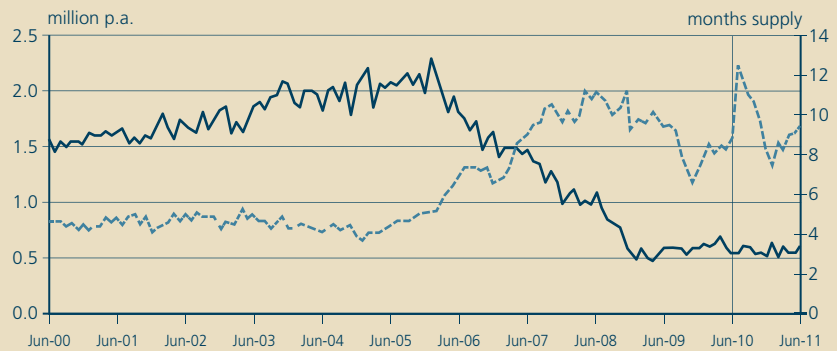
## "Big Box" Building Retailers Average (Total) Same Store Sales

% change from previous comparable period



## New and Existing Housing

— Housing starts (million p.a)  
 - - - Existing home inventory (months)



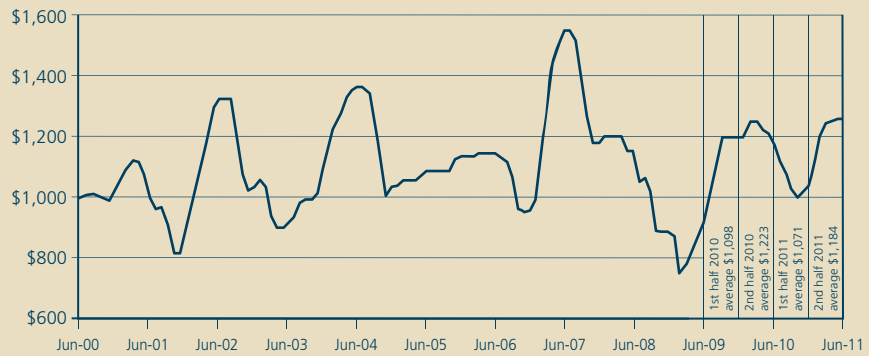
## NZD/USD Exchange Rate

NZD/USD exchange rates shown are effective (i.e. hedged)

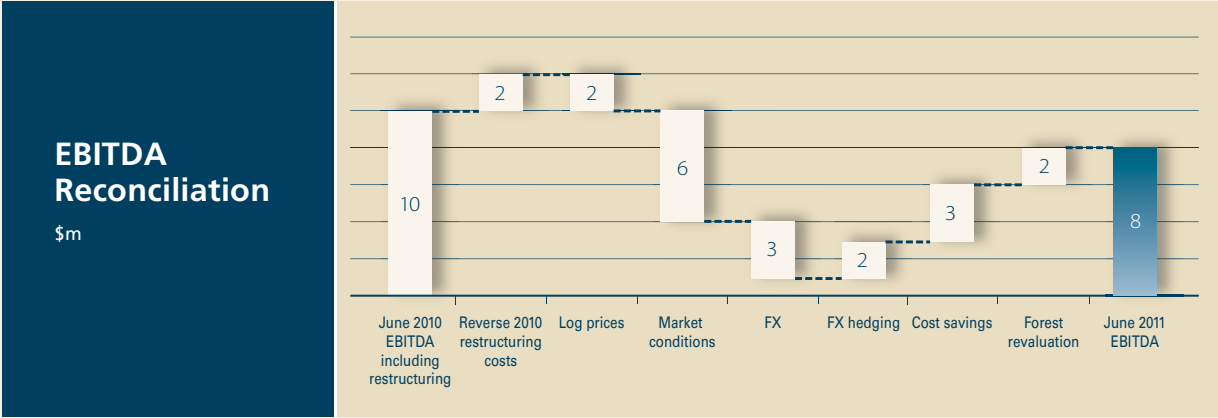


## Moulding & Better Lumber Pricing

US\$ mbf



Against this difficult market background, our operating earnings or EBITDA (i.e. earnings before interest, tax, depreciation and amortisations) declined from \$10 million (including restructuring charges of \$2 million) in fiscal 2010 to \$8 million in fiscal 2011 – in line with the market guidance we had previously issued to the NZX. Although simplified, the earnings reconciliation chart below provides a succinct summary of the key movements that drove the change in earnings year-on-year.



As this reconciliation shows, targeted initiatives were in place to address the lower level of demand that was faced during the year. For example, Tenon has retained some residual forest assets as a partial natural hedge to movements in log (i.e. feedstock) prices into the Taupo sawmill, and the revaluation of these forest assets in the period (as required under NZ IAS 41) offset the increase in the average log cost recorded across the year. We continued our financial and operational hedging strategies across the Group, which included establishing a three-year electricity hedge over one-third of our electricity usage at Taupo, effecting interest rate hedges over greater than 50% of our drawn debt today, and continuing our active foreign exchange cover strategy. This latter activity added some \$2 million to EBITDA as compared with the ‘do nothing’ alternative of simply taking cover on the day as required, and this hedging strategy offset two thirds of the adverse NZD:USD exchange rate movement that occurred in the period. We also benefited from actions taken last year which flowed through to this year’s earnings, the most significant of which was the rationalisation of US manufacturing activities which saw the closure of our Kok’s Woodgoods facility. This, together with other cost savings initiatives introduced in the period, added approximately \$3 million to EBITDA in 2011. However, the extensive cost-out programme that we have been continuously ‘renewing’, was only able to address 50% of the impact from a decline in market conditions, and it was primarily this difference that flowed through to reduce the earnings result for 2011.

As reported last year, fiscal 2010 included the positive sales impact from the Chile earthquake, however 2011 saw the negative impact of this event, as the temporary inventory spike last year which was needed to satisfy customer security of supply concerns had to fully clear the supply chain. The clearing process generated supply (and margin) pressures in fiscal 2011, and this is included in the ‘market conditions’ bar in the chart above. Overall, had it not been for the lingering impact of the Chile earthquake our earnings (inclusive of restructuring costs) would have been on a par with those recorded in fiscal 2010, despite a deteriorating operating environment. This is a reflection of the many positive operating initiatives we have in place across the entire Group that have targeted both the revenue and cost lines.

Some of these initiatives we put in place during the year did not actually impact the fiscal 2011 results, but will instead generate benefits in future periods. Examples of these include –

- Reducing the number of physical inventory locations used in our Fletcher Wood Solutions' US wholesale distribution activities, from 18 separate warehouse sites down to 11;
- Restructuring and strengthening our Asian sourcing function, which services (ex-China) our Empire, Southwest, and Ornamental operations in the US;
- At Ornamental, exiting lower contribution retail SKUs, and launching a new range of cabinetry products targeted at the kitchen cabinet professional contractors;
- Introducing new products for the budget conscious DIY consumer, such as 'RetroTread' and 'Easy Mantle'; and
- Launching the Creative Stairparts programme, which replaces an existing third-party source, allowing the programme to be brought 'in-house'.

Each of these is expected to produce earnings upside for us in coming periods.

Looking to other financial highlights, revenue of \$326 million was recorded, which although relatively flat year-on-year (\$329 million in 2010), was pleasing given the decline experienced in the wider US operating environment. Operating profit before financing costs was \$2 million (2010, \$4 million), and this combined with a favourable working capital movement, contributed to \$5 million of net cash from operating activities being generated in very difficult market conditions. A net loss of \$2 million was recorded, reflecting higher financing costs in the period (resulting from the establishment of the new five-year syndicated finance facility) and higher tax expense (with previously recognised US tax benefits being written-off as they expired unutilised). Without these two non-recurring factors, a break-even bottom line result would have been recorded (2010, \$2 million profit).

At \$52 million, our year end working capital level was in line with the levels reported at both June and December 2010, indicating that we have largely achieved the debt improvement to be gained from working capital optimisation. To this point, we closed fiscal 2011 with net debt of \$30 million, which compares with the \$29 million reported in June 2010 and the \$30 million level at December 2010.

As already discussed, on 24 June this year we put in place a new five-year syndicated debt facility. This new facility provides us with far greater operational flexibility than we have previously had, particularly in that it has no fixed charges (e.g. interest) or leverage coverage ratio requirements. Although our previous facility did not expire until June 2012, we took the opportunity to put in place the new facility well ahead of time in order to take advantage of a refinancing window we saw developing for asset-based financing of this type in our segment of the market. The timely closing of this financing deal was important, particularly given tumultuous global financial market movements since then.

## **Governance**

Our Annual Shareholder Meeting (ASM) was held in Wellington (New Zealand) in November last year. We had very high voting statistics, with approximately 82% of the Company's total issued shares being voted, and with all resolutions put to the meeting being passed with more than a 99% majority. This year our ASM will return to Auckland. Venue details and timing will be separately provided to shareholders with the Notice of Meeting.

Our CEO, Tom Highley, resigned during the year, and will be leaving the Company in early October. In every role Tom has held in his ten years with the Company, he has brought a tireless energy and enthusiasm to the accomplishment of the Company's strategic and operational goals. Since he took on the CEO role in 2009, he completely restructured the senior management roles to ensure the organisation is appropriately aligned with our key customers' needs. He has operated the Company through what have been the toughest housing and

credit market conditions that our sector has seen for more than 75 years. He is leaving the Company in very good strategic shape, well positioned to prosper when US housing market conditions recover. We wish Tom well for his future endeavours.

Following Tom's resignation, we announced the appointment of Tony Johnston to the role of Chief Operating Officer. Tony has over 20 years experience in international sales, marketing and distribution in the wood products sector, and he has actually returned to Tenon having formerly been a senior executive of the Company in its early stages of growth into the US. In that role he led the North American Consumer Solutions business, where he spearheaded Tenon's entry into the North American distribution market, at that stage to address the growing availability of high value product from our Taupo manufacturing operation. Whilst Tenon has since grown significantly from those initial beginnings, Tony's understanding of our market channels, the customer performance levels we must meet in order to be successful, as well as of the opportunities in the market to advance Tenon, will all be extremely valuable to us moving forward as we plan our growth strategy well beyond the current market downturn.

The Company is fortunate that it has strong management depth operationally, and that these senior management changes can occur seamlessly across the Group. The industry experience amongst the lead management team averages well over 20 years per manager today. This depth of industry knowledge and experience gives us considerable comfort that we will continue to meet our strategic and operational agenda moving forward.

## Looking Ahead

There are some strong positive fundamentals that will support, and drive, a recovery in the US housing sector. These include –

- US housing affordability at 40-year highs;
- US new home inventories at 40-year lows;
- US mortgage rates at 40-year lows;
- Robust population growth in line with long-term trends;
- Housing starts per head of population at 60-year lows;
- An aging US housing stock, with two-thirds of the total being greater than 25 years old; and
- US housing activity at well below underlying long-term demand.

To these last two points, US new home building is currently running at slightly over a third of the projected 1.7 million long-run level, and the median age of US homes is now over 35 years - so there is significant pent-up demand accumulating.

However, there are also some considerable hurdles to be overcome before a recovery can occur. These include the high unemployment level in the US, the back-log of foreclosed properties and unsold existing housing inventories, home prices that have fallen 30%+ from their peak through to today and have not yet stabilised, and restricted access to mortgage credit. These factors dictate that the outlook for the immediate 12 months period will remain uncertain. In addition, it is likely that Tenon will continue to be affected by a strong NZD:USD exchange rate, although the absolute level we will need to deal with over the next 6-12 months is an unknown. Indeed, there are so many moving variables that could make a significant difference to us in the short term, that it is extremely difficult to predict the course of our next fiscal year. By way of illustration, the chart on the following page tracks the NZD:USD exchange rate over a four week period in July-August this year. You can see that the volatility is extreme, and on an annualised basis the difference between the peak and the low in this chart translates into more than \$5 million in EBITDA to us (assuming all other variables are held constant).

## NZD/USD Exchange Rate



Given the current extreme volatility in the key industry factors that drive our earnings, it is possible to see EBITDA (before restructuring costs) outcomes for Tenon, for the first six months of the new fiscal year, ranging anywhere from 'flat' on the previous six-month period to break-even. Beyond that broad guidance, and for the reasons noted above, we will join our colleagues in the sector and refrain from giving a more precise statement at this stage. We will, however, update you on our earnings progress at our ASM later this year.

While short term earnings performance will still be largely dictated by the US housing market, the reality is that the macro-environment is largely an 'uncontrollable' for us. However, in terms of what we can control in our earnings outlook, we will continue to advance opportunities that will expand our earnings base by leveraging Tenon's existing specialty business model. In this respect, shareholders can expect to see the following types of activities in 2012 –

- New product innovation in high growth applications – particularly in the large outdoor segment. The intention is to announce a major new initiative this financial year;
- A restructuring of our NZ operations – to ensure they can operate profitably at a high NZD:USD exchange rate. Whilst this is likely to result in a short-term restructuring cost, any charge will be fully recovered within a 12 month period;
- Active participation in emerging supply trading opportunities – this may involve investment in wholesale markets in order to provide greater supply chain visibility; and
- Growth into non-US markets – particularly, China (as previously discussed), Australia and Europe.

Interestingly, the multiples at which our sector is now beginning to trade indicate that investors are starting to look beyond the next 12 months earnings period to assess value. As signs of market recovery emerge, investors will naturally select those companies best positioned to take advantage of the cyclical upside in the US housing sector – and for the reasons outlined in this Review, we believe Tenon will be an attractive investment in that regard.

Accordingly, the real value focus for Tenon must now clearly reside with those 'controllable' things that have the potential to strongly 'move the dial' in terms of value for our shareholders. In this regard, in order to drive efficiencies, industry consolidation is something in which Tenon can, and should, now play a key role. With an industry-leading position established, strong customer and channel relationships in place, 'best in class' full

service capabilities expanded, long-term debt financing recently secured for another five years, and management structure settled, Tenon is now well positioned to actively participate in this process – and we intend to do so over the coming period.

We will update you on our progress as events unfold.

As a final and very important note, we would like to thank all of our shareholders, employees and customers for their continued support throughout this past year. It is very much appreciated.

Sincerely,



Luke Moriarty (Chairman)  
26 August 2011



Tony Johnston (Chief Operating Officer)

# Financial Statements and Corporate Governance

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## Consolidated Income Statement for year ended 30 June

Tenon Limited		Note	Tenon Group	
2010 US\$m	2011 US\$m		2011 US\$m	2010 US\$m
–	–		<b>326</b>	329
–	–	5	<b>-241</b>	-236
–	–		<b>85</b>	93
–	–	5	<b>-72</b>	-72
–	–	5	<b>-13</b>	-15
–	–	5	<b>2</b>	-2
–	–		<b>2</b>	4
-16	<b>-17</b>	19	<b>-3</b>	-3
-16	<b>-17</b>		<b>-1</b>	1
–	–	6	<b>-1</b>	1
-16	<b>-17</b>		<b>-2</b>	2
			<b>8</b>	10
		5	<b>-6</b>	-6
			<b>2</b>	4
			<b>-2.8</b>	2.9

The accompanying notes form part of and are to be read in conjunction with these financial statements.

## Consolidated Statement of Comprehensive Income for year ended 30 June

Tenon Limited			Note	Tenon Group	
2010 US\$m	2011 US\$m			2011 US\$m	2010 US\$m
-16	<b>-17</b>	Net Profit/(Loss) after Taxation for the year		<b>-2</b>	2
-	-	Net movement of Cash Flow Hedges net of Tax	9	-	1
-13	<b>-43</b>	Movement in Currency Translation Reserve	9	<b>2</b>	-
-13	<b>-43</b>	Other Comprehensive Income for the year, net of Tax		<b>2</b>	1
-29	<b>-60</b>	Total Comprehensive Income for the year		-	3

The accompanying notes form part of and are to be read in conjunction with these financial statements.

## Consolidated Statement of Changes in Equity for year ended 30 June

Tenon Group	Note	Shares	Retained Earnings	Cashflow Hedge Reserves	Revaluation Reserve	Net Currency Translation	Total Group Equity and Reserves
		US\$m	US\$m	US\$m	US\$m	US\$m	US\$m
As at 1 July 2009		533	-408	-1	1	4	129
Net Profit/(Loss) after Taxation for the year		-	2	-	-	-	2
Other Comprehensive Income for the year		-	-	1	-	-	1
Total Comprehensive Income Attributable to the Equity holders of the Parent		-	2	1	-	-	3
As at 30 June 2010	9	533	-406	-	1	4	132
As at 1 July 2010		533	-406	-	1	4	132
Net Profit/(Loss) after Taxation for the year		-	-2	-	-	-	-2
Other Comprehensive Income for the year		-	-	-	-	2	2
Total Comprehensive Income Attributable to the Equity holders of the Parent		-	-2	-	-	2	-
As at 30 June 2011	9	533	-408	-	1	6	132

Tenon Limited	Note	Shares	Retained Earnings	Cashflow Hedge Reserves	Revaluation Reserve	Net Currency Translation	Total Group Equity and Reserves
		US\$m	US\$m	US\$m	US\$m	US\$m	US\$m
As at 1 July 2009		533	-476	-	-	8	65
Net Profit/(Loss) after Taxation for the year		-	-16	-	-	-	-16
Other Comprehensive Income for the year		-	-	-	-	-13	-13
Total Comprehensive Income Attributable to the Equity holders of the Parent		-	-16	-	-	-13	-29
As at 30 June 2010	9	533	-492	-	-	-5	36
As at 1 July 2010		533	-492	-	-	-5	36
Net Profit/(Loss) after Taxation for the year		-	-17	-	-	-	-17
Other Comprehensive Income for the year		-	-	-	-	-43	-43
Total Comprehensive Income Attributable to the Equity holders of the Parent		-	-17	-	-	-43	-60
As at 30 June 2011	9	533	-509	-	-	-48	-24

The accompanying notes form part of and are to be read in conjunction with these financial statements.

# Consolidated Balance Sheet as at 30 June

Tenon Limited		Note	Tenon Group	
2010 US\$m	2011 US\$m		2011 US\$m	2010 US\$m
<b>ASSETS</b>				
Current Assets:				
-	-		2	1
-	-	10	53	57
-	-	11	25	25
-	-	15	2	1
-	-		<b>82</b>	84
Non Current Assets:				
-	-	12	29	33
-	-	13	3	-
262	262	14	-	-
1	1		-	-
-	-	16	67	67
-	-	18	9	8
263	263		<b>108</b>	108
263	263		<b>190</b>	192
<b>LIABILITIES AND GROUP EQUITY</b>				
<b>Liabilities</b>				
Current Liabilities:				
-	-		-	1
1	1	17	26	30
-	-	19	1	6
1	1		<b>27</b>	37
Non Current Liabilities:				
-	-	19	31	23
226	286		-	-
226	286		<b>31</b>	23
227	287		<b>58</b>	60
<b>Group Equity</b>				
533	533	8	533	533
-497	-557	9	-401	-401
36	-24		<b>132</b>	132
263	263		<b>190</b>	192
Net Assets per Share (US\$)			<b>1.97</b>	1.97
Net Tangible Assets per Share (US\$)			<b>0.84</b>	0.85
Shares used for Net Assets per Share (millions)			<b>66.9</b>	66.9

The accompanying notes form part of and are to be read in conjunction with these financial statements.

For and on behalf of the Board  
19 August 2011



Chairman of Directors  
Luke Moriarty



Chief Executive Officer  
Tom Highley



Director (Chairman of Audit Committee)  
Michael Walls



Chief Financial Officer  
Adam White



## Reconciliation of Consolidated Net Earnings to Consolidated Net Cash from Operating Activities for year ended 30 June

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
		Cash was Provided from:		
-16	-17	Net Profit after Taxation	-2	2
16	17	Add Net Financing Expense	3	3
		Adjustments:		
-	-	Depreciation	6	6
-	-	Taxation	-	1
-	-	Asset valuation - Forest Assets <sup>(3)</sup> and Fixed Assets <sup>(4)</sup>	-2	1
-	-	Other	-1	-
-	-	Cash Flow from Operations before Net Working Capital Movements	4	13
-	-	Net Working Capital Movements <sup>(2)</sup>	1	-1
-	-	Net Cash from Operating Activities <sup>(1) (2)</sup>	5	12
		Net Working Capital Movements:		
-	-	Trade and Other Receivables <sup>(2)</sup>	2	2
-	-	Inventory	6	-7
-	-	Trade and Other Payables	-7	4
-	-		1	-1

(1) As per Statement of Cash Flows.

(2) Includes \$3 million reduction in net cash from the supply chain financing programme (June 2010: increase of \$6 million).

(3) Fair value adjustment to forest assets in 2011 year, refer to note 13.

(4) Impairment of fixed assets in 2010 year, refer to note 12.

The accompanying notes form part of and are to be read in conjunction with these financial statements.

# Notes to the Financial Statements

## 1 GENERAL INFORMATION

Tenon Limited (the Company) and its Subsidiaries (together the Group) is a processing, marketing and distribution business represented by one division - the Moulding and Millwork segment. The Group focuses on the North American market. The Group has strong direct and indirect supplier relationships for finished mouldings and boards with independent Pro-Dealers and with the two largest home improvement chains in the United States: Lowe's and The Home Depot and supplies appearance grade lumber to a number of US moulding and millwork manufacturers. As well as providing a channel to market for Tenon's New Zealand products, its wholly owned distribution businesses in the United States also source significant quantities of finished mouldings and millwork products from other suppliers.

The Company is a limited liability company incorporated and domiciled in New Zealand. The address of its registered office is 7 Fanshawe Street, Auckland, New Zealand.

The Company is listed on the New Zealand stock exchange. As at 30 June 2011 the Group was 57.96% owned by Rubicon Limited and its subsidiaries (June 2010: 57.96%).

These consolidated financial statements have been prepared on a consolidated Group basis and were approved for issue by the Board of Directors on 19 August 2011.

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## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these consolidated financial statements are set out below. These policies have been consistently applied to all years presented, unless otherwise stated.

### 2.1 Basis of Presentation

The consolidated financial statements presented are those of Tenon Limited and Subsidiaries (the Group).

### 2.2 Statement of Compliance

The financial statements have been prepared in accordance with New Zealand International Financial Reporting Standards (NZ IFRS) and other applicable financial reporting standards. The financial statements are in compliance with International Financial Reporting Standards (IFRS). The Group has designated itself as a profit-oriented entity for the purposes of compliance with NZ IFRS.

### 2.3 Basis of Preparation

The financial statements have been prepared in accordance with the requirements of the Financial Reporting Act 1993 and the Companies Act 1993 and comply with generally accepted accounting practice in New Zealand (NZ GAAP).

The presentation currency used in the preparation of these financial statements is United States dollars, rounded to the nearest million.

The accounting principles recognised as appropriate for the measurement and reporting of profit and loss and financial position on an historical cost basis have been applied, with the exception of derivative financial instruments, forest assets and assets held for sale which are stated at their fair value.

The preparation of financial statements in conformity with NZ IFRS requires the Group to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates (refer to note 3).

The Group financial statements consolidate the financial statements of subsidiaries, using the purchase method.

### 2.4 Changes in accounting policy and disclosures

#### (a) *New and amended standards adopted by the Group.*

No new standards or amendments to standards adopted by the Group in the current year had any impact on the Group.

The annual improvements project 2010 amended IAS 27 by giving additional guidance on the accounting for disposal or partial disposal of a foreign operation. The amendment states that the loss of control over a subsidiary, loss of control over an associate and the loss of joint control over a joint venture should be accounted for similarly. This amendment is effective for periods beginning after 1 January 2009 but has no impact on the Group's accounts.

# Notes to the Financial Statements continued

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

(b) *Certain new standards, amendments and interpretations to existing standards have been published that are mandatory for the Group's accounting periods beginning on or after 1 July 2011 or later periods.*

The Group has identified the following standards described below as relevant. The Group believes the annual improvements project 2010 and NZ IFRS 9 will not have a material effect on the Group's accounts but will require additional disclosure or format changes and amendments. The Group believes NZ IAS 24 will not have an impact on the consolidated financial statements. The Group has not early adopted the new or amended standards.

- Annual improvements project 2010. Key changes that may impact on the Group's accounts are amendments to:
  - IAS 1, 'Presentation of financial statements', the amendment allows an entity to present a breakdown of other comprehensive income in the statement of changes in equity or in the notes to the financial statements. This amendment is effective for periods beginning after 1 January 2011.
  - IAS 34, 'Interim financial reporting', the amendment places greater emphasis on the disclosure principles for significant events and transactions. This amendment is effective for periods beginning after 1 January 2011. Other amendments from the annual improvements project either relate to first time adopters of IFRS or are not relevant to the current structure of the Group.
- NZ IFRS 9 Financial Instruments: Classification and Measurement (mandatory for annual periods beginning on or after 1 January 2015). The major changes under the standard are:  
NZ IFRS 9 replaces the multiple classification and measurement models in NZ IAS 39 Financial Instruments: Recognition and Measurement with a single model that has two classification categories: amortised cost and fair value. The changes are designed to simplify the measurement of financial instruments.  
The impact on the Group is not expected to be significant. The Group will apply NZ IFRS 9 prospectively from 1 April 2015.
- NZ IAS 24 "Related Parties". In November 2009, the Accounting Standards Review Board approved a revised version of NZ IAS 24 "Related Parties". The main changes are not applicable to the Group as they relate to governments or government-related entities however the revision does include an amendment of the definition of a related party to clarify the intended meaning and remove some inconsistencies. The revised standard applies for annual periods commencing on or after 1 January 2011. The amendments will not impact the related party disclosures that the Group makes in its financial statements.
- Other interpretations and amendments that have been issued in the current period are unlikely to have an impact on the Group accounts and so have not been disclosed.

### 2.5 Basis of Consolidation

#### (a) *Subsidiaries*

Subsidiaries are entities that are controlled, either directly or indirectly, by the Parent Company. Control exists when the Parent has the power, directly or indirectly, to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that presently are exercisable or convertible are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

For acquisitions before 30 June 2009, the following purchase method of accounting was used to account for the acquisition of subsidiaries by the Group. The cost of an acquisition is measured as the fair value for the assets given, equity instruments issued and liabilities incurred or assumed at the date of exchange, plus costs directly attributable to the acquisition. Identifiable assets acquired and liabilities and contingent liabilities assumed in a business combination are measured initially at their fair values at the acquisition date, irrespective of the extent of any minority interest. The excess of the cost of acquisition over the fair value of the Group's share of the identifiable net assets acquired is recorded as goodwill. If the cost of acquisition is less than the fair value of the net assets of the subsidiary acquired, the difference is recognised directly in the income statement.

There have been no acquisitions subsequent to 1 July 2010, but if there had been the Group would have applied the purchase method of accounting as described above, modified by NZ IFRS 3 (Amendment) 'Business Combinations'. The most significant change to the purchase method of accounting brought about by the adoption of NZ IFRS 3 is that all costs relating to a business combination must be expensed and not capitalised to the cost of the acquisition. In addition subsequent remeasurement of the business combination would be required to be put through the income statement.

## Notes to the Financial Statements continued

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

#### (b) *Goodwill*

All business combinations are accounted for by applying the purchase method. In respect of business acquisitions that have occurred since 1 July 2004, goodwill represents the difference between the cost of the acquisition and the Group's share of the fair value of the net identifiable assets acquired. In respect of acquisitions prior to this date, goodwill was calculated by comparing the fair values of assets and liabilities of subsidiaries acquired to the purchase price of those assets and liabilities. Goodwill arising upon acquisition was amortised to earnings on a systematic basis and the balance of the goodwill was included in the accounts at its net carrying value at the date of transition to NZ IFRS.

Goodwill is stated at cost less any accumulated impairment losses. Goodwill is allocated to cash-generating units and is no longer amortised but is tested annually for impairment at each reporting date.

#### 2.6 Presentation and Functional Currencies

##### (a) *Presentation currency*

These financial statements are presented in United States dollars, which is the functional currency of the Parent and principal operating subsidiaries. The use of the United States dollar as the presentation currency is because the predominant functional currency of the Group entities is the United States dollar.

##### (b) *Functional currency*

###### (i) *Foreign operations*

Items included in the financial statements of each entity in the Group are measured using the currency that best reflects the economic substance of the underlying events and circumstances relevant to that entity (the "functional currency"). The functional currency of the Parent is the United States dollar.

The assets and liabilities of all of the Group companies (none of which has a currency of a hyper-inflationary economy) that have a functional currency that differs from the presentation currency, including goodwill and fair value adjustments arising on consolidation, are translated to the functional currency at foreign exchange rates ruling at the balance sheet date. The revenues and expenses of these operations are translated to the functional currency at rates approximating the foreign exchange rates ruling at the date of the transactions. Non-monetary exchange differences arising from the translation of foreign operations are recognised in the foreign currency translation reserve.

###### (ii) *Transactions*

Transactions in currencies other than the functional currency are translated at the foreign exchange rate ruling at the date of the transaction. Monetary assets and liabilities denominated in currencies other than the functional currency at the balance sheet date are translated to the functional currency at the foreign exchange rate ruling at that date. Foreign exchange differences arising on translation are recognised in the income statement.

Non-monetary assets and liabilities that are measured in terms of historical cost in a currency other than the functional currency are translated using the exchange rate at the date of the transaction. Non-monetary assets and liabilities denominated in a currency other than the functional currency are stated at fair value and are translated to the functional currency at foreign exchange rates ruling at the dates the fair value was determined.

## Notes to the Financial Statements continued

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

#### 2.7 Valuation of Assets

##### (a) Land, buildings, plant and equipment

Land, buildings, plant and equipment are stated at historical cost less accumulated depreciation and impairments. Land is not depreciated. Depreciation on Buildings, Plant and Equipment and Office Equipment is calculated on the straight line method. Expected useful lives, which are regularly reviewed, are:

Buildings	30 years
Plant and equipment	10 to 13 years
Office equipment	3 to 5 years

##### (b) Inventory

Trading inventory, raw materials and work in progress are valued at the lower of cost or net realisable value and are determined principally on the first-in-first-out basis. Cost includes direct manufacturing costs and manufacturing overheads at normal overheads at normal operating levels. Net realisable value is the estimated selling price in the ordinary course of business, less applicable variable selling costs.

##### (c) Trade receivables

Trade receivables are recognised initially at fair value and subsequently measured at amortised cost using the effective interest method, less provision for impairment. A provision for impairment of trade receivables is established when there is objective evidence that the Group will not be able to collect all amounts due according to the original terms of the receivables. The amount of the provision is the difference between the asset's carrying amount and the present value of estimated future cash flows, discounted at the effective interest rate. The movement in the provision is recognised in the income statement.

Trade receivables are derecognised when the rights to receive cashflows from the transaction have expired or have been transferred and the Group has transferred substantially all of the risks and rewards of ownership.

##### (d) Cash

Cash and cash equivalents comprise cash balances and call deposits. Bank overdrafts that are repayable on demand and form an integral part of the Group's cash management are included as a component of cash and cash equivalents for the purpose of the statement of cash flows.

##### (e) Assets held for sale and discontinued operations

Assets held for sale are assets whose carrying value will be recovered principally through sale rather than through continuing use. Assets held for sale are stated at the lower of their carrying amount and fair value less costs to sell and are not depreciated or amortised while they are classified as held for sale.

A discontinued operation is a component of the Group's business that represents a separate major line of business. Classification as a discontinued operation occurs upon disposal or when the operation meets the criteria to be classified as held for sale, if earlier.

##### (f) Forest assets

Forest Assets are standing trees on leased forest land, and are residual forest assets remaining after the sale of the majority of the Group's forest assets during 2004. Previously the Forests had been treated within discontinued operations and held at the lower of carrying value and fair value.

As the decision has been made to hold these forest assets through to harvest the assets are now valued at their fair value. All the costs necessary to maintain the forest assets are included in the income statement together with the change in fair value for each accounting period. The value is based on discounted forestry cashflow models where the fair value is calculated using cashflows based on sustainable forest management plans. The fair value is measured as the present value of cashflows from one growth cycle on leased forest land, taking into consideration environmental, operational and market restrictions.

## Notes to the Financial Statements continued

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

#### (g) *Impairment of non-financial assets*

The carrying amounts of the Group's non-financial assets are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, the asset's recoverable amount is estimated. An impairment loss is recognised whenever the carrying amount of an asset or its cash-generating unit exceeds its recoverable amount. Impairment losses are recognised in the income statement.

For goodwill, the recoverable amount is estimated at each balance sheet date.

Impairment losses recognised in respect of cash-generating units are allocated first to reduce the carrying amount of any goodwill allocated to cash-generating units and then to reduce the carrying amount of other assets in the cash-generating unit on a pro rata basis.

The recoverable amount of assets, other than receivables, is the greater of their fair value less costs to sell and value-in-use. In assessing value-in-use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the business. For an asset that does not generate largely independent cash flows, the recoverable amount is determined for the cash-generating unit to which the asset belongs. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount.

An impairment loss in respect of goodwill is not reversed.

An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognised.

#### 2.8 Valuation of Liabilities

##### (a) *Trade and other payables*

Trade and other payables are initially recognised at fair value and subsequently carried at amortised cost.

##### (b) *Provisions*

A provision is recognised in the balance sheet when the Group has a present legal or constructive obligation as a result of a past event, and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are measured at the Group's best estimate of the expenditure required to settle the present obligation. Provisions are determined by discounting the expected future cash flows at a rate that reflects current market assessments of the time value of money and, where appropriate, the risks specific to the liability.

##### (c) *Interest-bearing borrowings*

Interest-bearing borrowings are recognised initially at fair value less attributable transaction costs. Subsequent to initial recognition, borrowings are stated at amortised cost with any difference between cost and redemption value being recognised in the income statement over the period of the borrowings on an effective interest rate basis.

##### (d) *Deferred income tax*

Deferred income tax is provided in full, using the liability method, on temporary differences arising between the tax bases of assets and liabilities and their carrying amounts in the consolidated financial statements. Deferred income tax is not accounted for if it arises from initial recognition of an asset or liability in a transaction, other than a business combination that at the time of the transaction affects neither accounting nor taxable profit or loss. Deferred income tax is determined using tax rates (and laws) that have been enacted or substantially enacted by the balance sheet date and are expected to apply when the related deferred income tax asset is realised or the deferred income tax liability is settled. Deferred income tax assets are recognised to the extent that it is probable that future taxable profit will be available against which the temporary differences can be utilised. Deferred income tax is provided on temporary differences arising on investments in subsidiaries except where the timing of the reversal of the temporary difference is controlled by the Group and it is probable that the temporary difference will not reverse in the foreseeable future.

## Notes to the Financial Statements continued

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

#### (e) *Derivative financial instruments*

The Group uses derivative financial instruments for the purpose of managing its exposure to adverse fluctuations in interest and foreign currency exchange rates and commodity prices. While these instruments are subject to fluctuations in value, such fluctuations are generally offset by the change in value of the underlying exposures being hedged.

The Group policy specifically prohibits the holding or issuing of derivative financial instruments for trading or speculative purposes, however derivatives that do not qualify for hedge accounting are classified as financial assets at fair value through the income statement. These derivative financial instruments are initially recognised at fair value at the date the contract is entered into. The subsequent gain or loss arising from changes in the fair value of derivative financial instruments is recognised immediately in the income statement.

Where derivatives qualify for hedge accounting, recognition of any resultant gain or loss depends on the nature of the item being hedged.

#### (f) *Cash flow hedges*

For cash flow hedge transactions in which the Group is hedging the variability of future cash flows related to a variable-rate asset, liability or a forecasted transaction, the effective portion of the changes in the fair value of the derivative instrument are reported in the Statement of Changes in Equity and the Statement of Comprehensive Income. The gains and losses on the derivative instrument that are reported in the Statement of Changes in Equity and Statement of Comprehensive Income are reclassified to earnings in the Consolidated Income Statement in the periods in which earnings are impacted by the variability of the cash flows of the hedged item.

The ineffective portion of all cash flow hedges is recognised in current year's earnings in the Consolidated Income Statement.

The net interest received or paid on the contracts is reflected as interest income or expense of the related hedged position. Gains and losses resulting from the termination of contracts are recognised over the original period hedged as long as the underlying cash flows are still probable of occurring. If the hedged positions are sold, or the underlying cash flows are no longer probable of occurring, any unrealised gains or losses are recognised in the current period as net gains or losses on sales of interest-earning assets.

#### (g) *Fair value hedges*

Changes in the fair value of derivatives which are designated and qualify as fair value hedges are recognised in the Consolidated Statement of Income, together with any changes in the fair value of the hedged asset or liability that are attributable to the hedged risk. The gain or loss relating to the effective portion of interest rate swaps hedging fixed rate borrowings is recognised in the income statement within "finance costs". The ineffective portion of all fair value hedges is recognised in the Consolidated Income Statement.

### 2.9 Income Determination

#### (a) *Revenue recognition*

Revenue comprises the fair value of the consideration received or receivable for the sale of goods in the ordinary course of the Group's activities. Revenue is shown net of any value added tax, returns, rebates and discounts and after eliminating sales within the Group.

#### (b) *Goods sold*

The Group's revenue is mainly from the North American market where it has strong direct and indirect supplier relationships for finished mouldings and boards with independent Pro-Dealers and with the two largest home improvement chains in the United States: Lowe's and The Home Depot. The Group also supplies appearance grade lumber to a number of US moulding and millwork manufacturers. As well as providing a channel to market for Tenon's New Zealand products, its wholly owned distribution businesses in the United States also source significant quantities of finished mouldings and millwork products from other suppliers. Sales of goods are recognised when a group entity has delivered the product to the customer and/or the title and risk of loss has passed to the customer. Products are generally sold with volume discounts and customers have a right to return faulty product. Sales are recorded based on the price negotiated with the customer, net of estimated volume discounts and returns. Historical experience is used to estimate the level of returns likely and volume rebates are calculated on a preset formula.

#### (c) *Investment income*

Interest income is recognised in the income statement as it accrues, using the effective interest method.

## Notes to the Financial Statements continued

### 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES continued

#### (d) *Financing costs*

Financing costs comprise interest payable on borrowings calculated using the effective interest rate method and amounts payable in relation to the supply chain financing programme.

#### (e) *Leases*

The Group leases certain plant, equipment, land and buildings. Leases in which a significant portion of the risks and rewards of ownership are retained by the lessor are classified as operating leases. Operating lease payments are representative of the pattern of benefits derived from the leased assets and accordingly are charged to the income statement in the periods of expected benefit. Leases in which the Group assumes substantially all the risks and rewards of ownership are classified as finance leases. Upon initial recognition the leased asset is measured at an amount equal to the lower of its fair value and the present value of the minimum lease payments. Subsequent to initial recognition, the asset is accounted for in accordance with the accounting policy applicable to that asset.

#### (f) *Employee benefits*

Long service leave vests to the employee after varying periods of service. The Group's net obligation in respect of long service leave is the amount of future benefit that employees have earned in return for their service in the current and prior periods. The obligation is calculated using the projected unit credit method and is discounted to its present value. All actuarial gains and losses are recognised in the income statement.

### 2.10 Segmental Reporting

Operating segments are reported in a manner consistent with the internal reporting provided to the chief operating decision-makers. The chief operating decision-makers have been identified as the Tenon Group Board and the Executive Management team, who jointly make strategic decisions.

### 2.11 Goods and Services Tax (GST)

The Income Statement and Statement of Cash Flows have been prepared exclusive of Goods and Services Taxation (GST). All items in the Balance Sheet are stated net of GST, with the exception of trade receivables and trade payables, which include GST invoiced.

### 2.12 Research and Development Costs

All research costs are recognised as an expense when incurred. When a project reaches the stage where it is reasonably certain that further expenditure can be recovered through the processes or products produced, then further expenditure is recognised as a development asset. The asset is amortised from the commencement of commercial production of the product to which it relates, over the period of expected benefit.

### 2.13 Comparatives

Changes in prior year disclosure comparatives have been made to align with the current year presentation.

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## 3 CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

The Group makes estimates and assumptions concerning the future. The resulting accounting estimates may not equal the related actual results. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognised in the period in which the estimate is revised and in any future period affected. In particular, information about significant areas of estimation uncertainty and critical judgements in applying accounting policies that have the most significant effect on the amount recognised in the financial statements are described in the following:

- (a) Note 13 - Forest Assets
  - (b) Note 16 - Goodwill
  - (c) Note 18 - Provision for Current Taxation and Deferred Taxation
-

## Notes to the Financial Statements continued

### 4 RISK MANAGEMENT

This note presents information about the Group's potential exposure to financial, commercial and environmental risks that the Group has identified; the Group's objectives, policies and processes for managing those risks; the estimation of fair values of financial instruments; and the Group's management of capital. Quantitative disclosures of some of the key financial risks are made in note 20 of the consolidated financial statements.

#### 4.1 Approach to Risk Management

The Board of Directors has overall responsibility for the establishment and oversight of the Group's risk management framework. The Group actively operates a risk management programme, designed to minimise potential adverse effects on the Group's financial performance. The Group's risk management programme identifies and analyses the risks faced by the Group, sets appropriate risk limits and controls, and monitors risks and adherence to those limits. The Group uses an intra-Group web-based risk management system for standardised risk assessment and reporting.

Management reports to the Board on the key outputs of the Group's annual risk reviews. The Board establishes formal written policies covering specific areas, such as foreign exchange risk, interest rate risk, credit risk, use of derivative financial instruments and non-derivative financial instruments, and the investment of excess liquidity. The Board may waive or modify the application of such policies, and from time to time has done so, where particular circumstances make it, or have made it, appropriate to do so.

#### 4.2 Key Financial Risks

The Group's principal financial instruments comprise receivables, payables, bank loans and overdrafts, finance leases, cash and short-term deposits and derivatives.

The Group manages its exposure to the key financial risks - market risk (including commodity price risk, foreign exchange risk and interest rate risk), credit risk and liquidity risk - in accordance with the policies set down by the Board as discussed above. The Group enters into derivative transactions (principally interest rate swaps and forward currency contracts) to manage interest rate and currency risks.

##### (a) Market risk

The Group is exposed to changes in market demand, prices, foreign exchange rates and interest rates that affect the Group's earnings or the value of its holding of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimising returns. The Group enters into derivative transactions in order to manage market risks. All such transactions are carried out within the guidelines set by the Board of Directors as discussed above. The Group does not use derivative financial instruments for trading or speculative purposes.

##### (i) Price risk (input and output)

The Group operates in a competitive environment and takes all commercial actions necessary to minimise the risk of increasing input prices including operating procurement programmes to ensure raw materials are sourced on a competitive basis and the fostering of relationships with customers that allow the re-negotiation of selling prices in response to input/source price changes as appropriate.

Product prices, particularly in the US market, can be cyclical and volatile. Prices for the Group's products are influenced by North American housing inventory levels (new and existing), house price movement, housing construction levels, remodelling and renovation expenditure levels and other factors that affect consumer demand, such as employment levels and interest rates. Prices are also influenced by product availability, which can be a function of interest and foreign exchange variation, seasonal factors or supply availability and competition from a number of countries that supply products into the North American market, particularly New Zealand, North and South America and China. US lumber prices are particularly volatile, while US prices for finished products (such as mouldings) tend to be less volatile and on longer-term supplier programmes. Movements in the above factors materially affect the Group's financial performance. A movement of \$50 per thousand board feet in the sales price for Moulding & Better lumber is estimated to affect EBITDA by approximately \$0.75 million per annum assuming the Taupo sawmill is operating at full capacity. The average Moulding & Better 5/4 lumber price, per Crow's, in the 2011 fiscal year was approximately \$1,126 per thousand board feet (2010: \$1,160 per thousand board feet). Tenon can manage some of this pricing volatility by increasing or decreasing total production and/or internal consumption of the Moulding & Better lumber in the Taupo remanufacturing plant. Actual monthly sales volumes will vary depending on market and operating circumstances.

## Notes to the Financial Statements continued

### 4 RISK MANAGEMENT continued

Sawlogs are the key raw material for the Group's New Zealand based solid wood processing operations. A failure to secure wood supply could have a material adverse effect on the Group's New Zealand production. To mitigate this risk, the Group maintains specialist in-house procurement expertise and has a number of long-term sawlog supply agreements with the purchasers of its former forest estate and varies the grades of log utilised. The Group also purchases sawlogs under shorter-term supply arrangements and on the spot market. A movement in the average cost of logs of NZ\$1/tonne is estimated to affect EBITDA by approximately US\$0.3 million assuming up to 400,000 tonnes of logs are processed at full capacity on an annual basis.

In addition, should existing third party suppliers of sawlogs fail to maintain Forest Stewardship Council (FSC) Certification, or an equivalent certification, and the Group is unable to source replacement certified volume, this might result in the loss of some contracts to supply US customers who require that the wood they purchase come from forests that are managed according to internationally agreed social and environmental principles and criteria. The Group considers it currently has sufficient FSC certified volume available, but it is actively managing this risk, for example, by offering its customers the option of taking non-FSC products in certain product categories to minimise this risk.

The Group relies on international shipping being available at competitive prices for the distribution of its products, particularly those manufactured in New Zealand. Shipping contracts are typically 2 years in duration, with fixed container rates in US dollar currency for the contract period, subject only to fluctuations in fuel prices.

In December 2010, the Group entered into a 3-year electricity commodity contract to replace the previous contract that expired on 31 December 2010. The new commodity contract provides an economic hedge against approximately 33% (previous contract 75%) of electricity costs incurred at the Taupo site when the site is operating at full capacity. The new and old contracts were determined as effective hedges under NZ IAS 39 (Financial Instruments: Recognition and Measurement), with the 30 June 2011 and 30 June 2010 mark-to-market valuation adjustments being required to be taken to the hedging reserve in Group Equity.

Other than the above electricity commodity contract, during the year the Group did not use any commodity price swaps, futures or options to manage the market price risk of any commodities.

#### *(ii) Foreign exchange risk*

The Group operates internationally and is exposed to foreign exchange risk arising from various currency exposures, primarily with respect to the US dollar and the NZ dollar. Foreign exchange risk arises from future recognised assets and liabilities and net investments in foreign operations. The Group's functional currency is the US dollar. Accordingly, strengthening or weakening in the NZ dollar against the US dollar has had, and could have in the future, a material impact on the Group's financial condition or results of operations. Approximately 21% of the Group's 2011 costs and approximately 7% of the Group's 2011 revenues are incurred in New Zealand dollars, and approximately 3% of the Group's 2011 costs and 3% of the Group's 2011 revenues are incurred in Canadian dollars. In addition, log costs in New Zealand are linked to the US/NZ exchange rate, typically moving, after some delay, partially in correlation with New Zealand dollar export returns from logs or procured wood products. However, recent weakening in the US dollar and relative strengthening in the NZ dollar, combined with strong pruned log demand out of China to meet China domestic needs, has caused this historic correlation to weaken. The currencies of the Group's key non-New Zealand manufacturer competitors could also have a material impact on the Group's financial condition or results of operations. Such movements would be partially offset to the extent the Group's North American operations can leverage lower purchase prices from lower (in US dollars) cost countries. A 1 cent change in the value of the NZ dollar against the US dollar is estimated to have an impact on EBITDA of approximately US\$0.65 million at full operating capacity, assuming key pricing variables remain constant.

The Group uses forward contracts to manage its foreign exchange risk arising from future commercial transactions and recognised assets and liabilities. Foreign exchange risk arises when commercial transactions and recognised assets and liabilities are denominated in a currency other than the Group's functional currency.

The Group's policy is to manage currency exchange rate exposure to limit the impact that any adverse changes in foreign exchange rates might have on the Group's financial position, profitability or cash flow. Non-monetary assets are recorded in their functional currency, as determined by the dominant currency of cashflows, sales prices, sales markets, expenses and debt structure. The currency denomination and quantum of debt outstanding are managed so that economic risk exposure to currency movements on the aggregate of balance sheet and revenue items is offset within policy defined limits. Where the proportion of the underlying debt in any currency does not equate to the required proportion of total debt, derivative financial instruments may be entered into to manage the exposure within formal Board policies as discussed above.

## Notes to the Financial Statements continued

### 4 RISK MANAGEMENT continued

#### *(iii) Interest rate risk*

The Group's debt facility comprises a mixture of long-term debt and short-term LIBOR loans. Interest on both types of debt is based on LIBOR rates and can be for a term of one, two, three or six months, and borrowings issued at these short term variable rates expose the Group to market interest rate risk. Interest is also paid on a supply chain financing programme sponsored by the Bank of America based on LIBOR rates. The Group's policy is to manage its interest position depending upon underlying interest rate exposures and economic conditions. The Group manages its interest rate risk by using floating-to-fixed interest rate swaps. Such interest rate swaps have the economic effect of converting borrowings from floating rates to fixed rates. Borrowings issued at fixed rates expose the Group to fair value interest rate risk. The Group raises long-term borrowings at floating rates and when appropriate swaps them into fixed rates that are lower than those available if the Group borrowed at fixed rates directly. Under the interest rate swaps, the Group agrees with other parties to exchange, at specified intervals (mainly monthly), the difference between fixed contract rates and floating rate interest amounts calculated by reference to the agreed notional principal amounts (refer to note 20 (a) - exposure to interest rate risk).

#### *(b) Credit risk*

Credit risk is the risk of financial loss to the Group if a customer or counterparty to a financial instrument fails to meet its contractual obligations, and arises principally from the Group's receivables from customers and financial derivatives it has entered into.

##### *(i) Trade and other receivables*

The Group's exposure to credit risk is influenced by the individual characteristics of each customer or counterparty. Credit arrangements are entered into in accordance with limits set forth by the Group as to credit rating and dollar limits. It is the Group's policy that all customers who wish to trade on credit terms are subject to credit verification procedures including an assessment of their independent credit rating, financial position, past experience and industry reputation. In the United States, the Group has entered into credit insurance arrangements that cover approximately 48% of trade receivables as at 30 June 2011 (excluding national retail accounts), thereby reducing the Group's credit risk exposure. The total amount of policy cover is approximately \$6.75 million and is subject to certain blanket deductibles per Group entity and specific cover limits and deductibles for individual customers. The Group establishes a provision for doubtful debts based upon an estimate of losses expected in respect of trade and other receivables (refer to note 20 (b), credit risk, exposure to credit risk, for analysis of accounts receivable and note 4.3 commercial risk (a) market demand risk, for customer concentration risk). Tenon's largest customer is Lowe's, the second largest retail home store operator in the U.S. Whilst there is a degree of customer concentration with Lowe's, its credit rating has remained strong throughout the current US housing down-cycle and global credit crisis. Tenon has minimised the commercial credit risk with this customer by entering into the supply chain financing programme (refer to note 4.2 (c), liquidity risk) in respect of most of its receivables exposure with it. In addition, Tenon's strategy is to actively grow pro-dealer business to provide greater diversity of revenue and earnings streams.

##### *(ii) Financial derivatives*

The Group is exposed to counterparty risk in respect of potential default of a counterparty to a financial instrument, with the maximum exposure equal to the carrying amount of those instruments. Financial instruments are able to be spread amongst a number of financial institutions to minimise the risk of default of counterparties. Authorised counterparties for financial instruments (apart from electricity price hedge arrangements) are restricted to those financial institutions that form part of the Group's syndicated debt facility.

#### *(c) Liquidity risk*

The Group Treasury policy aims to maintain flexibility in funding by keeping committed credit lines available.

On 24 June 2011, a new long-term debt financing facility was established, replacing the Group's previous syndicated facility. The new facility is a syndicated facility structured on a group basis with JP Morgan Chase Bank, N.A. ("JP Morgan Chase") as Agent. The term of the facility is for 5 years. The facility is a \$57.6 million secured facility, comprising a \$50 million revolver facility and a \$7.6 million amortising term loan. In addition, the facility has an "accordion" feature whereby, with the approval of the bank syndicate, an additional \$12.4 million can be drawn upon (taking the total to \$70 million) without the need to negotiate a new banking arrangement.

The new facility is an "asset-based" lending facility, whereby the underlying assets and working capital of Tenon secure the obligations to the bank syndicate. The amount available for drawdown at any one time is determined by the value of the assets under a Borrowing Base covenant, based on the current value of the Group's inventory and receivables, reported to the Agent on a monthly basis, subject to certain prescribed exclusions, reserves and deductions. The Borrowing Base calculations are subject to periodic examination by the Agent during the remaining life of the credit facility (refer to note 19 (2)).

## Notes to the Financial Statements continued

### 4 RISK MANAGEMENT continued

The Group's banking facility requires a minimum "availability" Borrowing Base of \$7.5 million. At 30 June 2011, the amount of availability was \$21.9 million. Should availability fall below \$7.5 million at any time, this would result in a default under the terms of the banking facility giving the banks the right to impose certain restrictions on the Group's access to and use of its funds including demanding repayment of the amount borrowed, thereby requiring the Group to source alternative funding. The terms of the facility also include certain negative covenants in relation to acquisitions and dividends, each of which are limited to \$5 million per calendar year (without bank approval) and each subject to a minimum availability of \$12.5 million existing immediately after the acquisition or the payment of the dividend. In addition, the facility has an annual excess cash flow recapture provision of up to \$1 million to be applied against the balance of the term loan owing at the end of the relevant fiscal year commencing June 2012. The Group is also limited to the amount of third party borrowing, which cannot exceed \$5 million. With the exception of the provision relating to excess cash flow recapture, the new facility is not otherwise subject to earnings or fixed charge based financial covenants.

The supply chain financing programme announced on 16 June 2008 sponsored by the Bank of America, which allows Tenon the opportunity to receive payment from the Bank of America for a large portion of its receivables in advance of normal customer credit payment terms, is not affected by the change in these new bank facilities.

The Group's previous banking facility was entered into in July 2007 and was due to expire in June 2012. Before the new credit facility was entered into in June 2011, Tenon had a credit facility comprising of a revolver facility of \$35 million, an amortising term facility of \$10 million and a mortgages facility of \$2.7 million. This facility was subject to a borrowing base covenant and several financial covenants.

The borrowing base covenant required the Group to maintain minimum levels of assets as security for loans under the banking facility. The value of the assets under the Borrowing Base covenant was calculated based on the current value of the Group's inventory and receivables, reported to the Agent on a monthly basis, subject to certain exclusions, reserves and deductions as prescribed in the amendment. The Borrowing base calculations were subject to periodic examination by the Agent during the remaining life of the credit facility.

The financial covenants were calculated each calendar quarter. Failure to comply with these covenants would have resulted in a default under the terms of the banking facility giving the banks the right to cancel the commitments under the bank facility and/or demand repayment of the amount borrowed, requiring the Group to source alternative funding. The key financial covenants under the banking facility were the Leverage Ratio and the Interest Cover Ratio (terms as defined in the credit agreement).

The Group was at all times in compliance with the financial covenants throughout the period of the loan.

#### 4.3 Commercial Risk

The geographical nature of the Group's operations and history of the Group give the Group exposure to the following risks:

- Market demand risk
- Fletcher Challenge separation risk

##### (a) *Market demand risk*

Over 90% of the Group's earnings are sourced from the North American market. Material changes in market conditions have had, and will have, a material consequential effect on the Group's business. There is a risk of an adverse impact on the Group's business during periods of prolonged economic downturn in this key market.

Negative factors affecting the housing sector in North America, including credit market conditions, falling house prices, higher levels of housing inventory and reduced mortgage availability, have had and are having a material negative effect on the total consumption of building products and therefore the Group's level of revenue, earnings and cash flow. As at 30 June 2011, it remains uncertain as to how long the current negative market conditions may continue.

## Notes to the Financial Statements continued

### 4 RISK MANAGEMENT continued

The Group experiences strong competition in our global market. Radiata pine mouldings from Chile and other New Zealand suppliers and pine mouldings from the United States and Brazil compete with the Group's New Zealand manufactured Radiata pine mouldings in the North American market. Radiata pine lumber from Chile and other New Zealand suppliers and other lumber species from Canada and the United States compete with the Group's appearance grade lumber products. Increasing product supply from China also competes with the Group's products manufactured in North America. The Group purchases products from third parties to supplement products manufactured by the Group, particularly where it is more cost effective to do so.

Some of the Group's manufactured products are subject to competition from products which perform the same or similar functions. These include alternative wood types and non-wood products such as plastic composites. Changes in consumer preference in favour of these alternative products, comparative pricing levels of the competing products and technological advances of these products could all materially affect the Group's financial performance. The Group continues to explore new channels where there is opportunity for new products and as such changes in the market occur the Group will look to satisfy customer demand for new products. In addition, the Group is materially dependent on certain major customers for a significant portion of its revenues. The loss of one or more of these customers or a material loss of their business to a competitor, or a material reduction in the margin earned on the Group's product sales to these customers would have a material effect on the Group's financial performance. The Group's strategy is to continue to improve its product and service offerings to these customers to ensure the Group remains the most competitive and innovative supply partner in specific categories.

#### *(b) Fletcher Challenge separation risk*

Following the separation of the Fletcher Challenge Group, which was completed in March 2001, Tenon Limited remains as the continuing business of Fletcher Challenge Limited, the former ultimate parent company of the Fletcher Challenge Group. As some of the Fletcher Challenge Limited assets and liabilities were difficult to isolate or to transfer, prior to separation, the new owners of the former Fletcher Challenge divisions entered into an agreement with Tenon Limited (the Amended and Restated Deed Relating to Assets and Liabilities - "Deed") under which the economic benefits and risks of these assets and liabilities were assumed by the division to which they were properly attributed. Following separation, any claims made on Tenon Limited that are properly attributed to one or more of the other three divisions require Tenon to exercise its rights under the Deed to require payment from the relevant division or its successor or purchaser. Tenon is exposed to the risk that, in these circumstances, the relevant division (or its new owners) will not, or cannot, make the required payment. In more than ten years since separation only one claim has been made on Tenon that has required Tenon to seek to exercise its rights under the Deed. Under the terms of the Deed, Tenon attributed this claim to the relevant division and its purchaser, and it was settled by the purchaser with no material impact to Tenon.

#### 4.4 Environmental Risk

The Group considers that its activities currently comply in all material respects with applicable environmental laws and regulations. Failure to comply with these laws and regulations may result in orders being issued that could cause certain of the Group's activities to cease or be curtailed or may require installation of additional equipment at substantial cost. Violators may be required to compensate those suffering loss or damage by reason of violations and may be fined if convicted of an offence under such legislation.

Environmental due diligence is part of the investigative process for any acquisition of a business by the Group. The Group has historically been a party to a number of disposals of businesses and assets which included potential associated environmental exposures. An entity that created an environmental liability may continue to retain liability for the environmental exposure, notwithstanding any change of ownership. In addition, the New Zealand operations include historical environmental risks which are being monitored by the Company. The costs of environmental compliance and remedial work are generally included in the normal cost of conducting the Group's businesses.

The Group has no reason to believe that these costs vary significantly from similar costs incurred by other companies engaged in similar businesses. Assuming that the environmental laws and regulations are applied uniformly, the Group considers that its environmental compliance and remedial costs are not likely to have a material adverse effect on its relative competitive position or its financial position or results of operations.

The precise cost of any future compliance and remedial work will depend on, among other things, the nature and extent of the current and future environmental laws and regulations, the timing and nature of any required remedial work, the extent of any contamination, the technology available to meet the required standards, the determination of any liability in proportion to that of other parties and the extent to which any costs are recoverable from third parties.



## Notes to the Financial Statements continued

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
<b>6 INCOME TAX EXPENSE</b>				
Current Taxation:				
-	-	United States	-	-1
-	-	New Zealand	1	-
-	-	Total Current Taxation	1	-1
-	-	Taxation Expense/(Benefit)	1	-1
Net Profit/(Loss) before Taxation				
-16	-17	New Zealand	-	2
-	-	United States	-1	-1
-16	-17		-1	1
-5	-5	Taxation at 30 cents per dollar	-	-
Adjusted for:				
-	-	Expenses/(Income) not included in Assessable Income	-	-1
-	-	Tax losses written off	18	1
5	5	Valuation allowance	-	-
-	-	Taxation Expense/(Benefit)	1	-1

### Imputation Credit Account and Dividend Withholding Payment Account

The Imputation Credit Account and the Dividend Withholding Payment Account for the Group and Tenon Limited as at 30 June 2011 were nil (June 2010: nil).

	Tenon Group	
	2011	2010
<b>7 NET EARNINGS PER SHARE</b>		
Basic and Diluted Net Earnings per Share (cents)	-2.8	2.9
Numerator for Basic and Diluted Net Earnings per Tenon Share (\$ millions)	-2	2
Denominator for Basic and Diluted Net Earnings per Tenon Share (millions), refer to note 8.	66.9	66.9

	Tenon Group and Parent	
	2011	2010
	US\$m	US\$m
<b>8 CAPITAL</b>		
<b>Capital</b>		
<b>Reported Capital:</b>		
Reported Capital at the beginning of the year	533	533
Reported Capital at the end of the year	533	533

	Tenon Group and Parent	
	2011	2010
<b>Tenon Ordinary Shares<sup>(1) (2)</sup></b>		
Number of Shares at the beginning of the year	66,850,661	66,850,661
Number of Shares at the end of the year	66,850,661	66,850,661

(1) These shares are authorised, issued and fully paid and have no par value.

(2) Includes 182,548 (June 2010: 182,548) fully paid Tenon Limited Ordinary Shares held by the Tenon Employee Share Purchase Scheme, accounted for as treasury stock.

## Notes to the Financial Statements continued

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
<b>9 RESERVES</b>				
<b>Retained Earnings</b>				
-476	<b>-492</b>	Opening Balance	<b>-406</b>	-408
-16	<b>-17</b>	Net Profit/(Loss) after Taxation	<b>-2</b>	2
<b>-492</b>	<b>-509</b>		<b>-408</b>	-406
<b>Cash Flow Hedging Reserves<sup>(1)</sup></b>				
-	-	Opening Balance	-	-1
-	-	Fair Value Gains for the year	<b>1</b>	1
-	-	Hedge Gains Transferred to Earnings in the year	<b>-1</b>	-
-	-		-	-
<b>Revaluation Reserve<sup>(2)</sup></b>				
-	-	Opening Balance	<b>1</b>	1
-	-		<b>1</b>	1
<b>Net Currency Translation<sup>(3)</sup></b>				
8	<b>-5</b>	Opening Balance	<b>4</b>	4
-13	<b>-43</b>	Net Variations on Translation of Foreign Currency Financial Statements	<b>2</b>	-
<b>-5</b>	<b>-48</b>		<b>6</b>	4
<b>-497</b>	<b>-557</b>	<b>Total Reserves</b>	<b>-401</b>	-401

(1) The Hedging reserve records the effective portion of the gain or loss on a cash flow hedging instrument that is determined to be an effective hedge. As at 30 June 2011 the balance comprises the effective portion of the fair value gains on foreign exchange contracts and the fair value loss on an electricity hedge contract at the Group's Taupo operation. (The 30 June 2010 balance comprised the effective portion of the fair value gains on foreign exchange contracts, the fair value loss on an electricity hedge contract at the Group's Taupo operation, and the fair value loss on an interest rate swap).

(2) The Revaluation reserve arose in November 2006 when the Group announced that it had exited its 50% investment in AWM and acquired 100% of Ornamental Mouldings. As the Group had previously held an indirect 25% shareholding in OMI through its investment in AWM, the acquisition of Ornamental Mouldings was treated as a two-step acquisition for accounting purposes and accordingly, under NZ IFRS 3 Business Combinations, Tenon's share of the reserves of Ornamental Mouldings when it was an associate was recognised as a revaluation reserve on consolidation.

(3) The Tenon Limited currency translation movement of \$43 million in the June 2011 year (June 2010: \$13 million) arises on the translation of intercompany New Zealand dollar advances at balance date. These advances are eliminated on consolidation of the Tenon Group. Under IFRS, investments in subsidiaries are held at cost and are not revalued to reflect exchange rate translation movements, investments in subsidiaries are also eliminated on consolidation. The current year movement in the currency translation reserve results in Tenon Limited equity reported as a negative \$24 million when presented in US dollars for reporting purposes only.

## Notes to the Financial Statements continued

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
<b>10 INVENTORY</b>				
-	-	Raw Materials and Work in Progress	4	4
-	-	Finished Goods	49	53
-	-		<b>53</b>	<b>57</b>

The cost of inventory recognised as an expense and included in cost of sales amounted to \$241 million (June 2010: \$236 million).

		<b>11 TRADE AND OTHER RECEIVABLES</b>		
-	-	Trade Debtors <sup>(1) (2)</sup>	19	19
-	-	Prepayments	3	3
-	-	Other Receivables	3	3
-	-		<b>25</b>	<b>25</b>

(1) Trade Debtors were \$19 million (June 2010: \$22 million) lower than they would otherwise have been as a result of the introduction of the supply chain financing programme in July 2008, refer to note 4.2 (c).

(2) The Group's exposures to credit and currency risks and impairment losses related to Trade Debtors are disclosed in notes 20 (a) and 20 (b).

		<b>12 FIXED ASSETS</b>		
Cost				
-	-	Land and Improvements	6	5
-	-	Buildings	19	19
-	-	Plant and Equipment	76	79
-	-	Total Cost	<b>101</b>	103
-	-	Impairment on Plant and Equipment <sup>(1)</sup>	-	-1
Accumulated Depreciation				
-	-	Buildings	-7	-6
-	-	Plant and Equipment	-65	-63
-	-	Total Accumulated Depreciation	<b>-72</b>	-69
-	-	Total Fixed Assets at Net Book Value	<b>29</b>	33
Domicile of Fixed Assets				
-	-	New Zealand	13	16
-	-	United States	16	17
-	-	Total Fixed Assets at Net Book Value	<b>29</b>	33

	Land & Improvements US\$m	Buildings US\$m	Plant & Equipment US\$m	Total US\$m
Net Book Value 1 July 2009	5	14	18	37
Additions	-	-	3	3
Impairment <sup>(1)</sup>	-	-	-1	-1
Depreciation Charge	-	-1	-5	-6
Net Book Value 30 June 2010	5	13	15	33
Additions	1	-	1	2
Depreciation Charge	-	-1	-5	-6
Net Book Value 30 June 2011	6	12	11	29

(1) The Asset impairment in the June 2010 year related to the closure of one of five manufacturing facilities in North America. The carrying value of the impaired plant was written down to fair value less estimated costs to sell.

## Notes to the Financial Statements continued

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
<b>13 FOREST ASSETS</b>				
-	-	Opening Balance	-	-
-	-	Reclassification of forest assets	1	-
-	-	Gain attributable to fair value changes	2	-
-	-	Closing Balance	3	-

The Group has an interest in a forest asset growing on leased forest land (358.8 hectares) and the forestry rights to several forest assets growing on other forest land (78.7 hectares). The lease on the forest land expires in 2075 and the forestry rights expire between 2022 and 2046. The forest assets comprise a combination of clearwood (pruned) and framing (unpruned) stands in 4 separate locations. The forest assets form part of the security supporting the Group's global credit facility. The forests were residual assets remaining after the sale of the majority of the Group's forest assets in 2004 and had been classified as a discontinued asset under NZ IFRS 5, and valued at the lower of historic cost or fair value less costs to sell. In 2011, the decision was made to hold the current crop through to harvest, and the assets have now been valued under NZ IAS 41 "Biological Assets" and presented in the accounts as forest assets.

### Valuation

The carrying value of our forest assets in these Financial Statements is their fair value of \$3.4 million. This is derived from a current, independent forest valuation, as at 30 June 2011, which valued the forests at \$3.4 million (net of selling costs). The independent valuation assumes a post-tax cashflow assumption, an historical 4 quarter average pricing series to March 2011, and a transaction derived discount rate of 7% (real after-tax). Although Tenon is entitled to replant the land once harvesting is complete, the valuation only assumed a single rotation. The first stand is projected to be harvested in 2014. As Tenon does not own the forest land, carbon tax credits were not assumed.

As noted above, Tenon intends to hold the forest crop through to harvest. As the Group currently has sufficient carried forward New Zealand tax losses to offset the forecast assessable net income earned upon harvest, it is unlikely that tax will need to be paid on the positive net cashflows generated from the forest assets. On current discount rate and cashflow assumptions, the Company expects that the discounted net cashflows from the forest assets will exceed our carrying value and the independent valuation.

### Sensitivities

The fair value estimate is sensitive to changes in the log price at mill or wharf gate log price and to changes in the discount rate. A 10% change in log prices is estimated to change the fair value of the forest asset as at 30 June 2011 by \$0.3 million. A 1% change in the discount rate is estimated to change the fair value of the forest asset as at 30 June 2011 by \$0.3 million.

### Risk

As the Group operates a sawmill in Taupo in New Zealand that processes logs (total purchases of logs processed by the sawmill in the June 2011 year was \$40 million), there is a partial natural hedge where decreases/increases in the forest valuation due to log price changes are partially offset with increases/decreases in the cost of raw materials used by the Taupo sawmill.

## Notes to the Financial Statements continued

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
		<b>14 INVESTMENTS</b>		
262	<b>262</b>	Investment in Subsidiary Companies (refer to notes 24 and 26)	–	–
262	<b>262</b>		–	–

### 15 ASSETS HELD FOR SALE

The company owns approximately 12.5 hectares of bare land adjacent to the Taupo manufacturing site surplus to current operational needs which the company is actively marketing for sale.

–	–	Opening Balance	<b>1</b>	1
–	–	Currency translation and revision to costs to sell <sup>(1)</sup>	<b>1</b>	–
–	–	Closing Balance	<b>2</b>	1

(1) During the year, costs to sell were revised by \$0.3 million (June 2010: nil). Currency translation of the assets was \$0.2 million (June 2010: nil).

### 16 GOODWILL

–	–	Goodwill at beginning of the year	<b>67</b>	67
–	–	Balance at end of year	<b>67</b>	67

Goodwill is allocated to the Group's cash-generating units (CGUs) as determined at acquisition.

–	–	The Empire Company	<b>49</b>	49
–	–	Ornamental Mouldings Group	<b>18</b>	18
–	–		<b>67</b>	67

Tenon has allocated goodwill to two Cash Generating Units ("CGUs") being, firstly, Tenon's 100% ownership interests in its full service distribution activities comprising The Empire Company and Southwest Moulding Co., and, secondly, Tenon's 100% ownership interests in the Ornamental group. All business operate within Tenon's primary business segment. In the prior year Tenon reported The Empire Company and Southwest Moulding Co., as separate CGUs. The combining of The Empire Company and Southwest Moulding Co., reflects the further integration of the distribution businesses during the fiscal year under Tenon's management approach, reflecting Southwest Moulding's joint participation with Empire in supply chain and shared service activities, and the sharing of common customers and suppliers. As a result, the operating activities and cash flows of The Empire Company and Southwest Moulding Co., have to an increasing extent, become integrated since the acquisition. The reduction of three CGU's down to two CGUs has had no material effect on the impairment review of purchased goodwill carried out at the end of the fiscal year. Further integration of activities is taking place across the Group during fiscal 2012.

The recoverable amount of a CGU is determined based on value-in-use calculations. These calculations use discounted cash flow projections over a five year period. These cashflows assume a recovery from the currently depressed market conditions (but at a more moderate rate than previously assumed due to the prolonged depressed state of the housing market in North America) such that by year 5 of the projections (i.e. the terminal year) Tenon's consolidated EBITDA is projected to be \$32 million (June 2010 Annual Report estimate \$35 million).

Key assumptions used in the value-in-use calculations for each CGU are as follows, together with commentary on key sensitivities:

(1) For the purposes of the value-in-use calculations, the weak operating environment seen since 2008 is not forecast to materially improve until fiscal 2013. Longer term annual sales growth rates of between 5% and 7% are assumed for years 2013 to 2016, consistent with the assumption that long term growth in the new homes and remodelling markets gradually moving up from the bottom of the economic cycle, together with continued expansion from new stores and growth in market share from new products.

(2) Gross margin percentages are assumed to be similar to the current year's percentage for the next 5 years (i.e. +/- 2%).

(3) The discount rate applied to the cash flow projections was 8.3% pre tax (2010: 8.3%).

As the value in use significantly exceeded the carrying value plus allocated goodwill of the CGUs, no impairment existed at 30 June 2011.

## Notes to the Financial Statements continued

### 16 GOODWILL continued

#### Sensitivities

Sensitivity analysis was applied to each of the CGUs to determine whether under realistic scenarios there may be an impairment in goodwill. Even after applying these sensitivities, the value-in-use calculations for each CGU shows excess value significantly greater than the carrying value of the goodwill.

A sensitivity analysis shows that there would be no goodwill impairment even if:

- the discount rate was increased to 11% pa; or
- the compound annual sales growth rate assumption was halved
- the gross margin was held constant at current levels.

The results of the sensitivities apply to the previous CGU reporting structure as well as the CGU reporting structure applied for this fiscal year and going forward as described above.

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
<b>17 TRADE AND OTHER PAYABLES</b>				
–	–	Trade Creditors	14	17
–	–	Accrued Employee Benefits	4	6
1	1	Other Payables	3	3
–	–	Accruals	5	4
1	1		26	30
<b>18 PROVISION FOR CURRENT TAXATION AND DEFERRED TAXATION</b>				
Provision for Current Taxation:				
–	–	Opening Provision for Current Taxation	–	-1
–	–	Current Taxation (Expense)/Benefit in the Consolidated Income Statement	-1	1
–	–	Deferred Tax Movement during the year	–	2
–	–	Net Tax Payments/(Refund)	1	-2
–	–	Provision for Current Taxation Liability	–	–
Deferred Taxation:				
Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current tax assets against current tax liabilities and when the deferred income taxes relate to the same fiscal authority.				
The offset amounts are as follows:				
Deferred Taxation:				
–	–	Deferred Tax on Assets	9	7
–	–	Deferred Tax on Liabilities	–	1
–	–	Deferred Tax Asset	9	8
The gross movement on the deferred income tax account is as follows:				
Non Current Deferred Taxation:				
–	–	Opening Deferred Taxation	8	9
–	–	Effect of Currency Translation	1	1
–	–	Deferred Tax Movement during the year excluding tax losses written off	1	-2
–	–	Net Taxation losses written off <sup>(1)</sup>	-1	–
–	–	Deferred Tax Asset	9	8

(1) Previously recognised US tax losses that expired during the year or are due to expire in 2012/2013 have been expensed (\$1 million).

On 5 November 2009, the Worker, Homeownership and Business Assistance Act was passed in the US. The Act allows companies with net operating losses in the 2008 and 2009 tax years to carry back those losses for up to 5 years, subject to certain limitations. During the 2010 year the amount of the tax refund received by Tenon's US group of companies under the Act was \$3.2 million.

## Notes to the Financial Statements continued

### 18 PROVISION FOR CURRENT TAXATION AND DEFERRED TAXATION continued

On 20 May 2010, the New Zealand Government announced the removal of tax depreciation on buildings with an expected useful life of over 50 years. This change required Tenon to recognise a one time deferred tax liability on its New Zealand buildings in the 2010 financial statements. The tax impact of the change of \$1.4 million has been included within the 2010 year's tax benefit line on the Consolidated Income Statement as an expense. Tenon recognised additional previously unrecognised losses of \$4.8 million (\$1.4 million grossed up at 30c) in the year to 30 June 2010 to offset the impact of the change in this treatment of depreciation for taxation purposes.

	Depreciation US\$m	Forestry US\$m	Provisions US\$m	Tax Losses <sup>(1)</sup> US\$m	Current Assets US\$m	Total US\$m
<b>June 2010</b>						
Opening Provision for Deferred Taxation	–	–	1	8	–	9
Effect of Currency Translation	–	–	–	1	–	1
Tax losses refund (refer to foot note on note 18, page 39)	–	–	–	-3	–	-3
Deferred Taxation in the Income Statement:	-1	–	–	2	–	1
Closing Provision for Deferred Taxation	-1	–	1	8	–	8
<b>June 2011</b>						
Opening Provision for Deferred Taxation	-1	–	1	8	–	8
Effect of Currency Translation	–	–	–	1	–	1
Tax losses expensed in Income Statement	–	–	–	-1	–	-1
Deferred Taxation in the Income Statement:	-1	-1	-1	5	-1	1
Closing Provision for Deferred Taxation	-2	-1	–	13	-1	9

(1) Recognised tax losses include \$6.7 million of NZ tax losses (June 2010: \$4.2 million), that do not expire, subject to shareholder continuity provisions, and \$5.9 million (June 2010: \$3.8 million) of US tax losses which have an expiry date as detailed below.

	Expiry Dates				
	Total US\$m	2013 US\$m	2014 US\$m	2015 US\$m	2022 and beyond US\$m
<b>US Tax Losses</b>					
Gross Value	16.8	1.7	4.6	0.5	10.0
Tax Effected	5.9	0.6	1.6	0.2	3.5

Tenon has taxation losses in excess of the amount that can be recognised under NZ IFRS. NZ IFRS allows the recognition of taxation assets when utilisation is considered probable, which is subject to the future earnings of the Tenon Group and shareholder continuity. Tenon has \$26 million in unrecognised NZ tax losses, and no unrecognised US tax losses (June 2010: \$21 million NZ losses and \$6 million US losses).

Tenon Limited				Tenon Group	
2010 US\$m	2011 US\$m			2011 US\$m	2010 US\$m
<b>19 FINANCIAL COSTS AND DEBT</b>					
<b>Finance Costs</b>					
–	–	Interest Payable on Debt		1	3
–	–	Interest Payable on Supply Chain Financing		1	–
–	–	Amortisation of Refinancing Fees <sup>(1)</sup>		1	–
16	17	Interest Payable on Inter Company Advances (refer to note 24)		–	–
16	17	Net Financing Expense		3	3
<b>Non Current Debt</b>					
–	–	Loans <sup>(2)</sup>		31	23
–	–			31	23
<b>Current Debt</b>					
–	–	Loans <sup>(2) (5)</sup>		1	6
–	–			1	6
–	–	Total Debt <sup>(4)</sup>		32	29

## Notes to the Financial Statements continued

Tenon Limited			Tenon Group	
2010	2011		2011	2010
US\$m	US\$m		US\$m	US\$m
<b>19 FINANCIAL COSTS AND DEBT</b> <small>continued</small>				
<b>Summary of Repayment Terms<sup>(3)</sup></b>				
Due for Repayment:				
–	–	less than one year <sup>(5)</sup>	1	6
–	–	between one and two years	2	21
–	–	between two and three years	2	1
–	–	between three and four years	2	1
–	–	between four and five years	25	–
–	–	after five years	–	–
–	–	Total Debt	32	29
<b>Non Current Debt</b>				
<b>Summary of Interest Rates by Repayment Period (%)<sup>(6)</sup></b>				
Due for Repayment:				
–	–	between one and two years	5.03	7.07
–	–	between two and three years	5.03	2.82
–	–	between three and four years	5.03	2.83
–	–	between four and five years	4.82	2.60
–	–	after five years	–	–
–	–	Weighted Average Interest Rate	4.85	6.68
<b>Weighted Average Interest Rate comprises:</b>				
–	–	Weighted average interest rate on debt	3.32	4.30
–	–	Facility fees amortisation % on debt	1.53	2.38
–	–	Weighted Average Interest Rate	4.85	6.68
<b>Current Debt</b>				
<b>Summary of Interest Rates by Repayment Period (%)<sup>(6)</sup></b>				
Due for Repayment:				
–	–	less than one year	6.63	7.43
–	–	Weighted Average Interest Rate	6.63	7.43
<b>Weighted Average Interest Rate comprises:</b>				
–	–	Weighted average interest rate on debt	5.30	5.07
–	–	Facility fees amortisation % on debt	1.33	2.36
–	–	Weighted Average Interest Rate	6.63	7.43

(1) Includes the amortisation of the unamortised refinancing fees on the previous facility, due to be amortised in the 2012 year (\$0.4 million). No facility fees relating to the new facility have been expensed, they will be spread over the term of the facility and amortised at the rate of \$0.3 million per annum.

(2) Tenon has a bank credit facility provided by a consortium of banks led by JP Morgan Chase Bank, N.A. (the Agent). The facility, which is structured as a global facility supporting the operations of the Tenon group as a whole, was entered into on 24 June 2011 and does not expire until June 2016. The new facility is an "asset-based" lending facility whereby the underlying assets and working capital of Tenon secure the obligations to the bank syndicate, subject to availability under a Borrowing Base covenant. The value of the assets under the Borrowing Base covenant is calculated based on the current value of the Group's inventory and receivables, reported to the Agent on a monthly basis, subject to certain prescribed exclusions, reserves and deductions. The Borrowing Base calculations are subject to periodic examination by the Agent during the remaining life of the credit facility (refer to note 4.2 (c)).

The revolver facility is classified as non-current, reflecting the lenders' commitment to the Company for the life of the facility which expires in June 2016. Under the facility the Company can exercise its unconditional right to draw down or repay borrowings from time to time up to the amount of the facility, subject to the Company remaining in compliance with certain facility covenants (refer to note 4.2 (c)). As at 30 June 2011, the Company was in compliance with the Borrowing Base Covenant, accordingly the amount of debt drawn under the revolver facility as at 30 June 2011 is aged non-current. As at June 2010, the company was in compliance with the covenants of the previous facility, and the revolver was aged as non-current.

## Notes to the Financial Statements continued

### 19 FINANCIAL COSTS AND DEBT continued

(3) The total size of Tenon's new syndicated bank credit facility reduces as a result of the scheduled amortisation of the Term Loan and the payment of an annual excess cash flow recapture provision of up to \$1 million. The assumption in the notes to the financial statements has been made that, commencing in the 2012 year, the maximum \$1 million repayment will be made under the excess cashflow provision of the facility.

	\$m		Total
	Term	Revolver	
June 2011 <sup>(a)</sup>	7.60	50.00	57.60
June 2012 <sup>(b)</sup>	7.08	50.00	57.08
June 2013 <sup>(b)</sup>	5.46	50.00	55.46
June 2014 <sup>(b)</sup>	3.83	50.00	53.83
June 2015 <sup>(b)</sup>	2.21	50.00	52.21
June 2016	–	–	–

(a) Scheduled Term Loan amortisation of \$52,000 per month from 1 September 2011.

(b) Scheduled Term Loan amortisation of \$52,000 per month and \$1 million excess cash flow payment on 30 September.

(4) All Non-Current and Current Debt is denominated in United States Dollars.

(5) The current debt of \$1 million reflects term loan amortisation of \$0.5 million and finance lease payments of \$0.1 million.

(6) The weighted average interest rates reflect the effective interest rate, inclusive of fee amortisations and any applicable interest rate swaps. As at 30 June 2011, the Group's remaining interest rate swap was ineffective due to the refinancing activities of the Group on 24 June 2011. In calculating the future average interest rates by repayment period, the interest rate swap interest differential has been included in the effective interest rate for the current debt to be repaid in the 2012 year. Loans are drawn as floating rate loans and the Group enters into floating to fixed interest rate hedges (refer to note 20 (a) interest rate risk).

### 20 FINANCIAL INSTRUMENTS

#### (a) Market Risk

##### Exposure to Price Risk

In December 2010, the Group entered into an electricity commodity contract for the purposes of providing an economic hedge against New Zealand electricity costs, this three year contract replaced the previous contract that expired in December 2010. The contract was approved by the Board (refer to note 4.2 a (i)).

##### Exposure to Currency Risk

The functional currency of the Group is denominated in United States dollars. The risk to the Group's equity and earnings are from assets, liabilities, revenues and costs in currencies denominated in currencies other than United States dollars.

The Group's exposure to foreign currency risks on financial instruments is based on the following:

	Tenon Group Currency of Denomination					
	as at 30 June 2011			as at 30 June 2010		
	USD US\$m	NZD US\$m	CAD US\$m	USD US\$m	NZD US\$m	CAD US\$m
Cash and Liquid Deposits	2	–	–	–	1	–
Trade Debtors	17	2	–	16	3	–
Bank Overdraft	–	–	–	-1	–	–
Trade Creditors	-9	-5	–	-12	-5	–
Current Debt	-1	–	–	-6	–	–
Non Current Debt	-31	–	–	-23	–	–
Gross Balance Sheet Exposure		-3	–		-1	–

The following exchange rates applied during the year:

	Average rate <sup>(1)</sup>		Reporting date (spot rate)	
	2011	2010	2011	2010
USD/NZD	0.7586	0.6976	0.8228	0.6936
USD/CAD	0.9966	0.9439	1.0132	0.9653

(1) Excludes the impact of foreign exchange cover put in place during the year.

##### Sensitivity Analysis

Given the small size of the gross balance sheet exposure shown above, any movement in the NZD/USD foreign exchange rate is unlikely to be material (refer to note 4.2 a (ii)).

## Notes to the Financial Statements continued

### 20 FINANCIAL INSTRUMENTS continued

#### Exposure to Interest Rate Risk

The Group's interest rate policy is for interest to be a mixture of fixed rate and floating rate debt within an established ratio. Loans are drawn with floating interest rates and the Group enters into floating to fixed interest rate hedges to comply with Group risk management policy. As at 30 June 2011, the Group had one interest rate swap totalling \$4.375 million, covering 14% of total Debt (as at 30 June 2010 there was one interest rate swap of \$6.875 million, or 24% of total Debt). Due to the refinancing activities of the Group, completed in late June 2011 (refer to note 4.2 (c)), no new interest rate instruments were placed before 30 June 2011. The Group intends to enter into additional interest rate fixing instruments early in the new financial year to implement a minimum risk strategy.

As at 30 June 2011, the Group had one interest rate swap of \$4.375 million on which the Group pays a fixed interest rate of 3.42% and receives the current equivalent of the one month USD LIBOR floating rate (0.1855% as at 30 June 2011, 0.34719% as at 30 June 2010). This swap amortised in line with the Term Loan drawn under the previous credit facility (refer to note 4.2 (c)) over the life of the Term Loan and expires in June 2012.

Swaps are settled monthly on a net basis. Interest rate swaps are treated as hedging instruments and the effective portion of the change in the fair value of swaps is taken to the hedging reserve in Equity. The ineffective portions of any swaps are taken to Earnings. With the establishment of the new credit facility on 24 June 2011 (refer to note 4.2 (c)) and repayment of the Term loan drawn under the previous facility, the interest rate swap was deemed to be ineffective as at 30 June 2011 (100% effective as at 30 June 2010). The net fair value as at June 2011 was a liability to the Group of \$0.1 million (June 2010 liability of \$0.2 million) and was included in other current payables (June 2010 in other current payables) and as a financing expense in the income statement (June 2010: in the hedging reserve in Group Equity). The following table sets out the weighted average interest rate of borrowings and interest rate hedges assuming that the interest rate swap designated ineffective as at 30 June 2011 is included in the interest rate repricing for debt repayable within one year.

	2011 US\$m	Tenon Group		2010 %
		2011 %	2010 US\$m	
Interest Rates Repriced (including average interest rate):				
Debt repayable within one year	1	6.63	6	7.43
between one and two years	2	5.03	21	7.07
between two and three years	2	5.03	1	2.82
between three and four years	2	5.03	1	2.83
between four and five years	25	4.82	–	2.60
after five years	–	–	–	–
	<b>32</b>		<b>29</b>	

#### Sensitivity Analysis

As at 30 June 2011, a 1% increase in the floating interest rates of the debt outstanding at balance date would have resulted in an estimated \$0.2 million reduction in Profit before Taxation, a 1% decrease in the floating interest rate would have resulted in an estimated increase of \$0.3 million in Profit before Taxation. The 2011 earnings impact was calculated on the actual debt drawn as at 30 June 2011 and was for a full 12 months assuming that 14% of debt was subject to the one interest rate swap in existence as at 30 June 2011 and the swap was the only one for the whole year and taken out at the beginning of the year and the change in fair value of the swap was included in interest costs in the year. The supply chain financing interest cost is also based on LIBOR rates and therefore sensitive to interest rate changes. As at 30 June 2011 a 1% change in the floating LIBOR interest rates on the level of debtors de-recognised as a result of the supply chain financing programme (\$19 million as at 30 June 2011) would have had an estimated \$0.2 million impact on Profit before Taxation.

A 1% increase in interest rates would have reduced Equity by \$0.3 million, being the after tax increase in total interest costs.

A 1% reduction in interest rates would have increased Equity by \$0.3 million, being the after tax reduction in total interest costs.

## Notes to the Financial Statements continued

### 20 FINANCIAL INSTRUMENTS continued

As at 30 June 2010, a 1% increase in the floating interest rates of the debt outstanding at balance date would have resulted in an estimated \$0.2 million reduction in Profit before Taxation, a 1% decrease in the floating interest rate would have resulted in an estimated increase of \$0.3 million in Profit before Taxation. The 2010 earnings impact was calculated on the actual debt drawn as at 30 June 2010 and was for a full 12 months assuming that 24% of debt was subject to the one interest rate swap in existence as at 30 June 2010 and the swap was the only one for the whole year and taken out at the beginning of the year. The supply chain financing interest cost is also based on LIBOR rates and therefore sensitive to interest rate changes. As at 30 June 2010 a 1% change in the floating LIBOR interest rates on the level of debtors de-recognised as a result of the supply chain financing programme (\$22 million as at 30 June 2010) would have had an estimated \$0.2 million impact on Profit before Taxation.

A 1% increase in interest rates would have reduced Equity by \$0.2 million, being the after tax increase in total interest costs partially offset by a reduction in the fair value liability of the interest rate swap. A 1% reduction in interest rates would have increased Equity by \$0.3 million, being the after tax reduction in total interest costs partially offset by an increase in the fair value.

#### (b) Credit Risk

##### *Exposure to Credit Risk*

The carrying amount of financial assets represents the maximum credit exposure. The maximum exposure to credit risk at the reporting dates was:

	Tenon Group	
	2011	2010
	US\$m	US\$m
Cash and Liquid Deposits <sup>(1)</sup>	2	1
Trade and Other Receivables	25	25
	<b>27</b>	<b>26</b>

The status of Trade Debtors is as follows:

Neither past due nor impaired <sup>(2)</sup>	17	17
Past due but not impaired <sup>(3)</sup>	2	2
Impaired <sup>(4)</sup>	–	–
	<b>19</b>	<b>19</b>
Less provision for doubtful debts <sup>(5)</sup>	–	–
Net Trade Debtors	<b>19</b>	<b>19</b>

(1) Cash and Liquid Deposits are only held with banks that are part of the Group's banking consortium led by JP Morgan Chase Bank, N.A. In the event of default, cash balances may be set off against obligations owing by Tenon to its lenders. Moody's credit ratings of the counterparties for Cash and Liquid Deposits are all rated as P-1 which is designated by Moody's as "Issuers who have a superior ability to repay short-term debt obligations".

(2) The Group has an excellent history of trade debtor collections and there is no reason to believe that the \$17 million (June 2010: \$17 million) of "neither past due nor impaired" debtors will not be collected, taking into account the payment history of our customers, the share of total trade debtors owed by the National Accounts (both retail and pro-dealer), and the existence of credit insurance for a significant portion of the US based pro-dealer customers.

(3) As at 30 June 2011 \$2 million (June 2010: \$2 million) of Trade Debtors were past due but not impaired.

The ageing of these Trade Debtors is as follows:

	Tenon Group	
	2011	2010
	US\$m	US\$m
Days overdue:		
1 month	2	2
	<b>2</b>	<b>2</b>

## Notes to the Financial Statements continued

### 20 FINANCIAL INSTRUMENTS continued

(4) As at 30 June 2011, \$0.3 million (June 2010: \$0.4 million) of Trade Debtors were impaired. Impaired Trade Debtors relate to customers who have experienced or who are experiencing financial difficulties. A provision for Doubtful Debts of \$0.3 million (June 2010: \$0.4 million) exists to cover the balance of the impaired debtors not expected to be recovered under the credit insurance programme operated by Tenon's US Subsidiaries. The other classes of receivables do not contain any impaired asset. The creation and release of provision for doubtful debts are included in Administration Expense in the Consolidated Income Statement.

(5) Movements in the Group provision for doubtful debts.

In the year to June 2011, the net provision created through earnings during the period was nil. In June 2010, the net provision created through earnings during the period was \$0.5 million. Debtors written off directly against the provision during 2011 were \$0.1 million (June 2010: \$0.4 million).

#### (c) Liquidity Risk

The following are contractual maturities of financial liabilities and net settled derivatives (excluding estimated interest payments). The amounts disclosed are the contractual undiscounted cashflows.

	Carrying value	Fair value	6 months or less	2011 \$m 6-12 months	1-2 years	2-5 years	Over 5 years
Non Derivative Financial Liabilities:							
Trade and Other Payables	25	25	23	2	–	–	–
Debt	32	32	–	1	2	29	–
	57	57	23	3	2	29	–

	Carrying value	Fair value	6 months or less	2010 \$m 6-12 months	1-2 years	2-5 years	Over 5 years
Non Derivative Financial Liabilities:							
Bank Overdraft	1	1	1	–	–	–	–
Trade and Other Payables	28	28	26	2	–	–	–
Debt	29	29	3	3	21	2	–
	58	58	30	5	21	2	–

#### Interest Rate Swap Cash Flows

As at 30 June 2011 the future gross cashflows of the interest rate swaps (refer to note 20 (a) market risk, exposure to interest rate risk) are a \$0.2 million cash outflow (being fixed interest paid). The swap is settled on a net basis monthly. Of the net cash outflow (based on the prevailing floating interest rates as at 30 June 2011) of \$0.2 million, \$0.1 million is expected to occur in the 6 months to December 2011 and \$0.1 million in the 6 months to June 2012.

As at 30 June 2010 the future gross cashflows of the interest rate swaps (refer to note 20 (a) market risk, exposure to interest rate risk) was a \$0.5 million cash outflow (being fixed interest paid) and a cash inflow of less than \$0.1 million (being floating interest received). The swap was settled on a net basis monthly. Of the net cash outflow (based on the prevailing floating interest rates as at 30 June 2010) of \$0.4 million, \$0.1 million was expected to occur in the 6 months to December 2010, \$0.1 million in the 6 months to June 2011 and \$0.2 million in the twelve months to June 2012.

#### (d) Financial Instruments by Category

Cash and liquid deposits and trade and other receivables and intercompany advances are classified as loans and receivables. Bank overdraft, trade and other payables, current and non current debt and deferred settlements and intercompany advances are classified as other financial liabilities. The electricity hedge is classified as a derivative used for hedging. The interest rate swap is classified as fair value through the Income Statement.

## Notes to the Financial Statements continued

### 20 FINANCIAL INSTRUMENTS continued

#### (e) Financial Instruments Measured at Fair Value

The estimated fair values of the Group's financial assets and liabilities do not differ materially from the carrying values. The methods and valuation techniques used for the purposes of measuring fair value are unchanged compared to the previous reporting period (refer to note 4.6 Fair Value Estimation).

The Group adopted the amendments to NZ IFRS 7 'Financial Instruments - Disclosures' effective from 1 July 2009. These amendments require the Group to present certain information about financial instruments measured at fair value in the Consolidated Balance Sheet. The Group's financial assets and liabilities as at 30 June 2011 and 30 June 2010 were below levels requiring disclosure.

The parent company had no financial instruments at 30 June 2011 (30 June 2010: nil).

Tenon Group	
2011	2010
US\$m	US\$m

### 21 COMMITMENTS

#### Lease Commitments

The expected future minimum rental payments required under operating leases that have initial or remaining non-cancellable lease terms in excess of one year at 30 June are as follows:

within	one year	7	8
	two years	5	7
	three years	4	5
	four years	3	3
	five years	2	2
after	five years	2	2
		<b>23</b>	<b>27</b>

Operating lease commitments relate mainly to occupancy leases of buildings and vehicles. There are no renewal options to purchase in respect of any asset held under operating leases. Total lease costs for the year were \$8.4 million (June 2010: \$8.1 million).

There are no lease commitments for Tenon Limited.

#### Capital Expenditure Commitments

There were no material capital expenditure commitments for the Tenon Group or Tenon Limited.

### 22 CONTINGENT LIABILITIES

The Group has no material contingent liabilities (June 2010: nil).

### 23 CONTINGENT ASSETS

#### Central North Island Forest Partnership (CNIFP) Legal Proceedings

A subsidiary of Tenon Limited (CNI Forest Nominees Limited) is party to legal proceedings in the New Zealand High Court commenced by the Receivers of CNIFP (on 7 February 2008) against the Commissioner for Inland Revenue (the IRD) in order to determine whether it is the IRD or the secured lenders to the CNIFP (which include Tenon's subsidiary CNI Forest Nominees Limited, which is the trustee for advances of more than US\$200 million to the CNIFP by another subsidiary of Tenon Limited in 1996 which have not yet been repaid by CNIFP (these advances have been fully provided for in the Group's financial statements in past accounting periods) that have first priority to Goods and Services Tax (GST) paid to the Receivers by the purchaser of the CNIFP forest estate in 2003 and which was paid to the IRD at the time of the sale. In the event the Court holds that the secured creditors were entitled to the GST receipt ahead of the IRD, then, as a second ranking security holder, CNI Forest Nominees Limited would be entitled to receive in the order of NZ\$90 million from the GST receipt in partial repayment of the CNIFP loan. However, the issues are very complex, and the proceedings are being strongly resisted by the IRD. As a result, the outcome for the Group, including the amount and timing of any recovery, is uncertain. An application by the IRD to the High Court to strike out the legal proceedings was dismissed in 2010 and the IRD appealed that decision to the Court of Appeal. A hearing on the appeal is expected by the end of calendar year 2011.

## Notes to the Financial Statements continued

### 24 RELATED PARTY TRANSACTIONS

(a) The following related party transactions occurred during the year and as at 30 June the following balances, guarantees and shareholdings existed between related parties.

Services are negotiated with related parties based upon competitive market rates charged to unaffiliated customers for similar goods.

Rubicon Limited and its subsidiaries ("Rubicon") own 57.96% of Tenon Limited (June 2010: 57.96%). Two of Tenon Limited's directors are also directors of Rubicon Limited. Directors fees charged by Rubicon were \$0.1 million (June 2010: \$0.1 million). As at 30 June 2011, there was \$0.1 million owing between Tenon and Rubicon for outstanding Director's fees for the 2011 year (June 2010: nil). Office and administration costs charged by Rubicon to Tenon for the 2011 year were nil (June 2010: \$0.1 million).

	Tenon Group	
	2011	2010
	US\$m	US\$m
<b>Tenon Group</b>		
Borrowers under the credit agreement <sup>(1)</sup>	-	-
<b>Tenon Limited</b>		
Royalties and Management Fees received for Services Provided to Subsidiaries by Tenon Limited <sup>(2)</sup>	-	-
Finance Charges paid by Tenon Limited on Advance from Subsidiary <sup>(3)</sup>	-17	-16
Term Advance Liability from Subsidiary Company <sup>(4)</sup>	286	226
Term Advance Asset to Subsidiary Company <sup>(4)</sup>	1	1
Investment in Subsidiary Companies <sup>(5)</sup>	262	262

(1) All material subsidiaries of the Group are named borrowers in the credit facility signed on 24 June 2011.

(2) Royalties and management fees charged were \$0.3 million (June 2010: \$0.2 million). These charges are to New Zealand based subsidiaries Tenon Manufacturing Limited and Tenon Industries Limited.

(3) This advance is for no fixed term but represents a long-term funding advance, and bears interest at 7.08 % per annum (30 June 2010: 7.56 % per annum).

(4) This advance is for no fixed term but represents a long-term funding advance and is not interest bearing.

(5) The Principal Subsidiaries included within Investment in Subsidiary Companies are disclosed in note 26, Principal Operations.

	2011	2010
	US\$m	US\$m
<b>(b) Key Management Compensation</b>		
Salaries and other short-term employee benefits	3	3
Directors' fees paid to Non Executive Directors (refer to note 5(1))	-	-
	3	3

#### Chief Financial Officer's Incentive Plan

The Chief Financial Officer's remuneration includes a long-term incentive plan (LTI Plan). The LTI Plan was established on 1 July 2009. The LTI Plan has a one-time pay-out date of 1 September 2012. Whether or not any payment is made to him, and the quantum of any payment made is dependent upon the Company achieving set targets – the key target being Tenon's EBITDA for the fiscal year to 30 June 2012. Payment may also be triggered in the event of a change of control of the Company. There is a minimum 2012 EBITDA threshold of \$17.5 million (inclusive of corporate overhead) to earn a pay-out under the plan, and the maximum pay-out under the Plan will be made if fiscal 2012 EBITDA meets or exceeds \$30 million (inclusive of corporate overhead). The Company has not taken any charge to earnings in respect of the above arrangement.

## Notes to the Financial Statements continued

### 25 SEGMENTAL INFORMATION SUMMARY

Tenon derives its revenue from and operates within one material operating segment, being the Moulding and Millwork segment. The Board and the Executive Management team assess Tenon's performance, and review the allocation of resources, from reports presented as a single business operating within this one segment. Consequently no segmental information by business class is disclosed.

Geographic segmental reporting for the periods ended June 2011 and June 2010 split between North America and New Zealand is shown below.

	North America US\$m	New Zealand US\$m	Total US\$m
<b>2011</b>			
<b>Operating Revenue</b>	287	39	<b>326</b>
<b>Non Current Assets<sup>(1)</sup></b>	83	16	<b>99</b>
<b>Capital Expenditure</b>	2	–	<b>2</b>
	North America US\$m	New Zealand US\$m	Total US\$m
<b>2010</b>			
Operating Revenue	296	33	329
Non Current Assets <sup>(1)</sup>	84	16	100
Capital Expenditure	2	1	3

(1) Excludes Deferred Tax and Financial Instruments.

Revenues of approximately \$160 million (June 2010: \$167 million) are derived from a single external customer, these revenues are attributable to the North American geographic segment.

### 26 PRINCIPAL OPERATIONS

Tenon Limited is the holding company of the Tenon Group. The Tenon Group's principal subsidiaries all have June balance dates and are outlined below:

	Country of Domicile	Principal Activity	% Holding	
			June 2011	June 2010
<b>Principal Subsidiaries</b>				
Tenon Industries Limited	NZ	Funding	<b>100</b>	100
Tenon Manufacturing Limited	NZ	Processing	<b>100</b>	100
Fletcher Wood Solutions Inc	USA	Distribution	<b>100</b>	100
The Empire Company, Inc	USA	Distribution	<b>100</b>	100
Kok's Woodgoods, Inc	USA	Processing	<b>100</b>	100
Southwest Moulding Co, LP	USA	Distribution	<b>100</b>	100
Ornamental Mouldings LLC	USA	Processing	<b>100</b>	100
Ornamental Products LLC	USA	Processing	<b>100</b>	100
Ornamental Mouldings Company	Canada	Processing	<b>100</b>	100

# Independent Auditor's Report to the Shareholders of Tenon Limited



## Report on the Financial Statements

We have audited the financial statements of Tenon Limited on pages 15 to 48, which comprise the balance sheets as at 30 June 2011, the income statements, statements of comprehensive incomes and statements of changes in equity and cash flow statements for the year then ended, and the notes to the financial statements that include a summary of significant accounting policies and other explanatory information for both the Company and the Group. The Group comprises the Company and the entities it controlled at 30 June 2011 or from time to time during the financial year.

## Directors' Responsibility for the Financial Statements

The Directors are responsible for the preparation of these financial statements in accordance with generally accepted accounting practice in New Zealand and that give a true and fair view of the matters to which they relate and for such internal controls as the Directors determine are necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

## Auditors' Responsibility

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with International Standards on Auditing (New Zealand) and International Standards on Auditing. These standards require that we comply with relevant ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditors' judgement, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditors consider the internal controls relevant to the Company and Group's preparation of financial statements that give a true and fair view of the matters to which they relate, in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company and Group's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

We have no relationship with, or interests in Tenon Limited or any of its subsidiaries other than in our capacities as auditors and providers of other assurance services. These services have not impaired our independence as auditors of the Company and Group.

## Opinion

In our opinion, the financial statements on pages 15 to 48:

- (i) comply with generally accepted accounting practice in New Zealand;
- (ii) comply with International Financial Reporting Standards; and
- (iii) give a true and fair view of the financial position of the Company and the Group as at 30 June 2011, and their financial performance, and cash flows, for the year then ended.

## Report on Other Legal and Regulatory Requirements

We also report in accordance with Sections 16(1)(d) and 16(1)(e) of the Financial Reporting Act 1993. In relation to our audit of the financial statements for the year ended 30 June 2011:

- (i) we have obtained all the information and explanations that we have required; and
- (ii) in our opinion, proper accounting records have been kept by the Company as far as appears from an examination of those records.

## Restriction on Distribution or Use

This report is made solely to the Company's shareholders, as a body, in accordance with Section 205(1) of the Companies Act 1993. Our audit work has been undertaken so that we might state to the Company's shareholders those matters which we are required to state to them in an auditors' report and for no other purpose. To the fullest extent permitted by law, we do not accept or assume responsibility to anyone other than the Company and the Company's shareholders, as a body, for our audit work, for this report or for the opinions we have formed.

A handwritten signature in black ink, appearing to read 'PricewaterhouseCoopers', is written over a light blue background.

Chartered Accountants  
19 August 2011

Auckland

## Board of Directors as at 19 August 2011

### Simon Luke Moriarty

MS (Stanford), LLB (Hons), BCA (VUW)  
Chairman of Directors  
Non-Executive Director

#### Committees

Audit  
Nominations (Chairman)  
Last re-elected 2009

Mr Moriarty was appointed Chairman of Directors on 7 October 2005. He is the Chief Executive Officer and an Executive Director of Rubicon Limited. Prior to that he was a member of the Executive Office of the Fletcher Challenge Group, and was instrumental in structuring the financial separation of the Fletcher Challenge Group in 2001. He joined Fletcher Challenge Limited in 1982, and held a number of senior executive roles across the Fletcher Challenge Group Divisions in New Zealand and North America, including Chief Financial Officer of Fletcher Challenge Canada and Director of TimberWest Forests. He is also a director of ArborGen LLC. The Board has determined that Mr Moriarty is not an independent Director because he is a director of Rubicon Forests Holdings Limited, the Company's largest shareholder, and the Chief Executive Officer and Executive Director of Rubicon Limited, the holding company of Rubicon Forests Holdings Limited.

### Michael John Andrews

MNZIF  
Non-Executive Director

#### Committees

Nominations  
Remuneration  
Last re-elected 2010

Mr Andrews retired as Chief Executive Officer of Fletcher Challenge Limited in April 2001. He was acting Chief Executive Officer of Fletcher Building Limited until July 2001. He was previously Divisional Chief Executive of Fletcher Challenge Energy, Fletcher Challenge Forests and Fletcher Challenge Paper and previously Chief Executive Officer of the Solid Wood Forestry sector, and before that of the former Energy and Resources Group. He is a director of Orion NZ Limited and the National Centre for Advanced Bio Protection Technologies. The Board has determined that Mr Andrews is an independent Director.

### Rodger Herbert Fisher

FCIS, FCIT, FIDNZ, FNZIM  
Non-Executive Director

#### Committees

Audit  
Nominations  
Remuneration (Chairman)  
Last re-elected 2010

Mr Fisher practises as a business consultant. He was previously Managing Director of Owens Group Limited between 1987 and 1999. He is Chairman of Eurotech Group, Ultrafast Broadband Limited and Lyttelton Port Company Limited and is a director of The Property Group Limited. He is a former Chairman of the Civil

Aviation Authority and Aviation Security Services. He is a Fellow of the Chartered Institute of Secretaries, the Chartered Institute of Transport, the Institute of Directors in New Zealand and the New Zealand Institute of Management.

The Board has determined that Mr Fisher is an independent Director.

### Stephen Garfield Kasnet

BA University of Pennsylvania (Philadelphia)  
Non-Executive Director

#### Committees

Nominations  
Remuneration  
Last re-elected 2009

Mr Kasnet is currently Chairman of Rubicon Limited, the holding company of the Company's largest shareholder, Rubicon Forests Holdings Limited. He is also Chief Executive Officer of Calypso Management LLC, Chairman of Directors of Columbia Labs, Inc, President of Ocean Manchester Corporation, director of the First National Bank of Ipswich, Trustee and Vice President of the Governors Academy and director of Two Harbors Investment Corp. and Escon Capital Inc. He has previously held the roles of President and Chief Executive Officer of Harbor Global, a prime asset of which was a timber harvesting and sales operation in eastern Russia covering over three million acres of concession area, Managing Director of First Winthrop Corporation and Winthrop Financial Associates in the US, President and Chief Executive Officer of Raymond Property Group and Dartmouth Street Company and also Executive Vice President of the Pioneer Group Inc in the US. His responsibilities there covered the global strategic investments for the Pioneer Group, including venture capital and timber operations.

The Board has determined that Mr Kasnet is not an independent Director because he is the Chairman of Rubicon Limited, the holding company of the Company's largest shareholder, Rubicon Forests Holdings Limited.

### Michael Carmody Walls

BA, LLB (VUW), LLM (London)  
Non-Executive Director

#### Committees

Audit (Chairman)  
Nominations  
Last re-elected 2008

Mr Walls practises as a business consultant. He was previously the Managing Director, Investment Banking, for BZW New Zealand Limited, and then for its successor, ABN AMRO New Zealand Limited, from 1997 to 2000. Prior to that Mr Walls practised as a commercial lawyer at Chapman Tripp, where he was a partner from 1972 until 1996 specialising in mergers and acquisitions, international finance and corporate law. Mr Walls is a former Chairman of BHP NZ Steel Holdings Limited, and a former Chairman of the formerly listed Independent Press Communications Limited. In addition, he has been a director of a number of unlisted companies. He is the Chairman of the Board of the New Zealand Institute of Economic Research Inc.

The Board has determined that Mr Walls is an independent Director.

The Board of Tenon Limited is committed to the highest standards of corporate governance, which the Company recognises as fundamental to its business activities. The Company continually monitors, reviews and improves its governance practices.

The Company's governance procedures are designed to meet the following principles:

1. Directors should observe and foster high ethical standards.
2. There should be a balance of independence, skills, knowledge, experience, and perspectives among Directors so that the Board works effectively.
3. The Board should use committees where this would enhance its effectiveness in key areas while retaining Board responsibility.
4. The Board should demand integrity both in financial reporting and in the timeliness and balance of disclosures on Group affairs.
5. The remuneration of Directors and executives should be transparent, fair and reasonable.
6. The Board should regularly verify that the Group has appropriate processes that identify and manage potential and relevant risks.
7. The Board should ensure the quality and independence of the external audit process.
8. The Board should foster constructive relationships with shareholders that encourage them to engage with the Group.
9. The Board should respect the interests of stakeholders within the context of the Group's ownership type and its fundamental purpose.

### Code of Business Conduct and Ethics and Company Policies

The Company has written procedures to:

- Clarify the standards of the high ethical behaviour required of Directors, executives and employees; and
- Prescribe the circumstances where Directors and employees can trade in the Company's securities.

The Company's Code of Business Conduct and Ethics underpins all its activities, and recognises the Company's legal and other obligations to legitimate stakeholders. The Code ensures that Company decisions reflect the Company's core values of action orientation, innovation, commercial intensity, customer focus, accountability, teamwork, respect for the individual, respect for the environment and safety. The Board reviews the Code, ensures the Code is communicated to the Company's personnel, monitors adherence to the Code, and holds Directors, executives and other personnel accountable for any unethical behaviour. The Code can be viewed on [www.tenonglobal.com](http://www.tenonglobal.com).

Various policies and procedures are in place to effectively implement the Code of Business Conduct and Ethics. For example, a comprehensive code has been adopted by the Company to regulate trading in the Company's securities by Directors, executives and Company employees. Trading is subject to a formal Board approval process, designed within the framework of New Zealand's insider trading laws. In addition, a number of other policies cover such matters as continuous disclosure obligations under securities laws, financial management, environmental compliance, employment equal opportunity and whistleblowing by employees. Policies are published on the internal Company websites, which are accessible to all employees and, where appropriate, distributed to employees.

Appropriate training is provided to the Company's personnel, for example in the areas of insider trading laws and competition law.

## Role of the Board

The Board is elected by shareholders to create value and has overall responsibility for the strategic direction and management of the Company. The Board is structured in a way that it:

- Has a balance of independence, skills, knowledge, experience and perspectives among Directors;
- Has a proper understanding of, and competence to deal with, the current and emerging issues of the business; and
- Can effectively review and challenge the performance of Management and exercise independent judgement.

The Company achieves Board and Management accountability through having formal strategies, policies and procedures, which includes a formal charter for the Board and its Committees, and for the Chairman, Directors and Management.

The Executive is responsible for the day-to-day management of the Company's business and for ensuring that the policies and strategies approved by the Board are implemented. There are formal delegations of authority to the Executive.

The Executive comprises the Chief Executive Officer (until October 2011), Chief Operating Officer, Chief Financial Officer and General Manager Corporate.

The Board formally evaluates the performance of the Executive annually. The evaluation is based on criteria that include the performance of the business, the accomplishment of long-term strategic objectives and other specific objectives agreed at the beginning of each year.

The Board currently comprises five non-executive Directors. One third must retire at each Annual Shareholders Meeting.

The Chairman's role is to manage and provide leadership to the Board and to interact with the Executive. The Chairman is also responsible for fostering a constructive governance culture and for applying appropriate governance principles among Directors and with Management.

The governance procedures require that the roles of Chairman and Executive should not be held by one person at the same time.

The Board facilitates full and frank dialogue among the Company's Audit Committee, the auditor and Management. For example, the auditor receives copies of Board papers at the time they are sent to Directors, the auditor can and does discuss Company issues with Management outside of formal meetings with the Audit Committee, and the auditor attends Audit Committee meetings.

The Company's policy is that the Board should be comprised of at least two independent Directors.

Independent Directors are generally regarded as being independent of Management and free of any business or other relationship that could materially interfere with, or could reasonably be perceived to materially interfere with, the exercise of their unfettered and independent judgement.

The Board regularly assesses the independence of each Director, in light of interests disclosed by them to the Company.

S L Moriarty and S G Kasnet are not considered by the Board to be independent Directors because they are Directors of the parent company of the Company's largest shareholder, Rubicon Forests Holdings Limited. S L Moriarty is also Chief Executive of that company's parent, Rubicon Limited, and S G Kasnet is Chairman of Rubicon Limited.

Although the Chairman is not an independent Director, the majority of the Board, comprising R H Fisher (who is also the Chairman of the Remuneration Committee), M C Walls (who is also the Chairman of the Audit Committee) and M J Andrews are independent Directors under the NZX corporate governance guidelines, which are used by the Company to determine independence.

As stated above, the Board is responsible for the overall management of the Company. However day to day leadership and management of the Company is delegated to the Executive pursuant to formal delegations established by the Board.

Notwithstanding the delegations from the Board to the Executive, specific matters reserved to the Board include:

- Oversight of the Company;
- Monitoring Company and Management performance;
- Appointing, compensating and removing the Executive;
- Approving and monitoring corporate strategy and performance objectives;
- Reviewing risk management and reporting systems;
- Approval of major capital expenditure; and
- Approval of the Annual and Interim financial statements and reports.

## Board Process

The Board has scheduled meetings each year, but also meets on an as-needed basis. Directors receive comprehensive information on the Company's operations in advance of meetings. Senior Management is normally present at all Board meetings to make presentations, answer questions and to assist the Board in its understanding of the Company's business.

The Board of Directors meets periodically without Management present.

The Board also holds a strategic planning meeting once a year.

New Directors are appropriately introduced to the Company and to relevant industry knowledge and economics. This includes visits to specific Company operations, and briefings from key executives. Directors are required to consult with the Chairman before accepting any other board appointment or other commitment that might adversely impact on the ability of the Director to perform the Director's obligations to the Company. The Company provides training, in the form of presentations to the Board, and encourages Directors to ensure their skills, knowledge and experience remain up to date and relevant to the Company.

An annual performance evaluation is conducted of the Board and its members. This is conducted by the Chairman of the Board by one-on-one discussions with members. The results of the evaluation are discussed by the Board.

A Director may, with the prior written approval of the Chairman, and at the Company's expense, seek independent advice on an issue affecting the Director's duties to the Company.

## Board Committees

Committees have been established by the Board to assist the Board in the execution of its responsibilities.

They are used where this would enhance the Board's effectiveness in key areas, while retaining Board responsibility.

There are currently three Committees: Audit Committee, Nominations Committee and Remuneration Committee. Other Committees may be established from time to time to consider matters of special importance.

A Committee may engage separate independent counsel and/or advisors at the expense of the Company.

Each Committee has adopted a comprehensive Charter addressing membership, authority, responsibilities and reporting procedures. These can be reviewed on the Company's website, [www.tenonglobal.com](http://www.tenonglobal.com).

All non-executive Directors are entitled to attend all Committee meetings. Executive Directors and Management attend Committee meetings by invitation.

All non-executive Directors receive copies of papers for and minutes of meetings of the Committees.

The Chairperson of each Committee reports back to the Board in relation to proceedings of the Committee to allow other Directors to question Committee members.

An annual performance evaluation is conducted for each Committee. The results of the evaluation are discussed by the Committee, and by the Board.

## Audit Committee

### Committee members:

M C Walls (Chairman), R H Fisher and S L Moriarty

The Board appoints the members of the Audit Committee from the non-executive Directors of the Company. It consists of not fewer than three members. The Chairman is an independent Director who is not the Chairman of the Board, and a majority of the members are independent Directors.

The Audit Committee oversees all matters concerning:

- Internal accounting, control and business risk management policies and systems;
- Suitability of the Group's accounting policies and principles;
- Financial reporting and the integrity thereof, including reviewing the half year and full year financial statements;
- The internal audit function; and
- The appointment and supervision of the auditor.

The auditor attends all meetings of the Audit Committee.

A majority of the members of the Audit Committee must be independent Directors.

Any employee has access to the Chairman of the Audit Committee at any time.

The Audit Committee has a formal pre-approval procedure that must be followed for all audit and audit-related services and non-audit services to be provided by the Company's audit firm to ensure that they do not impair the audit firm's independence from the Company. During the year the auditor did perform non-audit related work for the Company in relation to the review of certain internal controls and the Company's Annual Shareholders Meeting. The work was in the nature of assurance and the total fees paid to the audit firm were US\$83,000 which the Company considers did not impair the audit firm's independence from the Company.

The Audit Committee also approves an annual internal audit (extended assurance) programme, and the results of that programme are reported directly to the Committee and also copied to all Directors.

### **Remuneration Committee**

#### *Committee members:*

R H Fisher (Chairman), M J Andrews and S G Kasnet

The Board appoints the members of the Remuneration Committee from the non-executive Directors of the Company. It consists of not fewer than three members. The Chairman is an independent Director and a majority of the members are independent Directors.

The Remuneration Committee ensures that remuneration and recruitment policies and practices are aligned with the creation of shareholder value and the Company's objectives. The Committee makes recommendations to the Board with regard to the remuneration of the Executive and of the direct reports to the Executive. The Committee also, at least annually, reviews the performance of the Company's senior management based on performance against agreed objectives, and determines the amount of variable incentive payments to be made to the Company's employees. The Committee also sets the guidelines for annual salary reviews and objectives for performance-based payments for senior salaried employees. The Executive's performance is also reviewed by the full Board.

The Remuneration Committee reviews and makes recommendations to the Board with regard to Director remuneration.

### **Nominations Committee**

#### *Committee members:*

S L Moriarty (Chairman), M J Andrews, R H Fisher, S G Kasnet and M C Walls

The Nominations Committee comprises the five non-executive Directors.

The Committee is responsible for considering Board nominations. In order to ensure the appropriate balance of skills and experience of the Board, the Committee assesses the necessary and desirable competencies of Board members before their appointment and makes recommendations to the Board from time to time as to changes to the Board composition that the Committee believes to be desirable.

## Financial Reporting

It is the Board's responsibility to ensure the integrity of the Company's financial reporting. A structure of review and authorisation has been put in place that is designed to ensure the quality and integrity of the Company's financial reporting including their relevance, reliability, comparability, and timeliness. This structure includes:

- An Audit Committee comprised of a majority of independent Directors, with a chairman who is not also the Chairman of the Board, appropriately resourced, and with a written charter;
- An independent review of the Company's financial statements by the Company's auditor;
- A review by the Audit Committee of the half year and full year financial statements, with management and the auditor present;
- A formal report from the Chairman of the Audit Committee to the Board in relation to the approval by the Board of the half year and annual financial statements;
- A review by the Board of the half year and full year financial statements, with management present;
- A formal Management Representation letter to the Board relating to the half year and annual financial statements, signed by each member of the Executive;
- Consideration by the Board of a formal Directors' Representation letter to the auditor relating to the half year and annual financial statements, signed by a Director under delegated authority from the Board;
- Signing of the financial statements by the Chief Financial Officer, the Chairman of the Board, and the Chairman of the Audit Committee;
- Policies to ensure the independence of the auditor;
- Processes and policies to ensure that the Company has an effective system of internal control for reliable financial reporting;
- The Audit Committee meeting with the auditor, without Management present; and
- A code of ethics for employees.

## Auditor Quality and Independence

The Board considers it is essential that the Company's auditor be independent, and also be seen to be independent. The Company has an auditor independence policy which is designed to ensure that the Company's auditor does not have a mutual or conflicting interest with that of the Company, nor its independence impaired in relation to its performance of audit, or audit-related, services to the Company.

The Company has adopted the following key policies in relation to auditor independence:

- The auditor is required to abide by defined independence standards;
- The Audit Committee must pre-approve the appointment of the auditor to provide any non-audit services to the Company or its subsidiaries and the Chairman of the Committee may, pursuant to a delegation from the Committee, approve lower-cost non-audit services to the Company;
- The auditor is required to report in writing to the Audit Committee on an annual basis on matters relating to its independence;
- The auditor is required to rotate its lead audit partner and the audit partner responsible for reviewing the audit on a five yearly basis, and such partners cannot be re-involved with the Company for a further five years;
- The auditor may freely, and is encouraged to, communicate directly with the Chairman of the Board and the Chairman of the Audit Committee and with Management, including, for example, if the auditor wished to make any complaint about the support being provided by the Company in relation to the audit process;
- The auditor attends all meetings of the Audit Committee, and is encouraged to speak freely at such meetings;
- The auditor is required to be available at the Annual Shareholders Meeting of the Company and answer any shareholder questions relating to the audit or audit report.

The nature of the Company's business requires an experienced auditor with a global presence. The Board, through the Audit Committee, together with Management of the Company monitors the performance of the auditor to ensure that the services being provided to the Company are of high quality, relevant, timely and cost effective.

## Remuneration Policy

The remuneration of Directors and executives is transparent, fair and reasonable. The Remuneration Committee reviews annually all remuneration paid to employees within the Group.

The Company has adopted remuneration policies that are designed to encourage and reward performance and the creation of shareholder value, and also attract and retain talented and motivated employees. A range of performance-based incentive schemes are in place among Tenon and its subsidiaries. These all involve a significant proportion of the annual remuneration of executive and senior management employees being linked to business performance and also individual performance. The Company uses objective third party benchmarking systems to ensure its remuneration is aligned to market. For example, in New Zealand the Company has a policy of maintaining base remuneration for its salaried employees within a band around the industry median. Remuneration outside that band is permitted only in exceptional circumstances, such as where special skills are required.

The Company has comprehensive and objective formal programmes for setting the performance objectives of its employees, and for monitoring performance against those objectives. Objectives are established for each financial year with the agreement of the Remuneration Committee and performance against those objectives is assessed by the Committee after completion of that year, and before any performance based payments are made to employees.

Adjustments to the remuneration of salaried employees are normally based on market movements and individual performance, and must first be approved by the Remuneration Committee or made within guidelines agreed by the Committee. The remuneration and other terms and conditions of employment of the Executive and the Executive's direct reports must be approved by the Board of Directors.

On page 58 is a table describing the fees paid to the Directors of the Company during the year. Directors do not receive any remuneration from the Company other than in their capacity as Directors.

The Company has prohibited the making of loans to Directors and employees.

## Employee Remuneration

In accordance with Section 211(1)(g) of the New Zealand Companies Act 1993, remuneration and other benefits in excess of NZ\$100,000 per annum paid to employees of Tenon Limited and its subsidiaries, both in New Zealand and overseas, not being Directors of the Company, during the year are detailed below. The bandings below include retirement and redundancy payments.

	US/Canada based Business Number of Employees	NZ based Business Number of Employees
NZ\$100,000 to NZ\$110,000	16	1
NZ\$110,000 to NZ\$120,000	10	–
NZ\$120,000 to NZ\$130,000	8	1
NZ\$130,000 to NZ\$140,000	11	5
NZ\$140,000 to NZ\$150,000	6	1
NZ\$150,000 to NZ\$160,000	5	1
NZ\$160,000 to NZ\$170,000	2	1
NZ\$170,000 to NZ\$180,000	1	1
NZ\$180,000 to NZ\$190,000	4	–
NZ\$190,000 to NZ\$200,000	2	–
NZ\$200,000 to NZ\$210,000	3	1
NZ\$210,000 to NZ\$220,000	5	–
NZ\$220,000 to NZ\$230,000	2	–
NZ\$230,000 to NZ\$240,000	2	–
NZ\$240,000 to NZ\$250,000	1	–
NZ\$250,000 to NZ\$260,000	–	1
NZ\$260,000 to NZ\$270,000	1	–
NZ\$280,000 to NZ\$290,000	1	–
NZ\$290,000 to NZ\$300,000	1	–
NZ\$300,000 to NZ\$310,000	2	1
NZ\$320,000 to NZ\$330,000	2	–
NZ\$330,000 to NZ\$340,000	1	–
NZ\$360,000 to NZ\$370,000	1	–
NZ\$410,000 to NZ\$420,000	2	–
NZ\$440,000 to NZ\$450,000	2	1
NZ\$610,000 to NZ\$620,000	1	–
NZ\$790,000 to NZ\$800,000	1	–
NZ\$910,000 to NZ\$920,000	1	–

## Controlling and Managing Risk

The Company is, like any other business, exposed to risks. A central function of Management is to effectively identify and manage those risks within policy levels set by the Board. The Board takes an active role in ensuring the Company has and operates a sound system of risk oversight and management and internal control. It has a range of policies, practices and procedures that help the Company to manage business risks. These are reviewed regularly as part of the Company's risk management process. The Executive is required to ensure that the Company's risk management and internal compliance and control system is operating efficiently and effectively in all material respects. All Directors are copied on all Committee papers and minutes of Committee meetings to ensure transparency of decision-making.

The Board meets on a regular basis and Management presents information to the Board on risks facing the Company and strategies adopted to manage those risks.

Details of many of the risks the Company is exposed to and the way the Company manages those risks are described in note 4 to the financial statements (see pages 28 to 33).

## NZX Corporate Governance Principles

The Company's corporate governance process materially differs from the principles set out in the NZX Corporate Governance Best Practice Code in that the Company does not offer any equity security compensation plan to Directors and all Directors may attend meetings of the Audit Committee.

## Ensuring the Market is Properly Informed

The Company has in place comprehensive, Board-approved, disclosure policies and procedures that are designed to ensure timely and balanced compliance with the information disclosure requirements of the New Zealand Exchange, which are designed to ensure that:

- All investors have equal and timely access to material information concerning the Company – including its financial situation, performance and governance; and
- Company announcements are factual and presented in a clear and balanced way.

The Board examines continuous disclosure issues as an agenda item at each Board meeting.

## Financial Markets Authority Corporate Governance Principles

The Company's corporate governance process differs from the principles set out in the Financial Markets Authority Corporate Governance in New Zealand Principles and Guidelines in that the Chairman of the Board is not an independent Director. However, the Board has a majority of independent Directors, and the Chairmen of the Company's Audit and Remuneration Committees are also independent Directors.

## Keeping in Touch with Shareholders and Stakeholders

The Company strives to effectively communicate with its shareholders and stakeholders, by giving them ready access to balanced and understandable information about the Company and corporate proposals, and by making it easy to participate in shareholder meetings. Ways that the Company achieves these objectives include:

- A website is maintained with information about the Company, including information about its businesses, copies of all stock exchange releases made by the Company, copies of media releases, full year and half year reports and supplementary financial information, and copies of key Company governance policies;
- An Annual Shareholders Meeting is held, which any shareholder can attend;
- The speeches and presentations which are delivered to the Annual Shareholders Meeting are placed on the Company's website;
- The results of the voting at shareholder meetings are announced to the stock exchange;
- Letters are sent directly to shareholders on major events affecting the Company;
- Full year reports and half year reports which include an update of Company strategy and developments are mailed to shareholders;
- The holding of Annual Shareholders Meetings at different locations to ensure that as broad a cross section of shareholders as possible have an opportunity to attend such meetings;
- Compliance with continuous disclosure obligations;
- The Code of Business Conduct and Ethics reflects the commitment of the Company to respect the interests of stakeholders (including customers, employees, compliance with the law and respect for the environment); and
- An investor relations email in-box enables a quick response to investor enquiries.

# Statutory Disclosure

## Directors' Interests Register

Directors' certificates to cover entries in the Interests Register in respect of remuneration, dealing in the Company's securities, insurance and other interests have been disclosed as required by the New Zealand Companies Act 1993.

## Non-Executive Directors' Remuneration

Non-executive Directors' remuneration for the 30 June 2011 year was \$51,206<sup>(1)</sup> (NZ\$67,500) per annum per Director, with the Chairman receiving \$98,618<sup>(2)</sup> (NZ\$130,000) per annum. The Chairman of the Audit Committee receives an additional \$4,930<sup>(1)(3)</sup> (NZ\$6,500) per annum and the Chairman of the Remuneration Committee receives an additional \$3,413<sup>(1)(3)</sup> (NZ\$4,500) per annum. Other members of board committees do not receive additional fees for participation on board committees.

The aggregate amount of fees paid by Tenon Limited to non-executive Directors for services in their capacity as Directors during the year ended 30 June 2011 was \$311,785<sup>(1)</sup> (NZ\$411,000). Fees, prior to any taxation liability, paid to individual non-executive Directors in the year ended 30 June 2011 were:

	Fee <sup>(1)</sup>
M J Andrews	51,206
R H Fisher	54,619
S G Kasnet	51,206
S L Moriarty <sup>(2)</sup>	98,618
M C Walls	56,136

- (1) Directors' fees have been translated from New Zealand dollars at an average foreign exchange rate of NZ\$1 = US\$0.7586.
- (2) Total Directors' fees in relation to S L Moriarty (Chairman) were paid directly to Rubicon Limited.
- (3) Chairmen's fees were introduced on 1 January 2010, reflecting the additional responsibilities required of the Chairmen.

## Executive Directors' Remuneration

Executive Directors do not receive remuneration as Directors of Group subsidiaries.

## Subsidiary Company Directors

Section 211(2) of the New Zealand Companies Act 1993 requires the Company to disclose, in relation to its subsidiaries, the total remuneration and value of other benefits received by Directors and former Directors and particulars of entries in the interests registers made during the year ended 30 June 2011.

Apart from S L Moriarty's position as Director of The Empire Company, Inc, no subsidiary except certain nominee companies had Directors who were not full-time employees of the Group.

No employee of the Tenon Limited Group appointed as a Director of Tenon Limited or its subsidiaries receives or retains any remuneration or other benefits as a Director.

The remuneration and other benefits of such employees, received as employees, are included in the relevant bandings for remuneration disclosed on page 56, where the employee received remuneration and other benefits totalling NZ\$100,000 or more during the year ended 30 June 2011.

The following persons respectively held office as Directors of subsidiary companies at the end of the year or in the case of those persons with the letter (R) after their name ceased to hold office during the year.

### **Fletcher Challenge Forests Finance Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R)

### **Tenon Custodians Limited**

A T Johnston, P M Gillard, J E Paice, A S White

### **Tenon Industries Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R)

### **Tenon Manufacturing Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R)

### **Tenon Holdings Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R)

### **Fletcher Challenge Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R),

### **Kaingaroa Holdings Limited**

P M Gillard

### **CNI Forest Nominees Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R)

### **Tenon Retirement Plan Nominees Limited**

A T Johnston, P M Gillard, J E Paice, A S White, T B Highley (R)

### **Tenon Employee Educational Fund Limited**

P M Gillard, A C Grinter, J McDonald

### **Tenon Welfare Fund Nominees Limited**

P M Gillard, G D Niccol, M R Taylor

### **NACS USA, Inc**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Fletcher Wood Solutions, Inc**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Tenon USA Holding Company**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Tenon Supply, LLC**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **The Empire Company, Inc**

A T Johnston, P M Gillard, T H Highley, S L Moriarty, A S White, T B Highley (R)

### **The Empire Canada Company Limited**

A T Johnston, A S White, P M Gillard, C Rogers, T B Highley (R)

### **Kok's Woodgoods, Inc**

A T Johnston, A S White, P M Gillard, T B Highley (R), T H Highley (R)

### **Southwest Moulding Co LP**

A T Johnston, D Bell, P M Gillard, A S White, T H Highley, T B Highley (R)

### **AWM Acquisitions Corporation**

A T Johnston, A S White, P M Gillard

### **Ornamental Mouldings Company**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Ornamental Mouldings, LLC**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Ornamental Investments, LLC**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Comanche Investments, LLC**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Fairfield Road, LLC**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Ornamental Products, LLC**

A T Johnston, A S White, P M Gillard, T B Highley (R)

### **Creative Stair Parts, LLC**

A T Johnston, A S White, P M Gillard

## Statutory Disclosure continued

### Directors' Interests

In accordance with Section 140(2) of the Companies Act 1993, Directors advised the following changes in their interests:

<b>S G Kasnet</b>		
Escon Capital Inc.	Appointed	Director
Stratleade Inc.	Resigned	Trustee
<b>R H Fisher</b>		
Ultrafast Broadband Limited	Appointed	Chairman
Unison Networks Limited	Resigned	Director
<b>M J Andrews</b>		
CO2 New Zealand Management Company Limited	Resigned	Director
Tukia Group Limited	Resigned	Board Advisor

### Directors' and Officers' Indemnity and Insurance

In accordance with section 162 of the New Zealand Companies Act 1993 and the Constitution of the Company, the Company has given indemnities to, and has effected insurance for, Directors and executives of the Company and its related companies which, except for specific matters which are expressly excluded, indemnify and insure Directors and executives against monetary losses as a result of actions or omissions by them in the course of their duties. Specifically excluded from the indemnity are actions for criminal liability or breach of the Director's duty to act in good faith and in what the Director believes to be the best interests of the Company.

On 1 July 2011 the Company effected directors' and officers' liability and statutory liability insurance which was noted in the Interests Register.

### Dealing in Company Securities

The Company's Code of Conduct for Securities Trading supplements the New Zealand legislation prohibiting short-term trading and dealing in the Company's securities by employees, whilst they are in possession of non-public material and relevant information about the Company.

### Donations

Charitable donations totalling US\$7,000 were made during the year.

### Auditor's Fees

Fees payable to PricewaterhouseCoopers during the year are disclosed on page 33. During the year the auditor was paid US\$83,000 for non-audit related work for the Company, which is discussed on page 53.

### Credit Rating

Tenon has not sought a credit rating.

### Directors' Holdings – Equity Securities

#### Tenon Limited Ordinary Shares

	30 June 2011			30 June 2010		
	Beneficial	Non-Beneficial	Associated Persons	Beneficial	Non-Beneficial	Associated Persons
M J Andrews	–	–	11,943	–	–	11,943
R H Fisher	750	–	–	750	–	–
S G Kasnet	–	–	–	–	–	–
S L Moriarty	27,155	–	–	27,155	–	–
M C Walls	10,750	–	–	10,750	–	–
	<b>38,655</b>	–	<b>11,943</b>	<b>38,655</b>	–	<b>11,943</b>

## Shareholder Statistics

### Largest Shareholders

The 20 shareholders with the largest holdings of shares as at 31 July 2011 were:

	Tenon Ordinary Shares	% of Tenon Ordinary Shares
Rubicon Forests Holdings Limited	38,747,695	57.96
New Zealand Central Securities Depository Limited	17,958,067	26.86
Leveraged Equities Finance Limited	331,558	0.50
G J Butler & S J Butler	305,740	0.46
Sok Eng Boey & Yeow Ann Chiam & Kay Hong Chiam & Shen Mei Chiam	255,000	0.38
C W Flood	200,000	0.30
Tenon Custodians Limited	182,548	0.27
Chin-Yi Lin & Yu-Ching Lin-Chao	180,150	0.27
Tenon Employee Educational Fund Limited	144,721	0.22
J E C Anderson & B L Denholm	140,000	0.21
E A Badham & L J Badham	92,367	0.14
Zero Commission New Zealand Limited	84,590	0.13
J B Mortimore & R A Hadfield	78,500	0.12
A Kaan & M Kaan & A Blackwood	70,000	0.10
Fletcher Building Nominees Limited	58,000	0.09
Walker Capital Management Limited	56,624	0.08
Sing Kwan Lee & Miu Chun Lee Ma	52,362	0.08
Custodial Services Limited	51,721	0.08
D Loo	50,500	0.07
J W Carson	50,000	0.07
	59,090,143	88.39
Total Shares	66,850,661	

### NZCSD

New Zealand Central Securities Depository Limited ("NZCSD") is a depository system which allows electronic trading of securities to its members. At 31 July 2011, the shareholdings held through NZCSD were:

	Tenon Ordinary Shares	% of Tenon Ordinary Shares
Accident Compensation Commission	4,756,948	7.11
Courtenay Nominees Limited	337	0.00
Citibank Nominees (New Zealand) Limited	2,197,871	3.29
Guardian Trust Investment Nominees (RWT) Limited	1,855	0.00
HSBC Nominees (New Zealand) Limited – A/C State Street	10	0.00
HSBC Nominees (New Zealand) Limited	38,248	0.06
J P Morgan Chase Bank NA	160,911	0.24
National Nominees New Zealand Limited	10,801,731	16.16
NZ Guardian Trust Investment Nominees Limited	156	0.00
	17,958,067	26.86
Total Shares	66,850,661	

## Shareholder Statistics continued

### Distribution of Shares – 29 July 2011

Size of Holdings	Ordinary Shareholders		Ordinary Shares	
	Number	%	Number	%
1 – 200	1,489	23.71	207,101	0.31
201 – 500	1,725	27.47	571,301	0.85
501 – 5,000	2,803	44.63	3,675,629	5.50
5,001 – 10,000	134	2.13	980,304	1.47
Over 10,000	129	2.06	61,416,326	91.87
<b>Total</b>	<b>6,280</b>	<b>100.00</b>	<b>66,850,661</b>	<b>100.00</b>

Less than a minimum holding: As at 29 July 2011, 3,214 holders of Ordinary shares held less than the minimum holding of 500 or less shares under the NZX listing rules.

### Supplemental Disclosure of Domicile of Beneficial Owners<sup>(1)</sup>

	Ordinary Shares	
	Number	%
New Zealand	53,418,075	79.91
United States of America	12,649,979	18.92
Other	782,607	1.17
<b>Total issued voting shares as at 8 August 2011</b>	<b>66,850,661</b>	<b>100.00</b>

(1) Updated for information received by 8 August 2011 in response to notices under sections 28 and 29 of the New Zealand Securities Markets Act 1988.

### Substantial Security Holders

As at 19 August 2011 the following persons have given notice (in terms of the New Zealand Securities Markets Act 1988) that they are substantial security holders in Tenon. In terms of the Act, the number of Tenon ordinary shares shown as held below is as last advised to Tenon by the substantial security holder.

	Tenon Ordinary Shares	% of Tenon Shares
Rubicon Forests Holdings Limited	38,747,695	57.96
Third Avenue Management LLC	10,482,120	15.68
Accident Compensation Commission	4,617,628	6.91
<b>Total</b>	<b>53,847,443</b>	<b>80.55</b>
<b>Total issued voting shares as at 19 August 2011</b>	<b>66,850,661</b>	

## Investor Information

Tenon reports six-monthly for the half year (to 31 December) and full year (to 30 June).

Copies of the Half Year and Annual Reports are available on the Company's website, [www.tenonglobal.com](http://www.tenonglobal.com).

### 2011-2012 Calendar

- Half Year End: 31 December 2011
- Half Year Results Announcement: February 2012
- Financial Year End: 30 June 2012
- Annual Results Announcement: August 2012
- Mailing of Annual Report: September 2012

### Dividend

There is no 2011 dividend.

### Tenon Shares

Tenon Limited has one class of shares, Ordinary shares.

### New Zealand Exchange

Ordinary shares    TEN

### Issued Share Capital (Number of Shares)

Ordinary shares    66,850,661 as at 19 August 2011

### Share Registry Enquiries

#### Enquiries

Computershare Investor Services Limited

Private Bag 92119,

Auckland 1142

159 Hurstmere Road,

Takapuna, North Shore City 0622

New Zealand

Telephone: 64-9-488-8777

Facsimile: 64-9-488-8787

E-mail: [enquiry@computershare.co.nz](mailto:enquiry@computershare.co.nz)

Please assist our registry by quoting your CSN or shareholder number.

#### Managing your shareholding online

To change your address, update your payment instructions, and to view your investment portfolio including transactions, please visit:

[www.computershare.co.nz/investorcentre](http://www.computershare.co.nz/investorcentre).

### Company Websites

[www.tenonglobal.com](http://www.tenonglobal.com)

[www.empireco.com](http://www.empireco.com)

[www.ornamentalmouldings.com](http://www.ornamentalmouldings.com)

[www.southwestmoulding.com](http://www.southwestmoulding.com)

[www.lifespanoutdoor.com](http://www.lifespanoutdoor.com)

[www.fwsdirect.com](http://www.fwsdirect.com)

### Other Investor Enquiries/Registered Office

Investor Relations

Tenon Limited

Level 3,

7 Fanshawe Street,

Auckland, 1010

Private Bag 92036,

Auckland, 1142, New Zealand

Telephone: 64-9-368-4193

Facsimile: 64-9-368-4197

E-mail: [investor-relations@tenon.co.nz](mailto:investor-relations@tenon.co.nz)

### Forward-Looking Statements

There are statements in this document that are "forward-looking statements". As these forward-looking statements are predictive in nature, they are subject to a number of risks and uncertainties relating to Tenon, its operations, the markets in which it competes and other factors (some of which are beyond the control of Tenon). As a result of the foregoing, actual results and conditions may differ materially from those expressed or implied by such statements. In particular, Tenon's operations and results are significantly influenced by the level of activity in the various sectors of the economies in which it competes. Fluctuations in industrial output, commercial and residential construction activity, changes in availability of capital, declining housing turnover and pricing, declining levels of repairs, remodelling and additions to existing homes in North America, relative exchange rates, interest rates in each market, and profitability of customers, can have a substantial impact on Tenon's results of operations and financial condition. Other risks include competitor product development and demand and pricing and customer concentration risk.

### Directors

Simon Luke Moriarty (Chairman)

Michael John Andrews

Rodger Herbert Fisher

Stephen Garfield Kasnet

Michael Carmody Walls

See page 50 for details of Directors.

### Executive Officers

#### **Tom Highley – Chief Executive Officer**

Tom Highley was appointed Chief Executive Officer on 1 September 2010. Tom's previous role was President and Chief Operating Officer of The Empire Company Inc. (a Tenon Group subsidiary), which he had held for five years. Tom joined The Empire Company in 2001 as Vice President of the Pro-Dealer National Chain business. He was promoted to Vice President of the entire Pro-Dealer Division in May of 2002, and subsequently to President of Empire in September of 2004. Prior to Tom's employment with the Tenon Group, he held a number of positions in sales, marketing and management within the consumer products and medical device industries. Tom has a Bachelor degree in International Relations and Economics from the University of Wisconsin in Milwaukee and an MBA from the University of Michigan Ross School of Business. Tom leaves Tenon in October 2011.

#### **Tony Johnston – Chief Operating Officer**

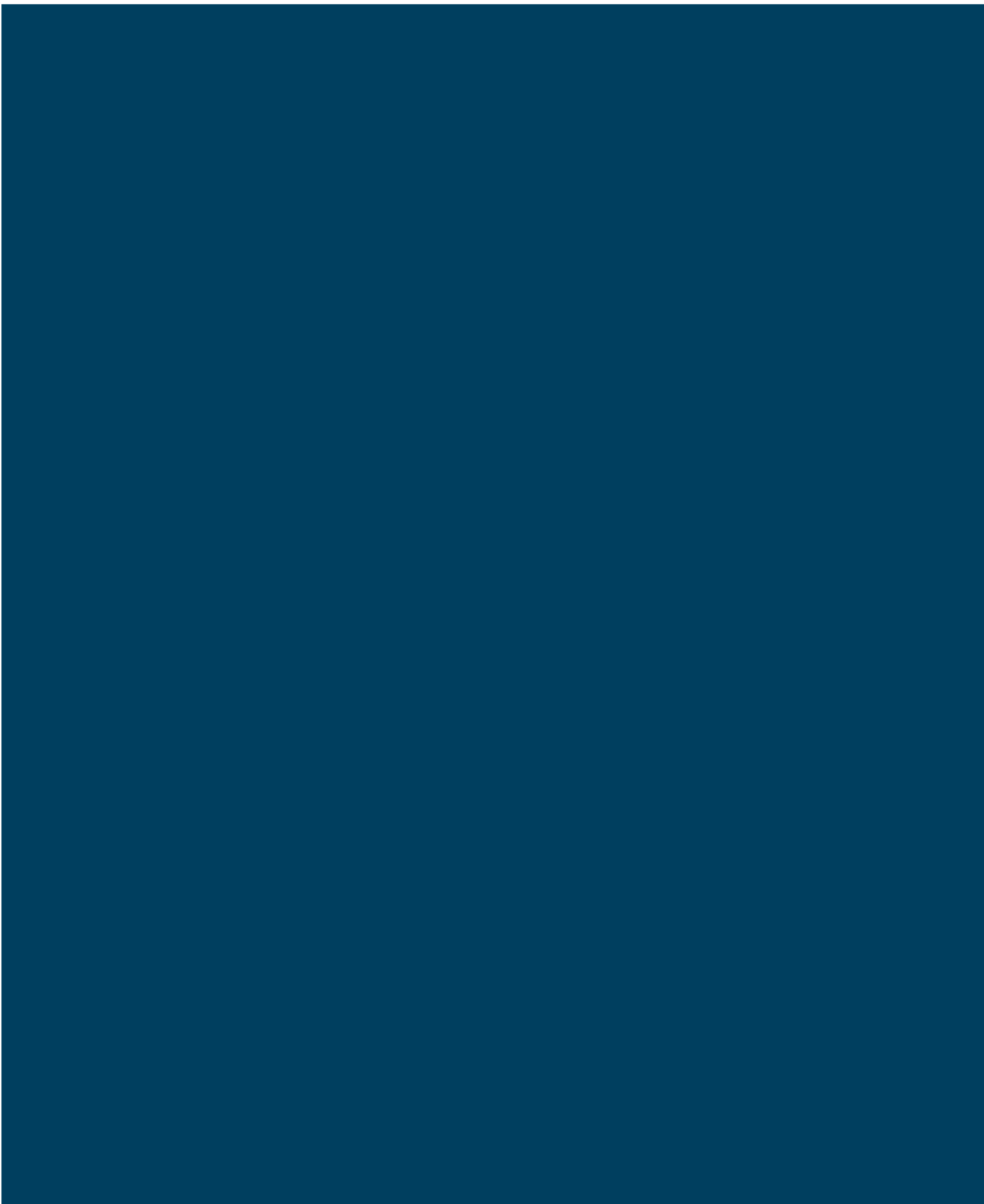
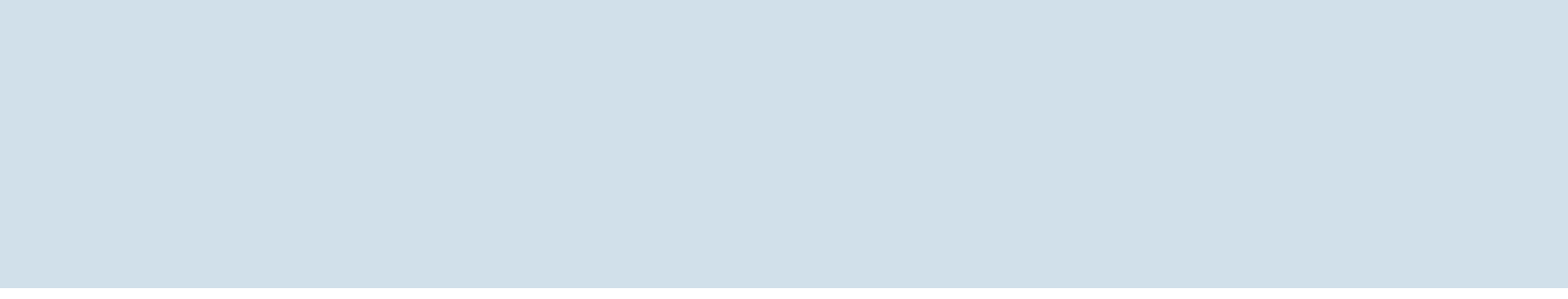
Tony Johnston joined Tenon in May 2011. Tony has 20 years experience in manufacturing, international sales, marketing and distribution in the wood products sector, returning to Tenon having formerly been a senior executive of the Company in its early stages of growth into the US. In that role he led the North American Consumer Solutions business, where he spearheaded Tenon's initial entry into the North American distribution market. Tony was previously an executive director of LumberLink Limited, an international wood marketing and export company he co-founded, based in New Zealand, and prior to that was the inaugural CEO of Wood Processors Association of New Zealand, Chairman of WOODCO (the NZ Forest Products Industry body), CEO of Thames Group Limited, a processor of pruned Radiata pine logs and marketer of lumber to the USA and elsewhere, and Group General Manager of Sales and Marketing for AFFCO, a New Zealand beef and lamb processing sales and marketing organization. Tony was also a senior executive in Tenon's predecessor Fletcher Challenge Forests business during the 1990s.

#### **Adam White – Chief Financial Officer**

Adam White joined Tenon Limited in 1999 as Commercial Manager for the North America business unit. He was appointed Chief Financial Officer of Tenon Limited in March 2006. He was also appointed Chief Financial Officer of The Empire Company Inc in March 2007, a role he previously occupied until February 2004. Prior to joining Tenon, Adam held corporate accounting roles in the UK and has worked for PricewaterhouseCoopers in New Zealand and the UK. Adam holds a Bachelor of Science degree from the University of Aston in Birmingham, UK.

#### **Paul Gillard – General Manager, Corporate**

Paul Gillard joined Tenon Limited in 2001. Paul's role includes company secretarial and governance, legal affairs and commercial negotiations for the Group. He had previously spent five years as Corporate Counsel with EDS (New Zealand) Limited, one of New Zealand's largest IT service providers. Paul's role with EDS also encompassed responsibilities in Australasia, for the EDS Group. From 1989-1996 he was Corporate Counsel and manager of the legal department for Telecom Limited. Paul formerly practised as a lawyer to partnership level in New Zealand, and also worked for a law firm in Washington DC. Paul has a Bachelor of Laws from Victoria University in Wellington.



[www.tenonglobal.com](http://www.tenonglobal.com)