Tenon
Wood Solutions to the World

# 2013

## Annual Report

## Contents



## Forward-looking Statements

There are forward-looking statements included in this document. As 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, particularly in North America. Fluctuations in industrial output, commercial and residential construction activity, capital availability, housing turnover and pricing, levels of repair and remodelling and additions to existing homes, new housing starts, relative exchange rates, interest rates, 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.

# Fiscal 2013 – Highlights

- Tenon share price more than doubled across the fiscal year;
- Recovery in the US housing market now evident –
  - Housing starts up 25% in 2013, year-over-year ("y-o-y")
  - New home sales up 26% y-o-y
  - Existing home sales up 15% y-o-y
  - Existing home prices up 12% y-o-y
- Revenue of $364 million, was up 9% on the previous year;
- Revenue from pro-dealer (i.e. primarily new house builder) customers up 25% y-o-y;
- Earnings result was in line with previous market guidance given;
- Net Profit after Taxation is projected to turn positive in 2014, (Net Loss after Taxation of $3 million in 2013, $9 million in 2012);
- EBITDA (a non-GAAP measure)(1) increased from a loss of $3 million (including restructuring costs) in 2012 to a profit of $5 million in fiscal 2013, and was achieved despite –
  - A higher NZ$/US$ cross rate, which averaged 82 cents across the year, negatively impacting earnings by $1 million
  - Business re-engineering costs incurred of $1 million;
- 80% of fiscal 2013 operating earnings were contributed in the second half of the year, indicating on-going momentum in the US market recovery;
- Tenon is leveraged both to new housing (45%) and DIY / retail (55%), and will be a beneficiary of the broader recovery in the US housing market as it occurs;
- Tenon is targeting fiscal 2014 EBITDA to be double that reported in 2013;

(1) EBITDA (i.e. Earnings before Interest, Taxation, Depreciation and Amortisation, please also refer to note 26 of the Financial Statements) is a non-GAAP earnings figure that equity analysts tend to focus on for comparable company performance analysis, because that number removes distortions caused by the differences in asset ages, depreciation policies, and debt : equity structures. EBITDA is calculated as Net Profit/Loss after Taxation of $-3 million (June 2012: $-9 million) less Income tax benefit of nil (June 2012: $2 million), plus Financing Costs of $4 million (June 2012: $3 million) and depreciation and amortisation of $4 million (June 2012: $5 million).

# Review of the 2013 Fiscal Year

## The 2013-Year Reviewed

In our December Interim Report to shareholders we wrote –

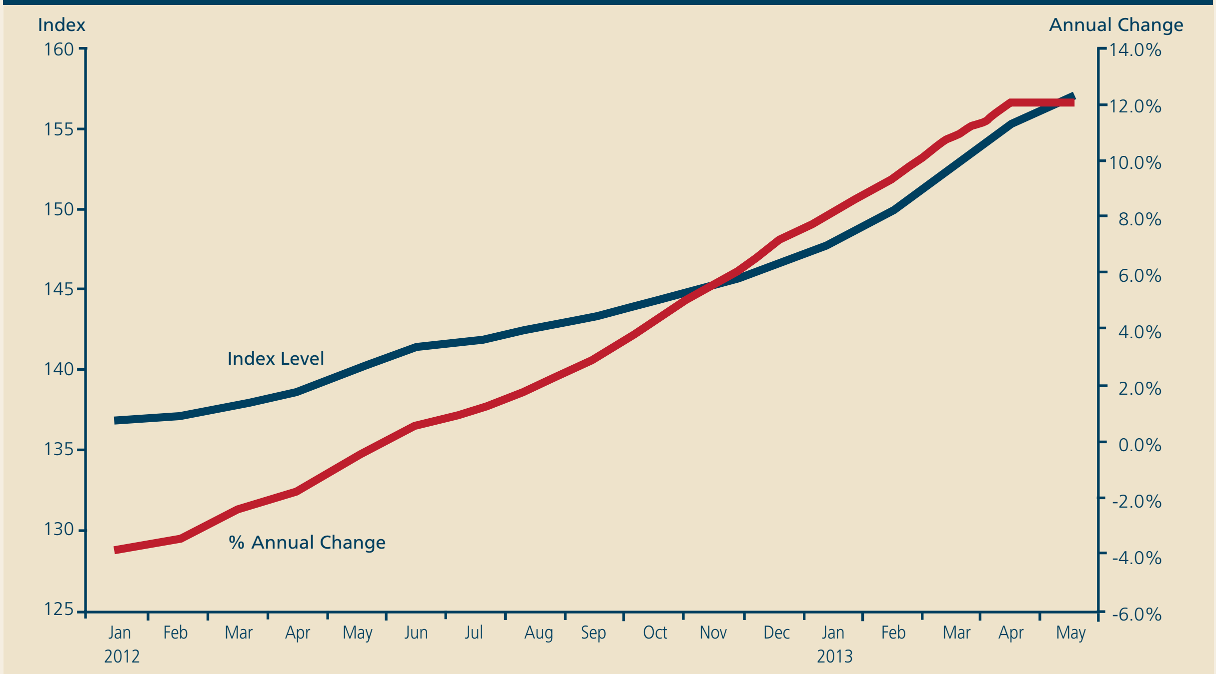
*"The US housing market – Tenon's largest market exposure – is now in the early stages of a full recovery. This is an extremely positive development for Tenon, although it is really only in very recent months that this improvement has occurred in any meaningful way. To date this recovery has been centred on new house construction, but the forward looking data now indicates that the rebound should also spread into a higher level of renovation and remodelling activity later in this calendar year. Given Tenon is exposed to both segments of the market (but more particularly the latter segment), we should see the benefit of the broader market recovery reflected in our earnings as the calendar year advances.*

*Although there are some notable hurdles to a full US housing market recovery … and moving forward the month-to-month data is likely to be a little bumpy, it appears clear now that we are heading out of the deep cycle-trough that has plagued the industry for too many years now."*

These statements proved to be absolutely true for the balance of fiscal 2013. This can be seen from a quick review of US industry data for the fiscal 2013 year, which showed –

- US housing starts up more than 25% on fiscal 2012;
- Permits issued for new house construction, at 918,000 (seasonally adjusted annual rate) in June, up 17% y-o-y;
- New homes sold up 26% y-o-y;
- New home inventory (measured in months of supply) at year-end was 4.3 months;
- New home average price up 11% y-o-y;
- Home builder confidence ending the year at the highest level recorded since 2006;
- Existing home sales up 15% y-o-y, to 5.1 million units;
- Existing home inventory down 20% to 5.1 months of supply, compared with 6.4 months a year ago;
- The pending home sales index (a forward looking indicator of existing home sales) at its second highest level since December 2006, and 11% higher than the prior year; and
- Existing home prices (as measured by the Case-Shiller index on the next page) up 12% y-o-y.

## S&P / Case-Shiller 20-City Composite (Seasonally Adjusted)




Each of these, individually, represents a very positive data point, but when taken in the aggregate they are reflective of a much broader housing recovery that is now underway in the US. It is pleasing to report that although we are only in the initial phase of this recovery, Tenon has already begun to benefit from these improved market conditions. A few highlights from our fiscal 2013 reported financial results show this point -

- **At $364 million, Revenue was up $30 million, or 9%, on the previous year.** Notably, Revenue recorded in the second half of the fiscal year was $190 million - up on the $174 million recorded in the first half, reflecting the acceleration in activity that occurred as the fiscal year progressed.

  This growth in top line revenue came primarily from a 25%+ increase in sales to our pro-dealer customers (who now represent approximately 45% of our total North American revenues), who in turn supply the new home construction market. Tenon has seen a strong recovery in the pro-dealer regional markets it services, and it is now beginning to benefit from the growth in market share that has been achieved in this segment over the past five years.

  Whilst to date the recovery in remodelling activity (as represented by sales into the large national home improvement centres) has lagged new home construction activity, this was as expected, and our large retail distribution operation that supplies this channel (i.e. Empire) began to show comparable store sales growth in the latter part of fiscal 2013.

  In addition, sales revenue in the period also benefited from geographic expansion and favourable product mix changes undertaken late in the year. In particular, our Taupo manufacturing operation rebalanced its product portfolio across lumber, clear boards and solid lineal mouldings products to optimise customer sales and margin opportunities.


Tenon supplied the finishing internal clearwood, from its Taupo operation in New Zealand, for the Waka inspired headquarters of Emirates Team New Zealand, at the 2013 America's Cup in San Francisco.

- **Gross profit of $83 million was recorded.** Importantly, in terms of on-going future market recovery, gross profit recorded in the second half of fiscal 2013 was 8% higher than in the first half of the year.

  The "thinness" of the industry supply-chain in a recovering US housing market saw manufacturers (including our own Taupo operation) place customers (i.e. distributors into the US, such as Empire) on product supply allocations during the period. Accordingly, our Cost of Sales increased in the period, as our third-party suppliers were able to push through product price increases in this very tight supply environment, and also as our absolute volume of purchases increased to match market demand. While our gross margin compressed slightly in the period by just over 1%, we believe this can be recovered as we continue to take costs out of the business (see below) and as the housing recovery cycle matures.

- **Operating Profit before Financing Costs[(1)] of $1 million compared favourably with the loss of $8 million recorded in the prior year** (including $3 million of Restructuring Costs).

  This much improved result was assisted by our on-going efforts to re-engineer our activities in order to improve efficiency and take costs out, which resulted in Distribution and Administration Expenses falling by $3 million y-o-y, despite sales volumes increasing over the period. These business re-engineering initiatives included -

(1) Operating Profit before Financing Costs is a non-GAAP financial measure and is calculated as Net Profit/( Loss) after Taxation of $-3 million (June 2012: $-9 million) less Income tax benefit of nil (June 2012: $2 million) plus Financing Costs of $4 million (June 2012: $3 million), please also refer to the Consolidated Income Statement on page 13 of the Financial Statements and note 26 of the Financial Statements.

- Completion of the consolidation of Ornamental's manufacturing activities onto one US site in North Carolina. The order files and manufacturing lines have now been transferred, functions have been integrated into Tenon's North American shared services operation, and all surplus Canadian property has now been sold releasing $3 million of cash. The results for the year include all costs relating to manufacturing "start-up" of the product lines now being produced at the single North Carolina site;

- Relocation of Southwest's Dallas pro-dealer operation to a larger, special purpose warehousing facility. Although the overall floor space has been expanded to match increased demand forecasts, efficiency gains allowed Southwest to improve its warehouse space utilisation and lower its overall costs in the second half of the year;

- Implementation of IT enhancements (e.g. electronic order confirmation, delivery and invoicing) across the Group which will assist in both improving working capital management and lowering back-office administration costs;

- Cost-out and efficiency improvement initiatives at our Taupo manufacturing facility, including the renegotiation of more favourable shipping contracts, and the achievement of improved sawmill conversion and clear-wood recovery rates resulting in significant cost savings; and

- Cost reduction initiatives in our North American distribution operations, including the restructuring of field services and product delivery activities, resulting in improved (i.e. more efficient) store service management, and reduced transportation and labour costs.

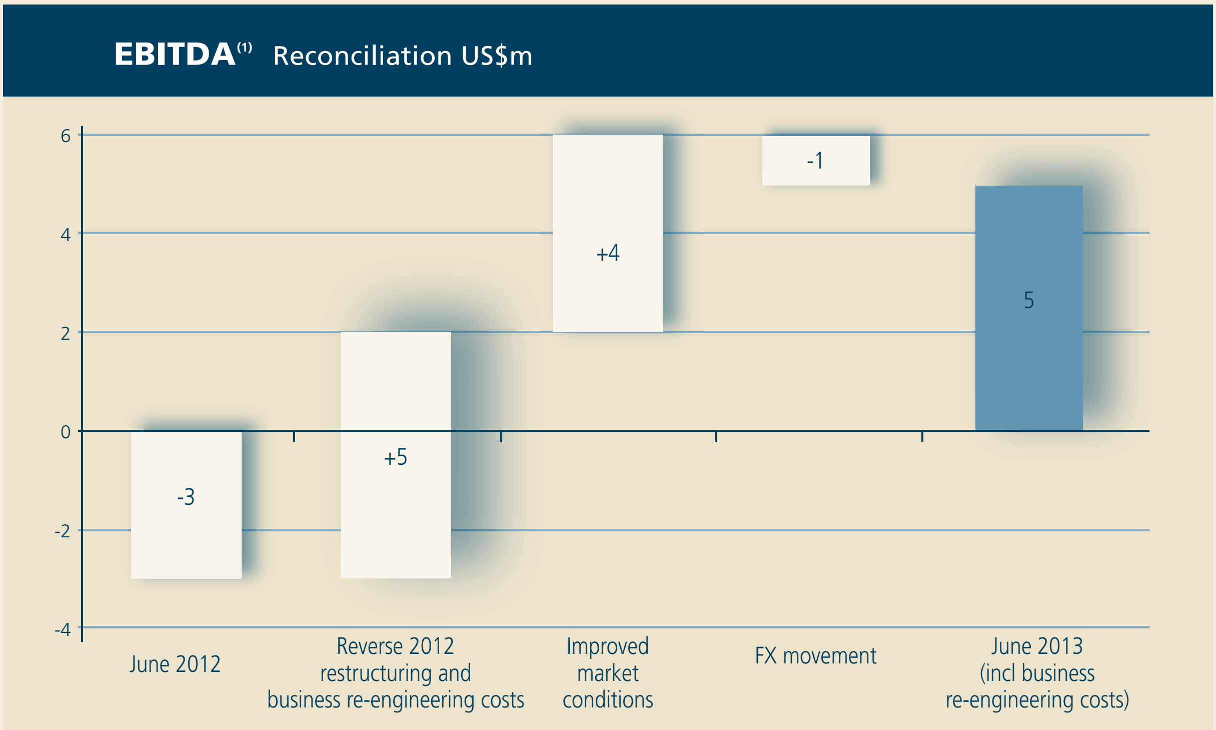
- After Financing Costs of $4 million, we recorded a **Net Loss after Taxation of $3 million (a $6 million improvement on fiscal 2012) however, we are projecting to report a Net Profit after Taxation in 2014.**

- **EBITDA(1) improved from a loss of $3 million last year (including restructuring costs) to a profit of $5 million in fiscal 2013.** This result was in line with the $4 - $5 million EBITDA market guidance announcement the Company made in May this year, and included business re-engineering costs of $1 million which were fully expensed in the period. This result was also achieved despite the headwind of a strengthening NZ dollar, which saw the average NZD : USD cross rate rise to an average 82 cents across the year, and which resulted in a $1 million negative impact on EBITDA in fiscal 2013.

  Of further note was the significant improvement in EBITDA achieved in the second half of fiscal 2013 compared with the first half – i.e. $4 million compared with $1 million. This is entirely consistent with the guidance we gave in last year's Annual Report to shareholders, when we said that any short-term lift in Tenon's earnings as a result of market recovery was unlikely to be felt until the second half of fiscal 2013.

(1) EBITDA is a non-GAAP financial measure. Please refer to note 1 on page 1 of this Annual Report, and also to note 26 of the Financial Statements.

This next chart shows the fiscal 2013 EBITDA summary reconciliation from last year's result.




- Total debt[(2)] increased from $39 million at 30 June 2012 to $49 million at balance date. This increase is a direct result of the higher inventory we need to carry as the market enters its recovery phase, in order to ensure we have no stock-outs with our delivery-sensitive customers as sales grow in our core product lines.

We do not see this level materially declining in the short term. Indeed, in order to continue to grow and expand our product categories, to meet our existing customers' needs, and to provide us with greater day-to-day operational flexibility, we determined a need to increase the size of our existing debt funding facility. Our objective is to put in place a bank facility that will allow Tenon to advance through the cyclical recovery in the US housing market on a much stronger financial footing. As at the date of this Review, negotiations to this end were well advanced, and we believe we will be in a position to make a positive announcement to the market on this in the very near future.

(1) EBITDA is a non-GAAP financial measure. Please refer to note 1 on page 1 of this Annual Report, and also to note 26 of the Financial Statements.

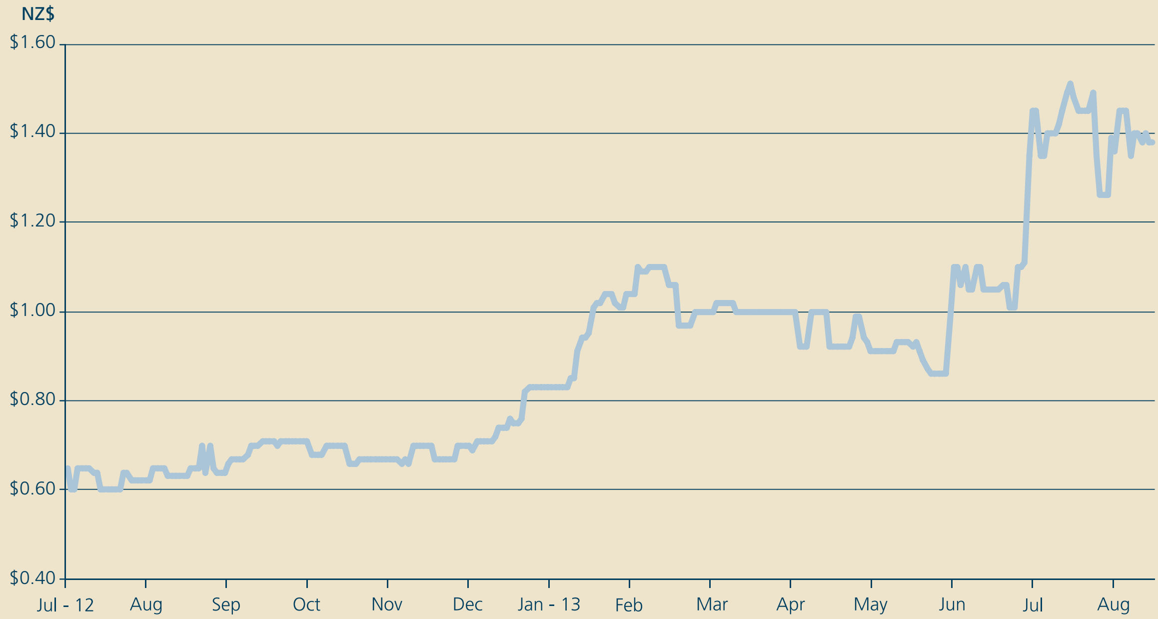
(2) Total debt is calculated as Current Debt of $1 million (June 2012: $1 million) plus Non-Current Debt of $46 million (June 2012: $37 million) plus Bank Overdraft of $2 million (June 2012: $1 million).

## Governance

Our last ASM was held in Wellington (NZ) on 13th of December 2012. Over 80% of the Company's issued shares were voted at the meeting, and all resolutions were passed - each with a majority of in excess of 99%. These excellent voting statistics are a reflection not only of the company's consolidated share register, but also of the confidence that shareholders have in Tenon's future.

Our ASM presentations (which are available on our website at **www.tenonglobal.com**) outlined the future potential for the Company in a recovering US housing market environment. As discussed above, US housing market data has been very positive showing healthy year-over-year gains, indicating that the US market is now clearly in a recovery-mode. All of this news, coupled with our earnings guidance announcement in May, has been positive for our share price performance, which, at the time of writing, had increased 85% since our ASM, and which has more than doubled off last year's low. This is well above the 15% recorded by the NZX50 over the same period (since our ASM).

**Tenon Share Price Performance**




While this is good news, we still believe our traded share price is well below "fair value" as at this point in the cycle. This view is supported by an equity analyst report released by the Edison Group early this calendar year which valued Tenon up to NZ$2.05 per share (inclusive of tax losses), and more recently (in a June Update Note) Edison made the comment that upwards share price moves by Tenon's US peer group comparators "suggests upside above NZ$2.00."

The Company's next ASM will be held in December 2013. We will separately advise shareholders of the time and venue at a later date. For those shareholders who are able to join us, we would of course very much appreciate your attendance.

## Looking Ahead

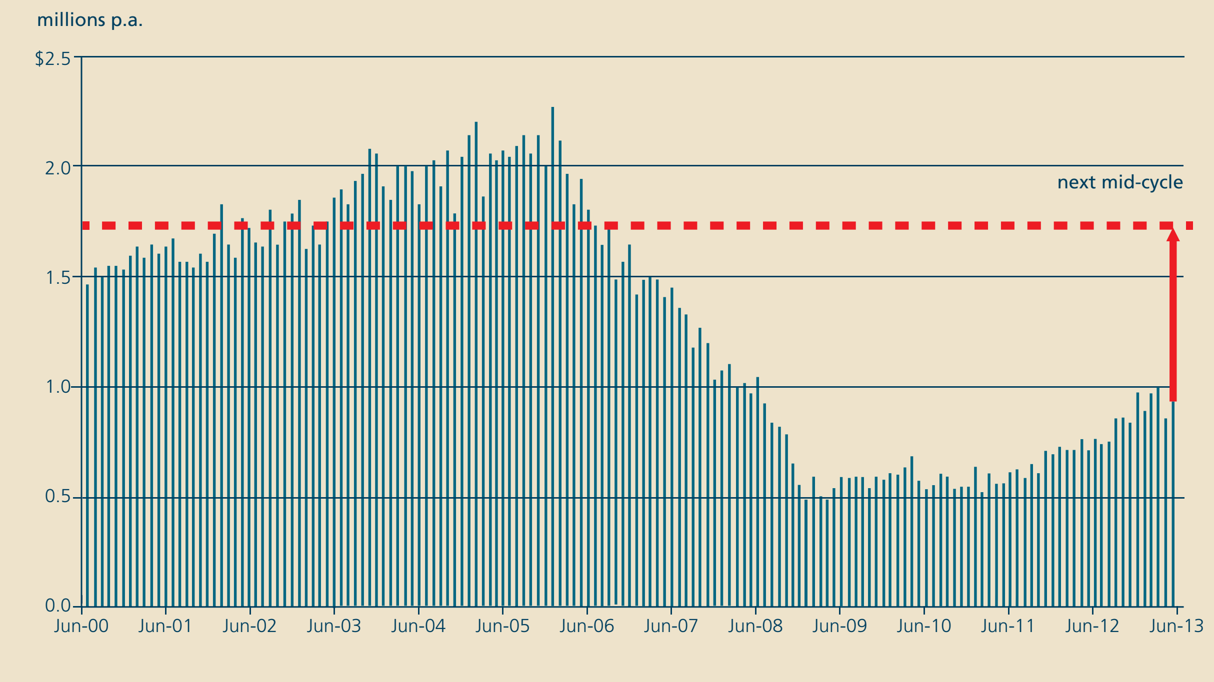
In our last Report we discussed the opportunity to also grow Tenon outside our core North American market, with Europe and China being specifically targeted. Operationally, we have more than tripled our clear-wood sales volumes into Europe over the past 12 months, and we have identified specific opportunities to take some of our Taupo manufactured products directly into retail channels in China rather than through the traditional wholesale market there. We have also identified new innovative products manufactured in China that we may be able to take directly into our US distribution channels. While this marketing work will continue, we have made the difficult short-term decision to slow our strategic advance into China in order to take full advantage of a quickly recovering US market. Although we had identified an entry point acquisition that would have placed us directly into the China wholesale market, we have determined that in the immediate term the risk : reward trade-off overwhelmingly now favours us focusing the bulk of our financial resources on the US marketplace.

Tenon has significant market exposure to US housing through our activities in both the new home construction and remodelling markets (now representing approximately 45% and 55% of Tenon's total North American revenues, respectively), and the continued recovery in each of these markets will support our future earnings performance. While the future month-to-month US housing data is likely to be bumpy (with the lower July new house sales data being such an example), an overall upward trend is expected to continue. However, access to mortgage credit, and the potential for rising mortgage rates resulting from a tighter US Federal Reserve monetary stance, must be considered as very real potential risks to a smooth recovery – each being a factor beyond Tenon's control. However, on the basis that the US housing recovery proceeds as we predict and the NZ : US cross rate does not strengthen from recent levels, then **our immediate earnings objectives are to more than double our fiscal 2013 EBITDA(1) result in the current fiscal 2014 year, and to materially improve that result again in the calendar 2014 year. If we can achieve these outcomes, then the Tenon share price should appreciate accordingly, continuing the price gains that have been made over the past 6-9 months.**

As we have previously noted, while this first phase of cyclical recovery in the US housing market is very encouraging, the forecast 2014 activity levels will still be a long way away from projected industry mid-cycle levels. By way of example, the chart on the next page succinctly shows the "gap" that exists between today's construction level and the projected future mid-cycle new house construction level (the dotted red line), based on underlying demand supported by strong population growth and demographics.

(1) EBITDA is a non-GAAP financial measure. Please refer to note 1 on page 1 of this Annual Report, and also to note 26 of the Financial Statements.

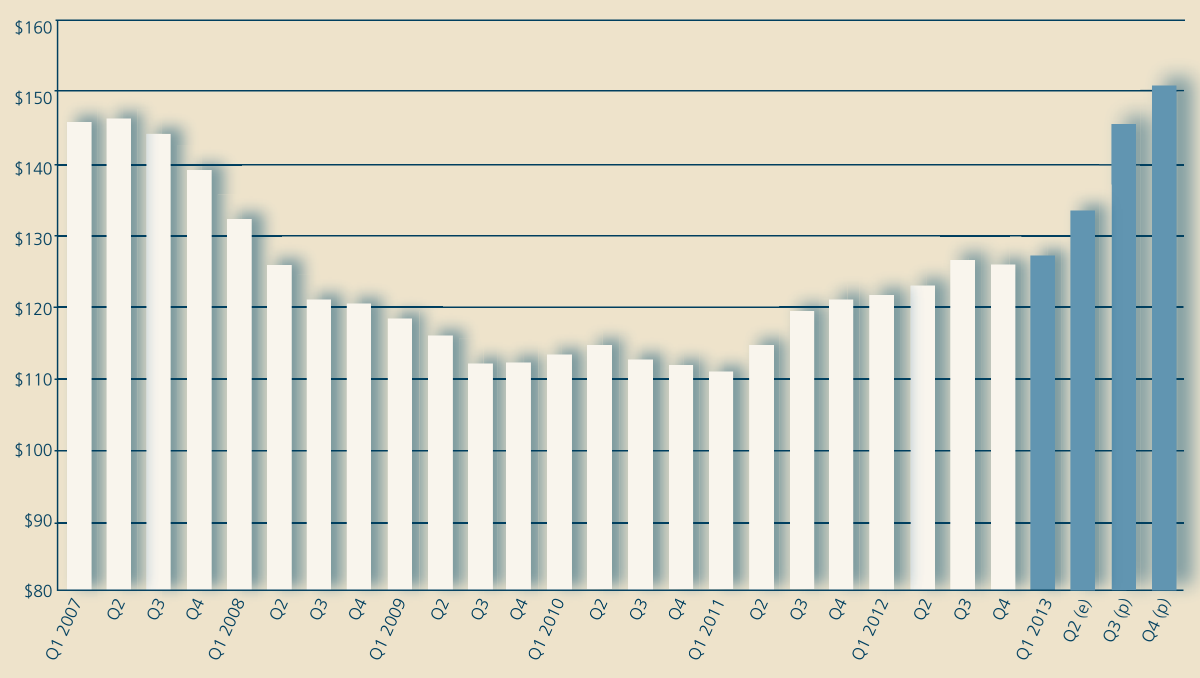
## US Housing Starts




A similar story holds true for the renovation and remodelling segment, where pent-up demand arising from the past five years of below average residential spending / investment is expected to see this segment expand more in the next mid-cycle than it did in the previous cycle peak. This can be seen in this next chart, Harvard's Housing Studies Leading Indicator of Remodelling Activity (LIRA), which projects strong growth through the balance of calendar 2013.

## Lending Indicator of Remodelling Activity (LIRA)

Homeowner Improvements 4-quarter moving totals
$ billions - July 2013 projections



Quite apart from these positive broader macro-industry factors that are expected to drive our earnings, we do also expect to reap the benefits from Company specific growth and profit improvement initiatives that continue to be identified and implemented. Examples of benefits expected to accrue from initiatives implemented this current fiscal year include -

- Annualised contribution to sales and earnings of new products launched during the second half of fiscal year 2013 (e.g. hardwood boards and plank panels);

- A significant lift in clear select pine board sales in fiscal year 2014, resulting from the substantial pick-up in retail/DIY volume requirements for this product - to be distributed via Empire, and sourced exclusively from our Taupo manufacturing facility;

- Strengthened relationships in Australia with the Mitre 10 and Danks chains, which are expected to deliver growth in this region, particularly in the specialist small moulding category where we have a clear competitive advantage; and

- Launch of new, smaller profile decorative hardwood moulding product lines into the North American home centre channels, targeted to occur in this fiscal year.

At our ASM in December, we outlined what our earnings potential might look like under future mid-cycle conditions – conditions where we see EBITDA of $35 - 40 million being achievable (assuming a mid-cycle NZ : US cross rate of 70 cents, and historic margin levels). Shareholders will understand that this expanded potential is a result of the significant organic growth that we have put in place through the down-cycle (refer 2012 Annual Report for a discussion of the growth that has been embedded in the Company). To date the gains from these growth initiatives have been masked by the extent of the downturn that has taken place, however they will become obvious as the market progresses to a mid-cycle path and the pace of recovery gains momentum.

Acquisitions remain on the agenda, and these opportunities will be focused on the large North America market, where we already have scale and where we have the ability to quickly integrate and leverage new activities into our existing business model.

Finally, we would like to thank all of our stakeholders for their continued support. As always, it is very much appreciated.

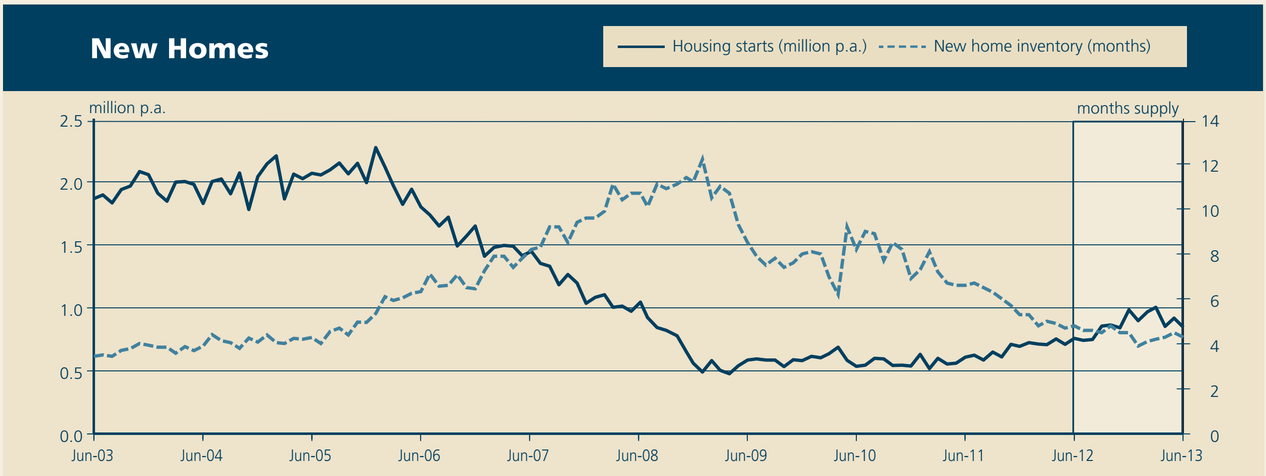
Sincerely,

Luke Moriarty
Chairman

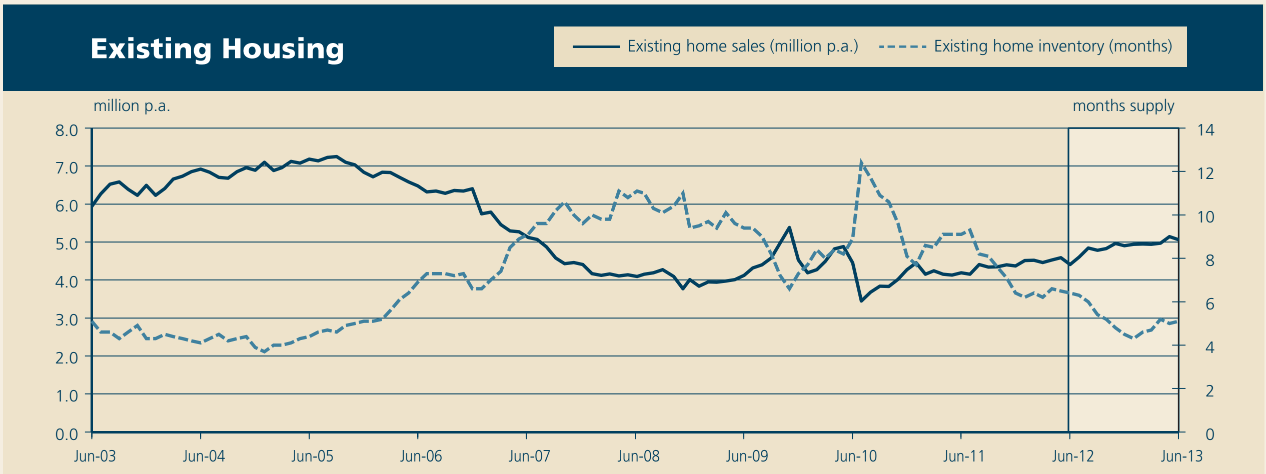
Tony Johnston
Chief Operating Officer

27 August, 2013

## New Homes

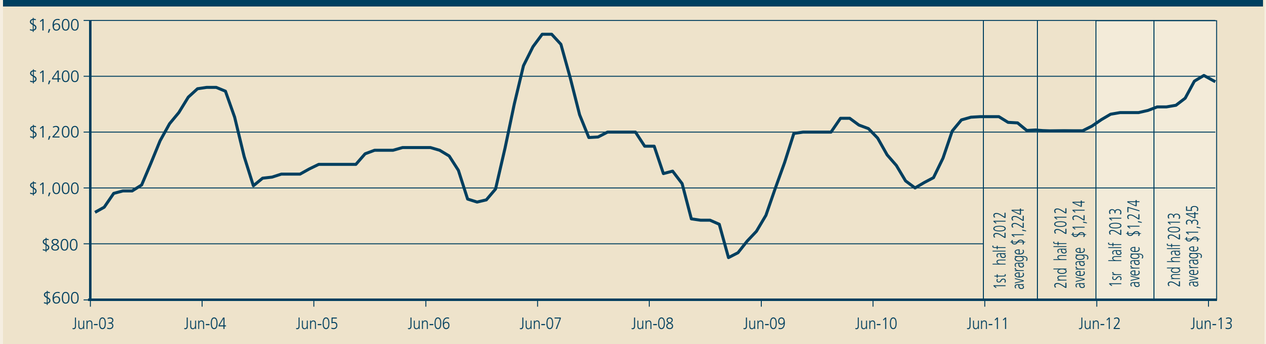



## Existing Housing




## Moulding and Better Lumber Pricing

US$ mbf




## NZD/USD Exchange Rate

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

# Financial Statements and Corporate Governance

# Consolidated Income Statement for year ended 30 June

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Note | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|---|
| – | **–** | Revenue | | **364** | 334 |
| – | **–** | Cost of Sales | 5 | **-281** | -254 |
| – | **–** | Gross Profit | | **83** | 80 |
| – | **–** | Distribution Expense | 5 | **-69** | -71 |
| – | **–** | Administration Expense | 5 | **-13** | -14 |
| – | **–** | Restructuring Costs | 5 | **–** | -3 |
| – | **–** | Operating Profit before Financing Costs | | **1** | -8 |
| -17 | **-18** | Financing Costs | 19 | **-4** | -3 |
| -17 | **-18** | Profit / (Loss) before Taxation | | **-3** | -11 |
| – | **–** | Income Tax (Expense) / Benefit | 6 | **–** | 2 |
| -17 | **-18** | Net Profit / (Loss) after Taxation | | **-3** | -9 |
| | | **Earnings Per Share Information** | | | |
| | | Basic and Diluted Net Earnings per Share (cents) | 7 | **-4.8** | -13.9 |

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 2012 US$m | Tenon Limited 2013 US$m | | Note | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|---|
| -17 | **-18** | Net Profit / (Loss) after Taxation for the year | | **-3** | -9 |
| | | Items that maybe recycled to the Consolidated Income Statement: | | | |
| – | **-1** | Net movement of Cash Flow Hedges net of Tax | 9 | **-1** | – |
| 13 | **3** | Movement in Currency Translation Reserve | 9 | **–** | -1 |
| 13 | **2** | Other Comprehensive Income for the year, net of Tax | | **-1** | -1 |
| -4 | **-16** | Total Comprehensive Income for the year | | **-4** | -10 |

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 US$m | Retained Earnings US$m | Cash Flow Hedge Reserves US$m | Revaluation Reserve US$m | Net Currency Translation US$m | Total Group Equity and Reserves US$m |
|---|---|---|---|---|---|---|---|
| As at 1 July 2011 | | 533 | -408 | – | 1 | 6 | 132 |
| Net Profit / (Loss) after Taxation for the year | | – | -9 | – | – | – | -9 |
| Other Comprehensive Income / (Loss) for the year | | – | – | – | – | -1 | -1 |
| Total Comprehensive Income Attributable to the Equity holders of the Parent | | – | -9 | – | – | -1 | -10 |
| Share Buyback (1) | | – | – | – | – | – | – |
| As at 30 June 2012 | 9 | 533 | -417 | – | 1 | 5 | 122 |
| As at 1 July 2012 | | 533 | -417 | – | 1 | 5 | 122 |
| Net Profit / (Loss) after Taxation for the year | | – | -3 | – | – | – | -3 |
| Other Comprehensive Income / (Loss) for the year | | – | – | -1 | – | – | -1 |
| Total Comprehensive Income Attributable to the Equity holders of the Parent | | – | -3 | -1 | – | – | -4 |
| As at 30 June 2013 | 9 | 533 | -420 | -1 | 1 | 5 | 118 |

## Tenon Limited

| | Note | Shares US$m | Retained Earnings US$m | Cash Flow Hedge Reserves US$m | Revaluation Reserve US$m | Net Currency Translation US$m | Total Group Equity and Reserves US$m |
|---|---|---|---|---|---|---|---|
| As at 1 July 2011 | | 533 | -509 | – | – | -48 | -24 |
| Net Profit / (Loss) after Taxation for the year | | – | -17 | – | – | – | -17 |
| Other Comprehensive Income for the year | | – | – | – | – | 13 | 13 |
| Total Comprehensive Income Attributable to the Equity holders of the Parent | | – | -17 | – | – | 13 | -4 |
| Share Buyback (1) | | – | – | – | – | – | – |
| As at 30 June 2012 | 9 | 533 | -526 | – | – | -35 | -28 |
| As at 1 July 2012 | | 533 | -526 | – | – | -35 | -28 |
| Net Profit / (Loss) after Taxation for the year | | – | -18 | – | – | – | -18 |
| Other Comprehensive Income / (Loss) for the year | | – | – | -1 | – | 3 | 2 |
| Total Comprehensive Income Attributable to the Equity holders of the Parent | | – | -18 | -1 | – | 3 | -16 |
| As at 30 June 2013 | 9 | 533 | -544 | -1 | – | -32 | -44 |

(1) On 14 November 2011, Tenon announced that it intended to make an offer to shareholders owning 10,000 or fewer Tenon shares, to buy back their shares, at 65 cents per share brokerage free, up to a maximum of 1,250,000 shares. The offer period closed on 28 December 2011 and 1,159,980 shares valued at NZ$753,987 were purchased and cancelled by Tenon on 30 December 2011.

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

Tenon Limited and Subsidiaries

# Consolidated Balance Sheet as at 30 June

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Note | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|---|
| | | **ASSETS** | | | |
| | | Current Assets: | | | |
| – | – | Inventory | 10 | **72** | 53 |
| – | – | Trade and Other Receivables | 11 | **34** | 31 |
| – | – | Assets Held for Sale | 15 | **–** | 3 |
| – | – | Total Current Assets | | **106** | 87 |
| | | Non Current Assets: | | | |
| – | – | Fixed Assets | 12 | **23** | 25 |
| – | – | Forest Assets | 13 | **4** | 3 |
| 262 | **262** | Investments | 14 | **–** | – |
| 1 | **1** | Intercompany Advances | 24 | **–** | – |
| – | – | Goodwill | 16 | **67** | 67 |
| – | – | Deferred Taxation Asset | 18 | **11** | 11 |
| 263 | **263** | Total Non Current Assets | | **105** | 106 |
| 263 | **263** | Total Group Assets | | **211** | 193 |
| | | **LIABILITIES AND GROUP EQUITY** | | | |
| | | **Liabilities** | | | |
| | | Current Liabilities: | | | |
| – | – | Bank Overdraft | | **2** | 1 |
| 1 | **1** | Trade and Other Payables and Provisions | 17 | **43** | 32 |
| – | **1** | Derivative Financial Instruments | 20 | **1** | – |
| – | – | Current Debt | 19 | **1** | 1 |
| 1 | **2** | Total Current Liabilities | | **47** | 34 |
| | | Non Current Liabilities: | | | |
| – | – | Non Current Debt | 19 | **46** | 37 |
| 290 | **305** | Intercompany Advances | 24 | **–** | – |
| 290 | **305** | Total Non Current Liabilities | | **46** | 37 |
| 291 | **307** | Total Group Liabilities | | **93** | 71 |
| | | **Group Equity** | | | |
| 533 | **533** | Capital | 8 | **533** | 533 |
| -561 | **-577** | Reserves | 9 | **-415** | -411 |
| -28 | **-44** | Total Group Equity | | **118** | 122 |
| 263 | **263** | Total Group Liabilities and Equity | | **211** | 193 |
| | | Net Assets per Share (US$) | | **1.80** | 1.86 |
| | | Net Tangible Assets per Share (US$) | | **0.61** | 0.67 |
| | | Shares used for Net Assets per Share (millions) | 8 | **65.7** | 65.7 |

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

For and on behalf of the Board
27 August 2013

Chairman of Directors
Luke Moriarty

Director (Chairman of Audit Committee)
Michael Walls

Chief Operating Officer
Anthony Johnston

Chief Financial Officer
Adam White

# Consolidated Statement of Cash Flows for year ended 30 June

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Note | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|---|
| | | Cash was Provided: | | | |
| | | From Operating Activities | | | |
| – | **–** | Receipts from Customers | | **360** | 327 |
| – | **–** | Total Provided | | **360** | 327 |
| – | **–** | Payments to Suppliers, Employees and Other | | **368** | 331 |
| – | **–** | Total Applied | | **368** | 331 |
| – | **–** | Net Cash to Operating Activities | | **-8** | -4 |
| | | To Investing Activities: | | | |
| – | **–** | Sale of Assets held for sale | 15 | **3** | – |
| | | Total Provided | | **3** | – |
| – | **–** | Purchase of Fixed Assets | 12 | **2** | 2 |
| – | **–** | Total Applied | | **2** | 2 |
| – | **–** | Net Cash from / (to) Investing Activities | | **1** | -2 |
| | | From Financing Activities: | | | |
| – | **–** | Debt Drawdowns | | **15** | 7 |
| 18 | **18** | Advances from Subsidiaries | | **–** | – |
| 18 | **18** | Total Provided | | **15** | 7 |
| – | **–** | Debt Settlements | | **6** | 1 |
| 17 | **18** | Interest and Refinancing Fees paid | | **3** | 2 |
| 1 | **–** | Share Buyback | | **–** | 1 |
| 18 | **18** | Total Applied | | **9** | 4 |
| – | **–** | Net Cash from Financing Activities | | **6** | 3 |
| – | **–** | Net Movement in Cash Held | | **-1** | -3 |
| – | **–** | Add Opening Cash, Liquid Deposits and Overdrafts | | **-1** | 2 |
| – | **–** | Closing Cash, Liquid Deposits and Overdrafts | | **-2** | -1 |

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

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

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | Cash was Provided from: | | |
| -17 | **-18** | Net Profit after Taxation | **-3** | -9 |
| 17 | **18** | Add Net Financing Expense | **4** | 3 |
| | | Adjustments: | | |
| – | **–** | Depreciation | **4** | 5 |
| – | **–** | Taxation | **–** | -2 |
| – | **–** | Other (2) | **-2** | 2 |
| – | **–** | Cash Flow from / (to) Operations before Net Working Capital Movements | **3** | -1 |
| – | **–** | Net Working Capital Movements | **-11** | -3 |
| – | **–** | Net Cash to Operating Activities (1) | **-8** | -4 |
| | | Net Working Capital Movements: | | |
| – | **–** | Trade and Other Receivables | **-4** | -7 |
| – | **–** | Inventory | **-19** | -1 |
| – | **–** | Trade and Other Payables | **12** | 5 |
| – | **–** | | **-11** | -3 |

(1) As per Statement of Cash Flows
(2) Restructuring costs paid and gain on sale of assets (June 2012: restructuring costs provided)

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 large home improvement chains in the United States, 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 global 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 2013 the Group was 58.99% owned by Rubicon Limited and its subsidiaries (June 2012: 58.99%).

These consolidated financial statements have been prepared on a consolidated Group basis and were approved for issue by the Board of Directors on 27 August 2013.

## 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 its 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 net 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 acquisition method.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 2.4 Changes in Accounting Policy and Disclosures

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

The Group adopted NZ IAS 1 Amendments, Presentation of Items of Other Comprehensive Income, on 1 July 2012. The amendment requires entities to separate items presented in other comprehensive income into two groups, based on whether they may be recycled to profit or loss in the future. This did not affect the measurement of any items recognised in the balance sheet or income statement in the current period.

*(b) Certain new standards, amendments and interpretations to existing standards have been published by the International Accounting Standards Board (IASB) and the External Reporting Board (XRB) that are mandatory for future periods and which the Group will adopt when they become mandatory. The Group has identified the following standards described below as relevant:*

- NZ IFRS 7 Financial Instruments: Amendments to NZ IFRS 7 Financial Instruments: Disclosures - Transition Disclosures (effective 1 January 2013). These amendments remove the requirement for the restatement of comparative period financial statements upon the initial application of the classification and measurement requirements of NZ IFRS 9. Instead, the amendments introduce additional disclosures on transition from the classification and measurement requirements of NZ IAS 39 Financial Instruments: Recognition and Measurement to those of NZ IFRS 9. The Group will adopt this standard from 1 July 2013.

- NZ IFRS 9 (2009) 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 impact on the Group is not expected to be significant. The Group has not yet decided when to adopt the new standard.

- NZ IFRS 9 (2010) Financial Instruments (effective 1 January 2015). NZ IFRS 9 (2010) supersedes NZ IFRS 9 (2009). The requirements for classifying and measuring financial liabilities were added to NZ IFRS 9 as issued in 2009. The existing NZ IAS 39 Financial Instruments: Recognition and Measurement requirements for the classification of financial liabilities and the ability to use the fair value option have been retained. However, where the fair value option is used for financial liabilities, the change in fair value is accounted for as follows:

    The change attributable to changes in credit risk are presented in other comprehensive income (OCI). The remaining change is presented in profit or loss.

  The impact on the Group is not expected to be significant and the Group has not yet decided when to adopt the new standard.

- NZ IFRS 10 Consolidated Financial Statements and NZ IFRS 12 Disclosure of Interests in Other Entities (effective 1 January 2013). NZ IFRS 10 replaces all of the guidance on control and consolidation in NZ IAS 27 Consolidated and Separate Financial Statements, and NZ IFRIC 12 Consolidation – Special Purpose Entities. The standard introduces a single definition of control that applies to all entities. NZ IFRS 12 sets out the required disclosures for entities reporting under the new standard, NZ IFRS 10. The Group does not expect the new standards to have a significant impact on the financial statements. The Group will adopt this standard from 1 July 2013.

- NZ IFRS 13 Fair Value Measurement (effective 1 January 2013). NZ IFRS 13 explains how to measure fair value and aims to enhance fair value disclosures. Application of the new standard will impact the type of information disclosed in the notes to the financial statements. The Group has not adopted the new standard before its operative date, which means that it would be first applied in the annual reporting period ending 30 June 2014. The Group expects there to be no material impact from the application of this standard. The Group will adopt this standard from 1 July 2013.

- Revised NZ IAS 27, effective from 1 January 2013, is renamed Separate Financial Statements and is now a standard dealing solely with separate financial statements. Application of this standard by the Group and Tenon Limited will not affect any of the amounts recognised in the financial statements, but may impact the type of information disclosed in relation to Tenon Limited's investments disclosure in Tenon Limited's financial statements. The Group will adopt this standard from 1 July 2013.

- 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 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 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.

*(b) Goodwill*

All business combinations are accounted for by applying the acquisition 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 and is tested regularly for impairment including 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 of monetary items are recognised in the income statement.

## 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 cash flows 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*

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.

*(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. The assets are 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 cash flow models where the fair value is calculated using cash flows based on sustainable forest management plans. The fair value is measured as the present value of cash flows from one growth cycle on leased forest land, taking into consideration environmental, operational and market restrictions.

*(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 and then to reduce the carrying amount of other assets in the cash-generating unit on a pro rata basis.

The recoverable amount of non-financial assets is the greater of their fair value less costs to sell and value-in-use. In assessing value-in-use, the estimated future pre-tax 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. 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 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

*(h) 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.

### 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) 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. 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.

*(e) 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.

## 2 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

*(f) 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 "financing 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 large home improvement chains in the United States. 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) 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.

*(d) 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, leased under a finance lease, is accounted for in accordance with the accounting policy applicable to that asset.

*(e) 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 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 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (continued)

### 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.

## 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

## 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.

## 4 RISK MANAGEMENT (continued)

### 4.2 Key Financial Risks continued

*(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 Operating Profit before Financing Costs and Equity by approximately $0.6 million per annum assuming the Taupo sawmill is operating at full capacity. Full capacity for the Taupo sawmill is equivalent to processing approximately 400,000 tonnes of logs per annum on a 4 shift basis. Currently the Taupo sawmill is operating at approximately 3/4 of full capacity. The average Moulding & Better 5/4 lumber price, per Crow's, in the 2013 fiscal year was approximately $1,309 per thousand board feet (2012: $1,219 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.

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 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 Operating Profit before Financing Costs and Equity 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 1 year 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 2013 and 30 June 2012 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.

## 4 RISK MANAGEMENT (continued)

### 4.2 Key Financial Risks continued

*(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 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 19% of the Group's 2013 costs and approximately 7% of the Group's 2013 revenues are incurred in New Zealand dollars, and approximately 1% of the Group's 2013 costs and 1% of the Group's 2013 revenues are incurred in Australian 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's 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 Operating Profit before Financing Costs and Equity 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 cash flows, 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.

*(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.

## 4 RISK MANAGEMENT (continued)

### 4.2 Key Financial Risks continued

*(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 30% of trade receivables as at 30 June 2013 (excluding national retail accounts), thereby reducing the Group's credit risk exposure. The total amount of policy cover is approximately $6 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 US. 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 long-term debt financing facility was established, replacing the Group's previous syndicated facility. The facility is a syndicated facility structured on a group basis with JPMorgan Chase Bank, N.A. ("JPMorgan Chase") as Agent. The term of the facility is for 5 years. The facility is a secured $50 million revolver facility and an amortising term loan of $4.5 million as at 30 June 2013. The term loan was initially for $7.6 million in June 2011, however $2.1 million was attached to the Canadian manufacturing operations and was repaid during the current year and $1 million has been repaid through scheduled monthly payments since July 2011.

The 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)).

The Group's banking facility requires a minimum "availability" Borrowing Base of $7.5 million. At 30 June 2013, the amount of availability was $17.5 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. 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 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, has continued under the current bank facility.

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

## 4 RISK MANAGEMENT (continued)

### 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. The Group has been materially adversely impacted by the prolonged economic downturn in this key market that prevailed from 2007 to 2012.

Negative factors that affected the housing sector in North America over this period were tight credit market conditions, falling house prices, higher levels of housing inventory and reduced mortgage availability. These each had a material negative effect on the total consumption of building products, and therefore the Group's level of revenue, earnings and cash flow over this period. These conditions have since improved, with 2013 recording a noticeable increase in new house construction activity, house prices and housing turnover.

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. Revenues of approximately $149 million (June 2012: $153 million) are derived from a single external customer. These revenues are attributable to the North American geographic segment.

*(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 RISK MANAGEMENT (continued)

### 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.

### 4.5 Capital Management

The Board's objectives when managing capital are to maximise the return for the Company's shareholders and to safeguard the Group's ability to continue as a going concern.

In order to maintain, improve or optimise the capital structure of the Group, Tenon may pay dividends, return capital, issue new shares or sell assets to reduce debt, subject to the terms of the Group's syndicated debt facility.

### 4.6 Fair Value Estimation

Financial instruments are recorded in the balance sheet at an estimated fair value. In the June 2013 and June 2012 years, foreign exchange contracts, interest rate swaps and the electricity commodity contract for difference are treated as effective hedges under NZ IAS 39 (refer to note 2.8 Valuation of Liabilities, Significant Accounting Policies). The fair value of financial instruments traded in active markets is based on quoted market prices at balance sheet date. The quoted market price used for financial assets held by the Group is the current bid price. The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. Externally sourced valuations are used to value interest rate swaps and foreign exchange contracts held at balance date. The carrying value less impairment provision of trade receivables and payables are assumed to approximate their fair values. The carrying amount of cash and liquid deposits and bank overdrafts is equivalent to the fair value. Long-term financial liabilities and other receivables are held at amortised cost. It is not practicable to estimate fair values of unlisted investments in Subsidiaries as there are no quoted market prices for those or similar investments. The carrying value of forest assets is equivalent to their fair value less estimated costs to sell. The Group has no unlisted investments in other companies.

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **5 OPERATING EARNINGS** | | |
| | | Operating Earnings includes: | | |
| – | **–** | Depreciation - Plant, Equipment and Buildings | | |
| – | **–** | Cost of Sales Expense | **3** | 4 |
| – | **–** | Selling and Distribution Expense | **1** | 1 |
| – | **–** | | **4** | 5 |
| – | **–** | Employee Benefit Costs | **56** | 55 |
| | | Restructuring Costs | | |
| – | **–** | – Employee Costs (3) | **–** | 2 |
| – | **–** | – Asset relocation costs (3) | **–** | 1 |

Other items in Operating Earnings were:
(1) Directors fees payable were $0.4 million for the current year (June 2012: $0.4 million) (refer Key Management Compensation note 24 (b))
(2) Payments made and accrued to PricewaterhouseCoopers were:
Statutory Audit $0.5 million for the current year (June 2012: $0.6 million)
Additional audit related work was $0.1 million for the current year (June 2012:$0.1 million)
(3) Restructuring costs in the year to June 2012 related to the Company's manufacturing activities in Canada and Taupo and the closure of the US Support office in Annapolis

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **6 INCOME TAX EXPENSE** | | |
| | | Current Taxation: | | |
| – | **–** | United States | **–** | -2 |
| – | **–** | Total Current Taxation | **–** | -2 |
| – | **–** | Taxation Expense / (Benefit) | **–** | -2 |
| | | Net Profit / (Loss) before Taxation | | |
| -17 | **-18** | New Zealand and Australia | **-2** | -4 |
| – | **–** | United States | **-1** | -7 |
| -17 | **-18** | | **-3** | -11 |
| -5 | **-5** | Taxation at 28 cents per dollar | **-1** | -3 |
| | | Adjusted for: | | |
| – | **–** | Expenses / (Income) not included in assessable income | **1** | 1 |
| 5 | **5** | Valuation allowance | **–** | – |
| – | **–** | Taxation Expense / (Benefit) | **–** | -2 |

**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 2013 were nil (June 2012: nil).

| | Tenon Group 2013 | Tenon Group 2012 |
|---|---|---|
| **7 NET EARNINGS PER SHARE** | | |
| Basic and Diluted Net Earnings per Share (cents) | **-4.8** | -13.9 |
| Numerator for Basic and Diluted Net Earnings per Tenon Share ($ millions) | **-3** | -9 |
| Denominator for Basic and Diluted Net Earnings per Tenon Share (millions), refer to note 8. | **65.7** | 66.3 |

| | Tenon Group and Tenon Limited 2013 US$ | Tenon Group and Tenon Limited 2012 US$ |
|---|---|---|
| **8 CAPITAL** | | |
| **Capital** | | |
| **Reported Capital:** | | |
| Reported Capital at the beginning of the year | **532,947,659** | 533,573,563 |
| Share Buyback (1) | – | -625,904 |
| Reported Capital at the end of the year | **532,947,659** | 532,947,659 |

| | Tenon Group and Tenon Limited 2013 | Tenon Group and Tenon Limited 2012 |
|---|---|---|
| **Tenon Ordinary Shares (1) (2)** | | |
| Number of Shares at the beginning of the year | **65,690,681** | 66,850,661 |
| Share Buy Back (1) | – | -1,159,980 |
| Number of Shares at the end of the year | **65,690,681** | 65,690,681 |

(1) On 14 November 2011, Tenon announced that it intended to make an offer to shareholders owning 10,000 or fewer Tenon shares, to buy back their shares, at 65 cents per share brokerage free, up to a maximum of 1,250,000 shares. The offer period closed on 28 December 2011 and 1,159,980 shares valued at NZ$753,987 were purchased and cancelled by Tenon on 30 December 2011.

(2) Includes 182,548 (June 2012: 182,548) fully paid Tenon Limited Ordinary Shares held by the Tenon Employee Share Purchase Scheme, accounted for as treasury stock.

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **9 RESERVES** | | |
| | | **Retained Earnings** | | |
| -509 | **-526** | Opening Balance | **-417** | -408 |
| -17 | **-18** | Net Profit / (Loss) after Taxation | **-3** | -9 |
| -526 | **-544** | | **-420** | -417 |
| | | **Cash Flow Hedging Reserve (1)** | | |
| – | **–** | Opening Balance | **–** | – |
| – | **-1** | Fair Value losses for the year | **-1** | – |
| – | **–** | Hedge gains transferred to Earnings in the year | **–** | – |
| – | **-1** | | **-1** | – |
| | | **Revaluation Reserve** | | |
| – | **–** | Opening Balance | **1** | 1 |
| – | **–** | | **1** | 1 |
| | | **Net Currency Translation (2)** | | |
| -48 | **-35** | Opening Balance | **5** | 6 |
| 13 | **3** | Net variations on Translation of Foreign Currency Financial Statements | **–** | -1 |
| -35 | **-32** | | **5** | 5 |
| -561 | **-577** | Total Reserves | **-415** | -411 |

(1) The Hedging reserve records the net movement of cash flow hedging instruments, comprising of foreign exchange contracts, an electricity hedge contract at the Group's Taupo operation and interest rate swaps.

(2) The Tenon Limited currency translation movement of $3 million in the June 2013 year (June 2012: $13 million) arises on the translation of inter-company New Zealand dollar advances at balance date. These advances are eliminated on consolidation of the Tenon Group. Under IFRS, investments in subsidiaries, which are also eliminated on consolidation, are held at cost and are not revalued to reflect exchange rate translation movements. Tenon Limited equity is positive when calculated in New Zealand dollars.

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **10 INVENTORY** | | |
| – | **–** | Raw Materials and Work in Progress | **6** | 6 |
| – | **–** | Finished Goods | **66** | 47 |
| – | **–** | | **72** | 53 |

The cost of inventory recognised as an expense and included in cost of sales amounted to $280 million (June 2012: $254 million).

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **11 TRADE AND OTHER RECEIVABLES** | | |
| – | – | Trade Debtors [1] | **29** | 26 |
| – | – | Prepayments | **3** | 3 |
| – | – | Other Receivables | **2** | 2 |
| – | – | | **34** | 31 |

(1) 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).

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **12 FIXED ASSETS** | | |
| | | Cost | | |
| – | – | Land and Improvements | **6** | 6 |
| – | – | Buildings | **17** | 17 |
| – | – | Plant and Equipment | **77** | 76 |
| – | – | Total Cost | **100** | 99 |
| | | Accumulated Depreciation | | |
| – | – | Buildings | **-8** | -7 |
| – | – | Plant and Equipment | **-69** | -67 |
| – | – | Total Accumulated Depreciation | **-77** | -74 |
| – | – | Total Fixed Assets at Net Book Value | **23** | 25 |
| | | Domicile of Fixed Assets | | |
| – | – | New Zealand | **12** | 14 |
| – | – | United States | **11** | 11 |
| – | – | Total Fixed Assets at Net Book Value | **23** | 25 |

| | Land & Improvements US$m | Buildings US$m | Plant & Equipment US$m | Total US$m |
|---|---|---|---|---|
| Net Book Value 1 July 2011 | 6 | 12 | 11 | 29 |
| Additions | – | – | 2 | 2 |
| Transfer from / to assets held for sale [1] | – | -1 | – | -1 |
| Depreciation Charge | – | -1 | -4 | -5 |
| Net Book Value 30 June 2012 | 6 | 10 | 9 | 25 |
| Additions | – | – | 2 | 2 |
| Depreciation Charge | – | -1 | -3 | -4 |
| Net Book Value 30 June 2013 | 6 | 9 | 8 | 23 |

(1) Refer to note 15.

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **13 FOREST ASSETS** | | |
| – | **–** | Opening Balance | **3** | 3 |
| – | **–** | Current year movement (1) | **1** | – |
| – | **–** | Closing Balance | **4** | 3 |

(1) The current year movement of the forests assets is made up of several small items: fair value expensed on sale of forests of $0.3 million (included in Cost of Sales in the Consolidated Income Statement), costs associated with maintaining the forests of $0.2 million and a fair value uplift due to improved log prices and reduced estimated costs of harvest of $0.3 million (included in Cost of Sales in the Consolidated Income Statement).

The Group has an interest in a forest asset growing on leased forest land (June 2013: 359 stocked area hectares, June 2012: 354.1 hectares) and the forestry rights to several forest assets growing on other forest land (June 2013: 57.6 stocked area hectares, June 2012: 76.1 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 are valued under NZ IAS 41 "Biological Assets" and presented in the accounts as forest assets.

During the year the harvesting of some of the Group's forests began and harvesting is expected to continue in the next financial year. Revenues of $1 million were recorded representing 17.5 ha of forest harvested. The realised gain on this harvesting was $0.3 million, over and above the $0.3 million of the fair value of the crop harvested, and is included in the gross profit for June 2013.

**Valuation**

The carrying value of the forest assets in these Financial Statements is their fair value of $3.6 million (June 2012: $3.4 million). This is derived from a current, independent forest valuation, as at 30 June 2013. The independent valuation assumes; a post-tax cash flow, a historical 12 quarter average pricing series to March 2013, 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. Harvesting of the first stand began in 2013. 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 cash flows generated from the forest assets. On current discount rate, taxation and cash flow assumptions, the Company expects that the discounted net cash flows from the forest assets will exceed the 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 2013 by $0.3 million (June 2012: $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 2013 by $0.2 million (June 2012: $0.2 million).

**Risk**

As the Group operates a sawmill in Taupo, New Zealand, that processes logs (total cost of logs processed by the sawmill in the June 2013 year was $44 million (June 2012: $41 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 profitability of the Taupo sawmill due to the change in the cost of raw materials used by the mill.

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **14 INVESTMENTS** | | |
| 262 | **262** | Investment in Subsidiary Companies (refer to notes 24 and 27) | **–** | – |
| 262 | **262** | | **–** | – |

## 15 ASSETS HELD FOR SALE

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| – | **–** | Opening Balance | **3** | 2 |
| – | **–** | Proceeds from sale of Canadian facility (1) | **-3** | – |
| – | **–** | Transfer from fixed assets (1) | **–** | 3 |
| – | **–** | Transfer to fixed assets (2) | **–** | -2 |
| – | **–** | Closing Balance | **–** | 3 |

(1) In 2012, it was announced that the manufacturing operations in Canada would be relocated and integrated into the existing Group facilities in the USA. The manufacturing facility owned in Canada was surplus to requirements and was classified as an asset held for sale as at 30 June 2012. The facility was sold in August 2012.

(2) The company owns approximately 12.5 hectares of bare land adjacent to the Taupo manufacturing site which had been classed as held for sale in previous years. In 2012 the land was reclassified as a fixed asset at the lower of the original cost and fair value ($1.5 million).

## 16 GOODWILL

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| – | **–** | Goodwill at beginning of the year | **67** | 67 |
| – | **–** | Balance at end of year | **67** | 67 |

Tenon has allocated goodwill to one Cash Generating Unit ("CGU") being, Tenon's 100% ownership interests in its North American manufacturing and distribution activities comprising The Empire Company, Southwest Moulding Co., and the Ornamental group of companies.

All businesses operate within Tenon's primary business segment being the North American geographic market.

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 cash flows assume the recovery in market conditions experienced in 2013 continues going forward, such that by year 5 of the projections (fiscal year 2018) (i.e. the terminal year) Tenon's consolidated EBITDA is projected to be $44 million (June 2012 Annual Report estimate: $30 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 longer term annual sales growth rates of between 5% and 10% (June 2012: 5% to 7%) are assumed for the following 5 years, consistent with assuming long term growth in the new homes and remodelling markets gradually moving up from the bottom of the economic cycle and growth in market share from new products.

(2) Gross margin percentages were assumed to be similar to the current year's percentage for the next 5 years (i.e. +/- 2%), (June 2012: +/- 2%).

(3) The discount rate applied to the cash flow projections was 8.25% real, pre tax (2012: 8.25%), which reflects Tenon's weighted average cost of capital (WACC).

(4) The terminal value growth rate used in the value-in-use calculation was 1% (June 2012: 1%) consistent with assuming a long term annual growth rate in the new homes and remodelling markets beyond year 5 of the projections.

As the value in use significantly exceeded the carrying value plus allocated goodwill of the CGUs, no impairment existed at 30 June 2013.

## 16 GOODWILL continued

### Sensitivities

Sensitivity analysis was applied to determine whether under realistic scenarios there may be an impairment in goodwill. Even after applying these sensitivities, the value-in-use calculations 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 doubled or
- the compound annual sales growth rate assumption was halved or
- the gross margin was held constant at current levels or
- the terminal value growth rate was nil

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **17 TRADE AND OTHER PAYABLES AND PROVISIONS** | | |
| – | **–** | Trade Creditors | **31** | 19 |
| – | **–** | Accrued Employee Benefits | **4** | 4 |
| 1 | **1** | Other Payables | **3** | 3 |
| – | **–** | Accruals | **5** | 4 |
| – | **–** | Restructuring Provision (1) | **–** | 2 |
| 1 | **1** | | **43** | 32 |
| | | Restructuring Provision (1) | | |
| – | **–** | Opening balance | **2** | – |
| – | **–** | Created through earnings | **–** | 2 |
| – | **–** | Paid during the year | **-2** | – |
| – | **–** | Closing Balance | **–** | 2 |

(1) Restructuring provision for the closure of manufacturing operations in Canada.

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **18 PROVISION FOR CURRENT TAXATION AND DEFERRED TAXATION** | | |
| | | Provision for Current Taxation: | | |
| – | **–** | Opening Provision for Current Taxation | **–** | – |
| – | **–** | Current Taxation (Expense) / Benefit in the Consolidated Income Statement | **–** | 2 |
| – | **–** | Deferred Tax Movement during the year | **–** | -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:

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| – | **–** | Deferred Tax on Assets | **10** | 10 |
| – | **–** | Deferred Tax on Liabilities | **1** | 1 |
| – | **–** | Deferred Tax Asset | **11** | 11 |
| | | The gross movement on the deferred income tax account is as follows: | | |
| | | Non Current Deferred Taxation: | | |
| – | **–** | Opening Deferred Taxation | **11** | 9 |
| – | **–** | Deferred Tax Movement during the year | **–** | 2 |
| – | **–** | Deferred Tax Asset | **11** | 11 |

| | Depreciation US$m | Forestry US$m | Provisions US$m | Tax Losses [1] US$m | Current Assets US$m | Total US$m |
|---|---|---|---|---|---|---|
| **June 2012** | | | | | | |
| Opening Provision for Deferred Taxation | -2 | -1 | – | 13 | -1 | 9 |
| Deferred Taxation in the Income Statement | -1 | – | 1 | 1 | 1 | 2 |
| Closing Provision for Deferred Taxation | -3 | -1 | 1 | 14 | – | 11 |
| **June 2013** | | | | | | |
| Opening Provision for Deferred Taxation | -3 | -1 | 1 | 14 | – | 11 |
| Deferred Taxation in the Income Statement | – | – | – | 1 | -1 | – |
| Closing Provision for Deferred Taxation | -3 | -1 | 1 | 15 | -1 | 11 |

(1) Recognised tax losses include $6.8 million of tax effected NZ tax losses (June 2012: $6.6 million), that do not expire, subject to shareholder continuity provisions, and $7.7 million (June 2012: $7.7 million) of US tax losses which have an expiry date as detailed below.

| | | Expiry Dates | |
|---|---|---|---|
| | Total | 2014 | 2021 and beyond |
| **US Tax Losses** | US$m | US$m | US$m |
| Gross Value | 22.7 | 1.7 | 21.0 |
| Tax Effected | 7.7 | 0.6 | 7.1 |

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 $24 million in unrecognised NZ tax losses (gross value), and no unrecognised US tax losses (June 2012: $25 million NZ losses and no unrecognised US tax losses).

| Tenon Limited 2012 US$m | Tenon Limited 2013 US$m | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|---|
| | | **19 FINANCIAL COSTS AND DEBT** | | |
| | | **Financing Costs** | | |
| – | **–** | Interest payable on Debt | **2** | 2 |
| – | **–** | Interest payable on Supply Chain Financing | **1** | 1 |
| – | **–** | Amortisation of Refinancing Fees (1) | **1** | – |
| 17 | **18** | Interest payable on Intercompany Advances (refer to note 24) | **–** | – |
| 17 | **18** | Net Financing Expense | **4** | 3 |
| | | **Non Current Debt** | | |
| – | **–** | Loans (2) | **46** | 37 |
| – | **–** | | **46** | 37 |
| | | **Current Debt** | | |
| – | **–** | Loans (2) (6) | **1** | 1 |
| – | **–** | | **1** | 1 |
| – | **–** | Total Debt (5) | **47** | 38 |
| | | **Summary of Repayment Terms (4)** | | |
| | | Due for Repayment: | | |
| – | **–** | Less than one year (6) | **1** | 1 |
| – | **–** | between one and two years | **1** | 2 |
| – | **–** | between two and three years | **45** | 2 |
| – | **–** | between three and four years | **–** | 33 |
| – | **–** | **Total Debt** | **47** | 38 |
| | | **Non Current Debt** | | |
| **%** | **%** | Summary of Interest Rates by Repayment Period (%) (7) | **%** | **%** |
| | | Due for Repayment: | | |
| – | **–** | between one and two years | **4.85** | 4.81 |
| – | **–** | between two and three years | **5.14** | 4.81 |
| – | **–** | between three and four years | **–** | 4.98 |
| – | **–** | **Weighted Average Interest Rate** | **5.13** | 4.97 |
| | | **Weighted Average Interest Rate comprises:** | | |
| – | **–** | Weighted average interest rate on debt | **4.03** | 3.65 |
| – | **–** | Facility fees amortisation % on debt | **1.10** | 1.32 |
| – | **–** | **Weighted Average Interest Rate** | **5.13** | 4.97 |
| | | **Current Debt** | | |
| | | Summary of Interest Rates by Repayment Period (%) (7) | | |
| | | Due for Repayment: | | |
| – | **–** | Less than one year | **4.82** | 4.80 |
| – | **–** | **Weighted Average Interest Rate** | **4.82** | 4.80 |
| | | **Weighted Average Interest Rate comprises:** | | |
| – | **–** | Weighted average interest rate on debt | **3.89** | 3.63 |
| – | **–** | Facility fees amortisation % on debt | **0.93** | 1.17 |
| – | **–** | **Weighted Average Interest Rate** | **4.82** | 4.80 |

## 19 FINANCIAL COSTS AND DEBT continued

(1) Includes the amortisation of unamortised refinancing fees of $0.3 million (June 2012: $0.3 million) and the costs related to refinancing activities of $0.4 million (June 2012: nil).

(2) Tenon has a bank credit facility provided by a consortium of banks led by JPMorgan 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 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 2013 and 30 June 2012, the Company was in compliance with the Borrowing Base Covenant, accordingly the amount of debt drawn under the revolver facility as at 30 June 2013 and 30 June 2012 is aged non-current.

(3) Proceeds from the sale of the manufacturing facility in Canada were used to repay $2.1 million of the Term Loan in September 2012.

(4) The total size of Tenon's 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 is that, commencing in September 2014, the maximum $1 million repayment will be made under the excess cash flow provision of the facility.

| | | $m | |
|---|---|---|---|
| | **Term** | **Revolver** | **Total** |
| June 2013 | 4.51 | 50.00 | 54.51 |
| June 2014[a] | 4.08 | 50.00 | 54.08 |
| June 2015[b] | 2.65 | 50.00 | 52.65 |
| June 2016 | – | – | – |

(a) Scheduled Term Loan amortisation of $36,000 per month

(b) Scheduled Term Loan amortisation of $36,000 per month and $1 million excess cash flow payment on 30 September.

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

(6) The current debt of $1 million reflects term loan amortisation of $0.4 million (June 2012: $0.6 million) and finance lease payments of $0.1 million (June 2012: $0.1 million).

(7) The weighted average interest rates reflect the effective interest rate, inclusive of fee amortisations and any applicable interest rate swaps. The Group's two interest rate swaps, entered into in July 2011, hedge the LIBOR contracts and the swap interest cost has been included in calculating the interest rate on the LIBOR loans, due for repayment in 2016. 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)).

## 20 FINANCIAL INSTRUMENTS continued

*Exposure to Currency Risk*

The functional currency of the Group is the United States dollar. The risks 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 2013 | | As at 30 June 2012 | |
| | USD US$m | NZD/AUD US$m | USD US$m | NZD/AUD US$m |
| Cash and Liquid Deposits | **–** | **–** | – | – |
| Trade Debtors | **27** | **2** | 23 | 3 |
| Bank Overdraft | **-1** | **-1** | – | -1 |
| Trade Creditors | **-27** | **-4** | -15 | -4 |
| Current Debt | **-1** | **–** | -1 | – |
| Non Current Debt | **-46** | **–** | -37 | – |
| **Gross Balance Sheet Exposure** | | **-3** | | -2 |

*Sensitivity Analysis - Group gross balance sheet exposure*

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)).

**Tenon Limited**

| | Currency of Denomination | | | |
|---|---|---|---|---|
| | As at 30 June 2013 | | As at 30 June 2012 | |
| | USD US$m | NZD US$m | USD US$m | NZD US$m |
| Intercompany Advance - Asset | **–** | **1** | – | 1 |
| Intercompany Advance - Liability | **–** | **-305** | – | -290 |
| **Gross Balance Sheet Exposure** | | **-304** | | -289 |

*Sensitivity Analysis - Tenon Limited gross balance sheet exposure*

The Intercompany advances are denominated in New Zealand dollars. A 1 cent change in the NZ / US dollar exchange rate will change the currency translation reserve in Tenon Limited Equity by $4 million (June 2012: $4 million) when reported in United States dollars (the presentation currency).

| **Tenon Limited and the Group Financial Instruments** | As at 30 June 2013 Selling USD | As at 30 June 2013 Buying NZD | As at 30 June 2012 Selling USD | As at 30 June 2012 Buying NZD |
|---|---|---|---|---|
| Foreign Exchange Contracts | **21** | **26** | 2 | 3 |

*Sensitivity Analysis - Financial Instruments*

As at 30 June 2013, Tenon Limited had foreign exchange contracts selling US$21 million into NZ$26 million at an average rate of 0.7935. All the contracts are due for settlement within the 6 months to 31 December 2013. As at 30 June 2012, Tenon Limited had foreign exchange contracts selling US$2 million into NZ$3 million at an average rate of 0.7511. All the contracts were due for settlement in July 2012.

As at 30 June 2013, the mark to market valuation adjustment on the contracts was a loss of $0.6 million (June 2012: gain of $0.1 million) and was included in the Cash Flow Hedging Reserve in Tenon Limited and Group Equity. If the NZ/US Dollar exchange rate changes by 1c before the contracts are settled, the mark to market valuation adjustment in Equity would change by $0.3 million (June 2012: less than $0.1 million).

| The following exchange rates applied during the year: | Average rate (1) 2013 | Average rate (1) 2012 | Reporting date (spot rate) 2013 | Reporting date (spot rate) 2012 |
|---|---|---|---|---|
| USD/NZD | 0.8168 | 0.8069 | 0.7790 | 0.7851 |

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

## 20 FINANCIAL INSTRUMENTS continued

*Exposure to Interest Rate Risk*

The Group's interest rate policy is for interest to be a mix 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 2013, the Group had two interest rate swaps totalling $15 million, covering 32% of total Debt (as at 30 June 2012 there were two interest rate swaps of $15 million, or 39% of total Debt). The two current period swaps are for $7.5 million each and were entered into in July 2011. They have a 4 year duration and expire in July 2015. The Group pays a fixed interest rate of 1.575% on one swap and 1.53% on the other. For both swaps the Group receives a rate based on the USD LIBOR floating rate. The rate receivable as at 30 June 2013 was 0.195% (June 2012: 0.2428%) on one swap and 0.1925% (June 2012: 0.2398%) on the other. The swap interest cost has been included in calculating the interest rate on the LIBOR loans, due for repayment in 2016.

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. The interest rate swaps were 100% effective as at 30 June 2013 and June 2012 and the net fair value of the interest rate swaps as at 30 June 2013 was a liability of $0.4 million (June 2012: liability of $0.5 million) and is included in other current liabilities and the hedging reserve in Equity.

The following table sets out the weighted average interest rate of borrowings and interest rate hedges:

| | | Tenon Group | | | |
|---|---|---|---|---|---|
| | | **2013 US$m** | **2013 %** | **2012 US$m** | **2012 %** |
| Interest Rates Repriced: | | | | | |
| (including average interest rate) | | | | | |
| Debt repayable | within one year | **1** | **4.82** | 1 | 4.80 |
| | between one and two years | **1** | **4.85** | 2 | 4.81 |
| | between two and three years | **45** | **5.14** | 2 | 4.81 |
| | between three and four years | **–** | **–** | 33 | 4.98 |
| | | **47** | | 38 | |

Intercompany interest on Tenon Limited intercompany advance liability is an average weighted rate based upon the 1 year NZ swap Rate (refer to note 24 (a)(3)).

*Sensitivity Analysis - Group*

As at 30 June 2013, a 1% increase in the floating interest rates of the debt outstanding at balance date would have resulted in an estimated $0.3 million reduction in Profit before Taxation, a 1% decrease in the floating interest rate would have resulted in an estimated increase of $0.4 million in Profit before Taxation. The 2013 earnings impact was calculated on the actual debt drawn as at 30 June 2013 and was for a full 12 months assuming that 32% of debt was subject to the two interest rate swaps in existence as at 30 June 2013 and the swaps were for the whole year and taken out at the beginning of the year. As effective hedges, the changes in fair value of the swaps are included in Equity. The supply chain financing interest cost is also based on LIBOR rates and therefore sensitive to interest rate changes. As at 30 June 2013, 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 ($16.7 million as at 30 June 2013) would have had an estimated $0.2 million impact on Profit before Taxation.

A 1% increase in interest rates would have had no impact on Equity, the reduction in the fair value liability of the interest rate swaps offsetting the after tax increase in total interest costs. A 1% reduction in interest rates would have increased Equity by $0.1 million, being the after tax reduction in total interest costs partially offset by an increase in the fair value liability of the interest rate swaps.

As at 30 June 2012, 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 2012 earnings impact was calculated on the actual debt drawn as at 30 June 2012 and was for a full 12 months assuming that 39% of debt was subject to the two interest rate swaps in existence as at 30 June 2012 and the swaps were for the whole year and taken out at the beginning of the year. As effective hedges, the changes in fair value of the swaps were included in Equity. The supply chain financing interest cost was also based on LIBOR rates and therefore sensitive to interest rate changes. As at 30 June 2012, 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 ($16 million as at 30 June 2012) would have had an estimated $0.2 million impact on Profit before Taxation.

A 1% increase in interest rates would have increased Equity by $0.2 million, being the reduction in the fair value liability of the interest rate swaps partially offset by the after tax increase in total interest costs. A 1% reduction in interest rates would have increased Equity by $0.1 million, being the after tax reduction in total interest costs partially offset by an increase in the fair value liability of the interest rate swaps.

## 20 FINANCIAL INSTRUMENTS continued

*Sensitivity Analysis - Tenon Limited*

As at 30 June 2013, a 1% change in the 1 year NZ swap rate would have resulted in an estimated $3.1 million change in Profit before Taxation and Tenon Limited Equity (June 2012: $2.9 million).

**(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 | |
|---|---|---|
| | **2013 US$m** | **2012 US$m** |
| Cash and Liquid Deposits (1) | **–** | – |
| Trade and Other Receivables | **34** | 31 |
| | **34** | 31 |
| The status of Trade Debtors is as follows: | | |
| Neither past due nor impaired (2) | **25** | 23 |
| Past due but not impaired (3) | **4** | 3 |
| Impaired (4) | **–** | – |
| | **29** | 26 |
| Less provision for doubtful debts (5) | **–** | – |
| Net Trade Debtors | **29** | 26 |

(1) Cash and Liquid Deposits are only held with banks that are part of the Group's banking consortium led by JPMorgan 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 $25 million (June 2012: $23 million) of "neither past due nor impaired" debtors will not be collected, taking into account the payment history of the Group's 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 2013, $4 million (June 2012: $3 million) of Trade Debtors were past due but not impaired. The ageing of these Trade Debtors is as follows:

| | Tenon Group | |
|---|---|---|
| | **2013 US$m** | **2012 US$m** |
| Days overdue: | | |
| 1 month | **4** | 3 |
| | **4** | 3 |

(4) As at 30 June 2013, $0.1 million (June 2012: $0.1 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 $0.1 million (June 2012: $0.1 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 2013, the net provision created through earnings during the period was $0.1 million (In June 2012, the net provision created through earnings during the period was $0.1 million). Debtors written off directly against the provision during 2013 were $0.1 million (June 2012: $0.3 million).

## 20 FINANCIAL INSTRUMENTS continued

### (c) Liquidity Risk

The following are contractual maturities of financial liabilities and net settled derivatives. The amounts disclosed are the contractual undiscounted cash flows.

| Tenon Group | | | | 2013 $m | | | |
|---|---|---|---|---|---|---|---|
| | Carrying value | Fair value | 6 months or less | 6-12 months | 1-2 years | 2-5 years | Over 5 years |
| **Non Derivative Financial Liabilities** | | | | | | | |
| Bank Overdraft | 2 | 2 | 2 | – | – | – | – |
| Trade and Other Payables | 43 | 43 | 41 | 2 | – | – | – |
| Debt | 47 | 47 | – | 1 | 1 | 45 | – |
| Interest Expense on Debt | – | – | 1 | 1 | 2 | 2 | – |
| **Derivative Financial Liabilities** | | | | | | | |
| Interest rate swaps ($0.2 million per annum for 2 years) | – | – | – | – | – | – | – |
| Forward Exchange Contracts | 1 | 1 | 1 | – | – | – | – |
| | 93 | 93 | 45 | 4 | 3 | 47 | – |

| Tenon Group | | | | 2012 $m | | | |
|---|---|---|---|---|---|---|---|
| | Carrying value | Fair value | 6 months or less | 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 | 31 | 31 | 30 | 1 | – | – | – |
| Debt | 38 | 38 | – | 1 | 2 | 35 | – |
| Interest Expense on Debt | – | – | – | 1 | 2 | 3 | – |
| **Derivative Financial Liabilities** | | | | | | | |
| Interest rate swaps ($0.2 million per annum for 3 years) | 1 | 1 | – | – | – | – | – |
| | 71 | 71 | 31 | 3 | 4 | 38 | – |

*Interest Rate Swap cash flows*

As at 30 June 2013 the future gross cash flows of the interest rate swaps (refer to note 20 (a) market risk, exposure to interest rate risk) are a $0.5 million cash outflow (being fixed interest paid). The swaps are settled on a net basis monthly. Of the net cash outflow (based on the prevailing floating interest rates as at 30 June 2013) of $0.4 million, $0.1 million is expected to occur in the 6 months to December 2013 and $0.1 million in the six months to June 2014. $0.2 million is expected to occur in the 2015 year.

As at 30 June 2012 the future gross cash flows of the interest rate swaps (refer to note 20 (a) market risk, exposure to interest rate risk) were a $0.7 million cash outflow (being fixed interest paid). The swaps were settled on a net basis monthly. Of the net cash outflow (based on the prevailing floating interest rates as at 30 June 2012) of $0.6 million, $0.1 million was expected to occur in the 6 months to December 2012 and $0.1 million in the six months to June 2013. $0.2 million was expected to occur in the 2014 and 2015 years.

## 20 FINANCIAL INSTRUMENTS continued

**Tenon Limited**

| | Carrying value | Fair value | 6 months or less | 2013 $m 6-12 months | 1-2 years | 2-5 years | Over 5 years (1) |
|---|---|---|---|---|---|---|---|
| **Non Derivative Financial Liabilities** | | | | | | | |
| Intercompany Advance Liability | 305 | 305 | – | – | – | – | 305 |
| Interest Expense on Intercompany Advance Liability | – | – | 10 | 10 | 20 | 80 | 20 |
| **Derivative Financial Liabilities** | | | | | | | |
| Forward Exchange Contracts (Tenon Limited and Group) | 1 | 1 | 1 | – | – | – | – |
| | 306 | 306 | 11 | 10 | 20 | 80 | 325 |

(1) Interest expense on the intercompany advance liability is $20 million per annum based upon the 30 June 2013 balance outstanding and the average interest rate for the 30 June 2013 year.

**Tenon Limited**

| | Carrying value | Fair value | 6 months or less | 2012 $m 6-12 months | 1-2 years | 2-5 years | Over 5 years (1) |
|---|---|---|---|---|---|---|---|
| **Non Derivative Financial Liabilities** | | | | | | | |
| Intercompany Advance Liability | 290 | 290 | – | – | – | – | 290 |
| Interest Expense on Intercompany Advance Liability | – | – | 9 | 9 | 18 | 72 | 18 |
| | 290 | 290 | 9 | 9 | 18 | 72 | 308 |

(1) Interest expense on the intercompany advance liability is $18 million per annum based upon the 30 June 2012 balance outstanding and the average interest rate for the 30 June 2012 year.

### (d) Financial Instruments by Category

*Tenon Limited and the Group*

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, forward exchange contracts and interest rate swaps are classified as derivatives used for hedging.

### (e) Financial Instruments measured at fair value

*Tenon Limited and the Group*

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 following table presents financial assets and liabilities measured at fair value in the Statement of Financial Position in accordance with the fair value hierarchy. This hierarchy groups financial assets and liabilities into three levels based on significance of inputs used in measuring the fair value of the financial assets and liabilities. The fair value hierarchy has the following levels:

- Level 1: quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The level within which the financial asset or liability is classified is determined based on the lowest level of significant input to the fair value measurement.

Of the Group and Tenon Limited's external financial assets and liabilities as at 30 June 2013 and 30 June 2012, only the foreign exchange rate contracts in existence as at 30 June 2013 were above levels requiring disclosure, and they have been determined to be within the level 2 of the fair value hierarchy as all significant inputs required to ascertain the fair value of these derivatives are observable.

## 20 FINANCIAL INSTRUMENTS continued

| | Level 1 | 2013 $m Level 2 | Level 3 | Total |
|---|---|---|---|---|
| **Liabilities** | (a) | (b) | (c) | |
| Derivatives used for Hedging - Forward Exchange Contracts | – | -1 | – | -1 |
| **Net Fair Value** | – | -1 | – | -1 |

There have been no transfers between levels 1, 2 and 3 in the reporting period.

(a) The fair value of financial instruments traded in active markets is based on quoted market prices at the balance sheet date. A market is regarded as active if quoted prices are readily and regularly available from an exchange, dealer, broker, industry group, pricing service or regulatory agency, and whose prices represent actual and regularly occurring market transactions on an arm's length basis. The quoted market price used for financial assets held by the Group is the current bid price. The Group has no instruments in level 1.

(b) The fair value of financial instruments that are not traded in an active market is determined by using valuation techniques. These valuation techniques maximise the use of observable market data where it is available and rely as little as possible on entity specific estimates. If all significant inputs required to fair value an instrument are observable, the instrument is included in level 2. The Group has interest rate swaps and forward exchange contracts that are classified as level 2 instruments, however only the forward exchange contracts are above disclosure levels.

(c) If one or more of the significant inputs is not based on observable market data, the instrument is included in level 3. The Group's electricity contract would be classified as a level 3 derivative due to the lack of market data, however as at 30 June 2013 the fair value of the electricity hedge is less than $0.1 million.

Specific valuation techniques used to value financial instruments include:

- Quoted Market prices or dealer quotes for similar instruments.
- The fair value of the interest rate swap is calculated as the present value of the estimated future cash flows based on observable yield curves. The valuation is performed by an external source.
- The fair value of forward foreign exchange contracts are determined using forward exchange rates at the balance date, with the resulting value discounted back to the present value. The valuations are performed by external sources.
- The fair value of the Electricity Hedge is determined using the closing bid price quoted at balance date.

## 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:

| | | Tenon Group 2013 US$m | Tenon Group 2012 US$m |
|---|---|---|---|
| within | one year | **6** | 7 |
| | two years | **6** | 5 |
| | three years | **5** | 5 |
| | four years | **3** | 4 |
| | five years | **2** | 2 |
| after | five years | **7** | 6 |
| | | **29** | 29 |

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 $9.4 million (June 2012: $9.3 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 2012: nil).

## 23 CONTINGENT ASSETS

**Central North Island Forest Partnership (CNIFP) legal proceedings**

On 28 November 2012, Tenon announced that the Supreme Court had dismissed its appeal from the decision of the Court of Appeal to strike out the legal proceedings in relation to the Central North Island Forest Partnership (CNIFP) Goods and Services Taxation dispute. The decision had no negative impact on Tenon's existing tax position (including available tax losses) and the matter is now closed.

## 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 58.99% of Tenon Limited (June 2012: 58.99%). Three of Tenon Limited's directors are also directors of Rubicon Limited. Directors fees received by Rubicon were $0.1 million (June 2012: $0.1 million). Office and administration costs received by Rubicon from Tenon for the 2013 year were $0.1 million (June 2012: $0.2 million).

| | Tenon Group | |
|---|---|---|
| | **2013 US$m** | **2012 US$m** |
| **Tenon Group** | | |
| Borrowers under the credit agreement (1) | **–** | – |
| **Tenon Limited** | | |
| Royalties and Management Fees received for services provided to subsidiaries by Tenon Limited (2) | **–** | – |
| Finance charges paid by Tenon Limited on Advance from Subsidiary (3) | **-18** | -17 |
| Intercompany Advance Liability from Subsidiary Company (3) | **305** | 290 |
| Intercompany Advance Asset to Subsidiary Company (4) | **1** | 1 |
| Investment in Subsidiary Companies (5) | **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 2012: $0.3 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 it is not expected that Tenon Industries Limited will call for Tenon Limited to repay it in the next 12 months. It bears interest at 6.4 % per annum (30 June 2012: 6.30 % per annum).

(4) This advance is for no fixed term but Tenon Limited does not expect to call it for repayment in the next 12 months. It is not interest bearing.

(5) The Principal Subsidiaries included within Investment in Subsidiary Companies are disclosed in note 27, Principal Operations.

| | **2013** | **2012** |
|---|---|---|
| (b) Key Management Compensation | **US$m** | **US$m** |
| Salaries and other short-term employee benefits | **3** | 3 |
| Directors fees paid to Non Executive Directors (refer to note 5 (1)) | **–** | – |
| | **3** | 3 |

## 25 SEGMENTAL INFORMATION SUMMARY

Tenon derives its revenue from and operates within one material operating segment, being the Moulding and Millwork segment. Tenon provides a wide range of Moulding and Millwork products to an extensive number of customers in this one 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 2013 and June 2012 split between North America and Australasia is shown below. Tenon announced that it had commenced trading in Australia in February 2012, offering a variety of products in the Moulding and Millwork segment to reseller chains and independent stores.

| 2013 | North America US$m | Australasia US$m | Total US$m |
|---|---|---|---|
| **Operating Revenue (1)** | 317 | 47 | **364** |
| **Non Current Assets (2)** | 78 | 16 | **94** |
| **Capital Expenditure** | 2 | – | **2** |

| 2012 | North America US$m | Australasia US$m | Total US$m |
|---|---|---|---|
| **Operating Revenue (1)** | 294 | 40 | 334 |
| **Non Current Assets (2)** | 78 | 17 | 95 |
| **Capital Expenditure** | 1 | 1 | 2 |

(1) Operating revenue excludes transfers between geographical segments. Such transfers are accounted for at competitive market rates charged to unaffiliated customers for similar goods. Transfers are eliminated on consolidation.

(2) Excludes Deferred Tax and Financial Instruments.

## 26 NON-GAAP MEASURES

Tenon uses EBITDA when discussing financial performance. EBITDA is Earnings before Interest, Tax, and Depreciation and Amortisation. This is a non-GAAP financial measure and is not recognised within IFRS. As it is not uniformly defined or utilised this measure may not be comparable with similarly titled measures used by other companies. Non-GAAP financial measures should not be viewed in isolation nor considered as a substitute for measures reported in accordance with IFRS. Management believes that EBITDA provides useful information, as it is used internally to evaluate performance, and it is also a measure that equity analysts focus on for comparative company performance purposes, as the measure removes distortions caused by differences in asset age and depreciation policies.

The following table reconciles Net Profit / (Loss) after Taxation to EBITDA:

| | Tenon Group | |
|---|---|---|
| | 2013 US$m | 2012 US$m |
| **Net Profit / (Loss) after Taxation (1)** | **-3** | -9 |
| Less Income Tax Benefit | **–** | -2 |
| Plus Financing Costs | **4** | 3 |
| Operating Profit before Financing Costs (1) | **1** | -8 |
| Plus depreciation and amortisation | **4** | 5 |
| **EBITDA (1)** | **5** | -3 |

(1) Includes pre-tax business re-engineering and restructuring costs of $1 million (June 2012: $5 million).

## 27 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 2013 | % Holding June 2012 |
|---|---|---|---|---|
| **Principal Subsidiaries** | | | | |
| Tenon Industries Limited | NZ | Funding | 100 | 100 |
| Tenon Manufacturing Limited | NZ | Processing | 100 | 100 |
| Fletcher Wood Solutions Inc. | USA | Distribution | 100 | 100 |
| Creative Stair Parts LLC | USA | Distribution | 100 | 100 |
| The Empire Company LLC | USA | Distribution | 100 | 100 |
| Southwest Moulding Co., LP | USA | Distribution | 100 | 100 |
| Ornamental Mouldings LLC | USA | Processing | 100 | 100 |
| Ornamental Products LLC | USA | Processing | 100 | 100 |
| Ornamental Mouldings Company | Canada | Distribution | 100 | 100 |

**Report on the Financial Statements**

We have audited the financial statements of Tenon Limited ('the Company") on pages 13 to 49, which comprise the balance sheets as at 30 June 2013, the income statements, statements of comprehensive income, statements of changes in equity and statements of cash flows 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 2013 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 preform 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 the 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 the 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 the Group.

**Opinion**

In our opinion, the financial statements on pages 13 to 49:

(i) comply with the generally accepted accounting practice in New Zealand; and

(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 2013, and their financial performance and cash flows for the year then ended.

pwc

### 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 2013:

(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.

PricewaterhouseCoopers

Chartered Accountants
27 August 2013

Auckland

# Board of Directors as at 27 August 2013

**Simon Luke Moriarty**

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

*Committees*
Audit

Nominations (Chairman)

Last re-elected 2012

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. In 2011 he was appointed Monetary Policy Advisor to the Governor of the Reserve Bank of New Zealand. 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 is 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.

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 2012

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 Fibre Limited and The Property Group Limited. He is a director of Lyttelton Port Company Limited. He is also a member of The First Management Group Limited advisory Board. 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.

**George Karaplis**

BEng, MBA (McGill)

*Committees*
Nominations

Elected 2011

Mr Karaplis has over 36 years experience in building and growing shareholder value and a proven track record in "turn-around" and high growth companies. He is currently Deputy Chairman of Netia, a Polish integrated telecom services and media solutions company, and he has previously led France Telecom's Global One business in Greece as Managing Director. He also acted as Chief Financial Officer and General Manager of International Investments for the Hellenic Telecommunications Organisation. Prior to that Mr Karaplis held a number of management positions in Canada and Europe. He has relevant experience in the forestry and wood products industry from his previous employment with Domtar, a Canadian Paper and Forest Products producer.

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

**Stephen Garfield Kasnet**

BA University of Pennsylvania (Philadelphia)
Non-Executive Director

*Committees*
Nominations
Remuneration

Last re-elected 2011

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 Ipswich Bank, Trustee of the Governors Academy and a director of Two Harbors Investment Corp and Silver Bay Realty Trust. 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 2011

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.

# Corporate Governance as at 27 August 2013

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.

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 and environmental compliance. 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.

## 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 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 six 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, S G Kasnet, and G Karaplis 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, half 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.

A performance evaluation is conducted of the Board, its Committees and its members. This is conducted by the Chairman of the Board and/or the Committees of the Board. 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.

All non-executive Directors are entitled to attend all Committee meetings. Management attends 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.

**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 extended assurance programme; 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 also approves an annual extended assurance programme, and the results of that programme are reported directly to the Committee and also copied to all Directors.

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 external 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$45,000 which the Company considers did not impair the audit firm's independence from the Company.

**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, M C Walls and G Karaplis

The Nominations Committee comprises the six 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 Operating Officer, 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 external 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 remuneration paid to executives and senior management 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. Performance-based incentive schemes are in place among Tenon and its subsidiaries. These 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 of the Executive's direct reports must be approved by the Board of Directors.

On page 61 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 | Australasia based Business Number of Employees |
|---|---|---|---|---|
| NZ$100,000 | to | NZ$110,000 | 7 | 3 |
| NZ$110,000 | to | NZ$120,000 | 8 | 2 |
| NZ$120,000 | to | NZ$130,000 | 4 | 1 |
| NZ$130,000 | to | NZ$140,000 | 6 | 2 |
| NZ$140,000 | to | NZ$150,000 | 8 | 3 |
| NZ$150,000 | to | NZ$160,000 | 1 | 1 |
| NZ$160,000 | to | NZ$170,000 | 4 | – |
| NZ$170,000 | to | NZ$180,000 | – | 2 |
| NZ$180,000 | to | NZ$190,000 | 4 | – |
| NZ$190,000 | to | NZ$200,000 | 3 | 2 |
| NZ$200,000 | to | NZ$210,000 | 2 | – |
| NZ$220,000 | to | NZ$230,000 | 1 | 1 |
| NZ$230,000 | to | NZ$240,000 | 3 | – |
| NZ$250,000 | to | NZ$260,000 | 1 | – |
| NZ$270,000 | to | NZ$280,000 | 1 | – |
| NZ$280,000 | to | NZ$290,000 | 1 | 1 |
| NZ$310,000 | to | NZ$320,000 | 1 | – |
| NZ$320,000 | to | NZ$330,000 | 1 | – |
| NZ$330,000 | to | NZ$340,000 | 1 | – |
| NZ$340,000 | to | NZ$350,000 | 2 | 1 |
| NZ$460,000 | to | NZ$470,000 | 1 | – |
| NZ$580,000 | to | NZ$590,000 | – | 1 |
| NZ$600,000 | to | NZ$610,000 | 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 25 to 30).

## Health and Safety

The Company has adopted a "zero-harm" policy with regard to health and safety. The Board takes steps to ensure that it has a good understanding of health and safety matters in the workplace, and as to the Company's operations and hazards and risks associated with those operations. The Board conducts site visits, receives presentations from managers on health and safety and requires regular reporting of health and safety information. All injuries are required to be reported to the Board. The Board also has the benefit of regular reviews by independent third parties. For example, in New Zealand the Company's Taupo site has been awarded "Tertiary" status by the Accident Compensation Commission, which is the highest qualification awarded by the Commission.

## 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 the following respects:

- The Company does not offer any equity security compensation plan to Directors and all Directors may attend meetings of the Audit Committee; and
- The Nominations Committee is not comprised of a majority of independent Directors, as half of the members of the Committee are independent Directors.

## NZX Diversity Disclosure

In accordance with Listing Rule 10.5.5(j) relating to diversity disclosures, of Tenon's 20 officers, 20% are female (June 2012: 16%). Tenon has 6 (June 2012: 6) Non-Executive Directors, all of whom are male. Tenon does not have any Executive Directors.

## 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 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 Chairmen of the Company's Audit and Remuneration Committees are 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);
- Investors may subscribe on the Company's website to an email service whereby stock exchange filings made by the Company are emailed to them; 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 2013 year was $55,134 (1) (NZ$67,500) per annum per Director, with the Chairman receiving $106,184 (2) (NZ$130,000) per annum. The Chairman of the Audit Committee receives an additional $5,309 (1) (NZ$6,500) per annum and the Chairman of the Remuneration Committee receives an additional $3,676 (1) (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 2013 was $390,839 (1) (NZ$478,500). Fees, prior to any taxation liability, paid to individual non-executive Directors in the year ended 30 June 2013 were:

| | Fee (1) |
|---|---|
| M J Andrews | 55,134 |
| R H Fisher | 58,810 |
| G Karaplis | 55,134 |
| S G Kasnet | 55,134 |
| S L Moriarty (2) | 106,184 |
| M C Walls | 60,443 |

(1) Directors' fees have been translated from New Zealand dollars at an average foreign exchange rate of NZ$1 = US$0.8168.

(2) Total Directors' fees in relation to S L Moriarty (Chairman) were paid directly to Rubicon Limited.

## 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 2013.

As at 30 June 2013, 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 58, where the employee received remuneration and other benefits totaling NZ$100,000 or more during the year ended 30 June 2013.

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

**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

**Tenon Manufacturing Limited**
A T Johnston, P M Gillard, J E Paice, A S White

**Tenon Holdings Limited**
A T Johnston, P M Gillard, J E Paice, A S White

**Fletcher Challenge Limited**
A T Johnston, P M Gillard, J E Paice, A S White

**Kaingaroa Holdings Limited**
P M Gillard

**CNI Forest Nominees Limited**
A T Johnston, P M Gillard, J E Paice, A S White

**Tenon Retirement Plan Nominees Limited**
A T Johnston, P M Gillard, J E Paice, A S White

**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

**Fletcher Wood Solutions, Inc**
A T Johnston, A S White, P M Gillard

**Tenon USA Holding Company**
A T Johnston, A S White, P M Gillard

**Tenon Supply, LLC**
A T Johnston, A S White, P M Gillard

**The Empire Canada Company Limited**
A T Johnston, A S White, P M Gillard, C Rogers

**Southwest Moulding Co LP**
A T Johnston, D Bell, P M Gillard, A S White, T H Highley

**AWM Acquisitions Corporation**
A T Johnston, A S White, P M Gillard

**Ornamental Mouldings Company**
A T Johnston, A S White, P M Gillard

**Ornamental Mouldings, LLC**
A T Johnston, A S White, P M Gillard

**Ornamental Investments, LLC**
A T Johnston, A S White, P M Gillard

**Comanche Investments, LLC**
A T Johnston, A S White, P M Gillard

**Fairfield Road, LLC**
A T Johnston, A S White, P M Gillard

**Ornamental Products, LLC**
A T Johnston, A S White, P M Gillard

**Creative Stair Parts, LLC**
A T Johnston, A S White, P M Gillard

**Forestry Corporation of New Zealand Limited**
P M Gillard

## Directors' Interests

In accordance with Section 140(2) of the Companies Act 1993, Directors advised the following changes in their interests during the year ended June 2013:

| | | |
|---|---|---|
| **M J Andrews** | | |
| National Centre for Advanced Bio Protection Technologies | Resigned | Director |
| **R H Fisher** | | |
| The First Management Group Limited | Appointed | Member of Advisory Board |
| **S G Kasnet** | | |
| Silver Bay Realty Trust | Appointed | Director and Chairman of Audit Committee |

## 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 2013 the Company effected directors' and officers' liability and statutory liability insurance which was noted in the Interests Register. During the year the Company authorised an updated Deed of Indemnity and Insurance for a member of senior management, which was noted in the Interests Register.

# Shareholder Statistics

## 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 totaling US$4,000 were made during the year.

## Auditor's Fees

Fees payable to PricewaterhouseCoopers during the year are disclosed on page 31. During the year the auditor was paid US$45,000 for non-audit related work for the Company, which is discussed on page 56.

## Credit Rating

Tenon has not sought a credit rating.

## Directors' Holdings – Equity Securities

**Tenon Limited Ordinary Shares**

| | 30 June 2013 | | | 30 June 2012 | | |
|---|---|---|---|---|---|---|
| | 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 | – | – |
| G Karaplis | **–** | **–** | **–** | – | – | – |
| | **38,655** | **–** | **11,943** | 38,655 | – | 11,943 |

# Shareholder Statistics continued

## Largest Shareholders

The 20 shareholders with the largest holdings of shares as at 31 July 2013 were:

| | Tenon Ordinary Shares | % of Tenon Ordinary Shares |
|---|---|---|
| Rubicon Forests Holdings Limited | 38,747,695 | 58.99 |
| New Zealand Central Securities Depositary Limited | 17,620,474 | 26.82 |
| Leveraged Equities Finance Limited | 331,083 | 0.50 |
| Caprian Developments Limited | 305,740 | 0.47 |
| Sok Eng Boey & Yeow Ann Chiam & Kay Hong Chiam & Shen Mei Chiam | 255,000 | 0.39 |
| C W Flood | 200,000 | 0.30 |
| Tenon Custodians Limited | 182,548 | 0.28 |
| Tenon Employee Educational Fund Limited | 144,721 | 0.22 |
| J E C Anderson & B L Denholm | 140,000 | 0.21 |
| D J Sandori | 120,000 | 0.18 |
| M H Teulon & E M Quigley | 103,569 | 0.16 |
| E A Badham & L J Badham | 102,367 | 0.16 |
| A Kaan & A Blackwood & I R Eades | 100,000 | 0.15 |
| S P Wallace & Sievwrights Trustee Services (No.4) Limited | 100,000 | 0.15 |
| Geary Limited | 85,783 | 0.13 |
| J Wilson | 80,000 | 0.12 |
| D J Campbell | 78,000 | 0.12 |
| D R Stevenson | 73,542 | 0.11 |
| N L Petry | 60,000 | 0.09 |
| Peter Donald Wheeler | 58,274 | 0.09 |
| | 58,888,796 | 89.64 |
| Total Shares | 65,690,681 | |

**NZCSD**

New Zealand Central Securities Depository Limited ("NZCSD") is a depository system which allows electronic trading of securities to its members. At 31 July 2013, the shareholdings held through NZCSD were:

| | Tenon Ordinary Shares | % of Tenon Ordinary Shares |
|---|---|---|
| JPMorgan Chase Bank NA | 10,528,633 | 16.03 |
| Accident Compensation Commission | 4,616,807 | 7.03 |
| Citibank Nominees (New Zealand) Limited | 1,828,335 | 2.78 |
| HSBC Nominees (New Zealand) Limited | 374,463 | 0.57 |
| National Nominees New Zealand Limited | 271,336 | 0.41 |
| Private Nominees Limited | 900 | 0.00 |
| | 17,620,474 | 26.82 |
| Total Shares | 65,690,681 | |

# Investor Information

## Distribution of Shares – 31 July 2013

| Size of Holdings | Ordinary Shareholders Number | Ordinary Shareholders % | Ordinary Shares Number | Ordinary Shares % |
|---|---|---|---|---|
| 1 – 200 | 962 | 22.88 | 133,400 | 0.20 |
| 201 – 500 | 1,100 | 26.16 | 365,686 | 0.56 |
| 501 – 5,000 | 1,874 | 44.56 | 2,577,991 | 3.92 |
| 5,001 – 10,000 | 121 | 2.88 | 911,020 | 1.39 |
| Over 10,000 | 148 | 3.52 | 61,702,584 | 93.93 |
| Total | 4,205 | 100.00 | 65,690,681 | 100.00 |

Less than a minimum holding: As at 31 July 2013, 927 holders of Ordinary shares held less than the minimum holding of 200 or less shares under the NZX listing rules.

## Supplemental Disclosure of Domicile of Beneficial Owners (1)

| | Ordinary Shares Number | Ordinary Shares % |
|---|---|---|
| New Zealand | 52,445,240 | 79.84 |
| United States of America | 12,784,281 | 19.46 |
| Other | 461,160 | 0.70 |
| Total issued voting shares as at 13 August 2013 | 65,690,681 | 100.00 |

(1) Updated for information received by 13 August 2013 in response to notices under sections 28 and 29 of the New Zealand Securities Markets Act 1988.

## Substantial Security Holders

As at 27 August 2013 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 notified to Tenon by the substantial security holder.

| | Tenon Ordinary Shares | % of Tenon Shares |
|---|---|---|
| Rubicon Forests Holdings Limited | 38,747,695 | 58.99 |
| Third Avenue Management LLC | 10,482,120 | 15.96 |
| Accident Compensation Commission | 4,617,628 | 7.03 |
| Total | 53,847,443 | 81.98 |
| Total issued voting shares as at 27 August 2013 | 65,690,681 | |

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.

## 2013-2014 Calendar

- Annual Shareholders Meeting: TBA
- Half Year End: 31 December 2013
- Half Year Results Announcement: February 2014
- Financial Year End: 30 June 2014
- Annual Results Announcement: August 2014
- Mailing of Annual Report: September 2014

## Dividend

There is no 2013 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 | 65,690,681 as at 27 August 2013 |

## Share Registry Enquiries

**Enquiries**

Computershare Investor Services Limited
Private Bag 92119,
Auckland 1142
159 Hurstmere Road,
Takapuna, Auckland City 0622
New Zealand
Telephone: 64-9-488-8777
Facsimile: 64-9-488-8787
E-mail: 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.

## Company Websites

www.tenonglobal.com
www.tenon.co.nz
www.empireco.com
www.ornamentalmouldings.com
www.southwestmoulding.com
www.lifespanoutdoor.com
www.fwsdirect.com

## Other Investor Enquiries/Registered Office

Investor Relations
Tenon Limited
Level 1,
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

## 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, particularly in North America. Amongst other things, fluctuations in industrial output, commercial and residential construction activity, changes in capital availability, declining housing turnover and pricing, levels of repair and remodelling and additions to existing homes, new housing starts, relative exchange rates, interest rates, profitability of customers, competitor product development, demand and pricing, and customer concentration risk can each have a substantial impact on Tenon's results of operations and financial condition.

## Directors

Simon Luke Moriarty (Chairman)
Michael John Andrews
Rodger Herbert Fisher
George Karaplis
Stephen Garfield Kasnet
Michael Carmody Walls

See page 52-53 for details of Directors.

## Executive Officers

**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. Tony has a Bachelor of Science (Hons) from the University of Otago.

**Don Bell – Chief Executive, Southwest Moulding - Texas**

Don Bell has over 30 years experience in the important Texas wholesale millwork distribution market with Tenon subsidiary Southwest Moulding Co., which was established in Dallas in 1952. Don is a former owner of Southwest. Under Don's continued stewardship, Southwest has continued to grow its various operations and capabilities, and is now recognized as having a leading position in the Texas market.

**Greg Clark – General Manager and Vice President Finance North American Manufacturing**

Greg Clark has over 20 years leadership experience in millwork manufacturing in North America. Greg is also a Chartered Public Accountant, with over 10 years experience in public and industry accounting. Prior to joining Tenon's manufacturing operations in North America in 2010 as General Manager and Vice President Finance, Greg held a number of roles in the industry, including President of American Millwork Corporation and General Manager at Woodgrain Millwork. Greg holds a Masters degree in accounting from Brigham Young University.

**Paul Gillard – General Manager Corporate**

Paul Gillard joined Tenon Limited in 2001. Paul's role includes commercial negotiations for the Group, company secretarial, governance and legal affairs. He had previously spent five years as Corporate Counsel with EDS (New Zealand) Limited, then 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.

**Thomas H. Highley – Chief Executive Officer, North American Operations**

Tom Highley joined Tenon subsidiary The Empire Company in 1991, when the then owner Westinghouse Credit Corporation engaged Tom to turn the business around, after he had successfully executed four turnarounds (manufacturing and distribution building material companies) in the prior ten years. Before becoming a turnaround agent, Tom worked for Owens Corning Fiberglass in various building materials sales and sales manager roles for 15 years, culminating in his employment as the East Coast Regional Sales Manager. Since Tom joined Empire, it has grown from a small regional millwork distribution business to one of the largest multi-regional millwork distribution businesses in North America. Tom is a graduate of The Ohio State University.

**Mark Taylor – General Manager New Zealand and Australia Operations**

Mark Taylor joined Tenon in 2004 (having previously worked for Fletcher Challenge for 18 years). He has held several management roles at Tenon's Taupo operations, including Sawmill and Solid Lineal Mouldings Plant Manager. He was appointed General Manager of the Taupo operation in May 2006. In 2012 Mark's responsibilities were expanded to include Tenon's Australian business, which he was instrumental in establishing. Mark has extensive experience in the manufacture of high quality wood products, and with his team has successfully managed the supply of high value radiata products to global customers for many years.

**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.

www.tenonglobal.com