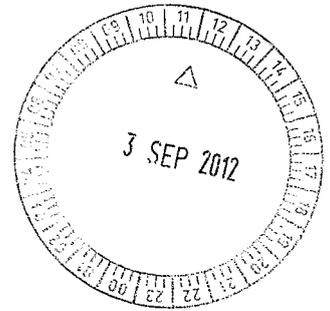




Wescorp Group



Hon. Brian Ellis MLC
Chair
Standing Committee on Environment and Public Affairs
C/- Parliament House
Harvest Terrace
PERTH WA 6000

RE: PETITION NUMBER 152 TABLED BY HON.WENDY DUNCAN

Dear Mr Ellis

I am the Executive Chairman of the Wescorp Group and have been intimately involved in the sandalwood industry for over 18 years.

History

Following the formation of the Sandalwood Act of 1929, all sandalwood exporting companies were amalgamated to form the Australian Sandalwood Company Ltd. The Australian Sandalwood Company was originally formed to provide for the orderly marketing of the State's sandalwood resource. Whilst this objective was achieved, the profits from the marketing and sale of Sandalwood remained with the company. The work undertaken by the Australian Sandalwood Company had never been offered under public tender. Following a rigorous public tender process in 1994 Wescorp won the rights to market and process sandalwood on behalf of the Western Australian Government. Since then the profits from sandalwood have largely remained with the State with the exception of subsidies to the oil extraction industry.

Wescorp as the State Government's Sandalwood Marketing and Processing Agent

Wescorp was formed in 1986 and its involvement in the export of primary produce from Western Australia dates back to 1926 through its previous owner Western Australian Farmers Co-Operative (now Wesfarmers Ltd). The exports were fruit and vegetables from our packing sheds; fresh dairy products from Masters and Harvey Fresh; meat; grain, pulse and hay; livestock and genetics; and seafood.

Wescorp has a long history in the export of Western Australian products and a reputation and relationship with customers that are envied by other competitors. Wescorp's success has always been based on the good of the industry above all other considerations.

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In the first two years as the sandalwood marketing and processing agent we were able to gain the confidence and understanding of the market and commenced to value add to the sandalwood in Western Australia. In the past there had always been baled raw product packed into five categories and a small amount of "large chip" into bags. From this practice of some sixty years we were able to develop a new product range that saw significant value adding in WA and thus created further employment and increased returns to the State.

At this stage I would like to invite members of the Standing Committee to the Wescorp factory in Canning Vale to view our operation and to gain an understanding of the value adding that is being carried out to sandalwood in Western Australia.

Wescorp as agent for the Forest Products Commission (FPC) has a number of obligations in its contract to ensure:

- ✓ Maximum financial return to the State Government
- ✓ Best utilisation of the Sandalwood resource, and
- ✓ Continued product development to maintain market position.

Included in our Contract obligations to CALM (prior to FPC) was to develop further value adding of the product. When expressions of interest were call for by CALM in 1996 to "extract oil" from the sandalwood, we also participated up to the point where we could not see how this could compete against the export prices being achieved for the current process. Unfortunately, we were very naïve as to the extent that CALM would subsidise a new business and for the length of time that that subsidy would last. This subsidy has cost the State in excess of \$5 million per annum directly and far more indirectly through loss of opportunities. The successful company continues to operate with this subsidy to 2016. This is the only area of the current commercial arrangements where the profits from sandalwood are not properly retained by the State.

By 2001, Wescorp had completed its research and development of manufacturing mosquito repellent joss sticks. New Mountain, a 100% owned subsidiary of Wescorp was opened by Hon Kim Chance MLC on 3rd October 2001. This company produced pure WA sandalwood joss sticks for repelling mosquitoes without any subsidy from any institution or Government body. This business is still operational and is responsible for the employment both directly and indirectly of over 70 people in this State. From raw material export value, it adds a further 17 times the value to that product at the wholesale level and obviously over 30 times at the retail level.

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Wescorp's first agreement with CALM/FPC finished in 2004. After another very competitive tender process, Wescorp was successful for a second term. It is interesting to note that many of the submissions to the Standing Committee were contenders in this 2004 tender process. This agreement finishes in 2014 as stated by many of the submissions.

Illegal Harvesting of Sandalwood

In the last 12 months illegal harvesting of sandalwood has climbed to a very serious level, with many stakeholders accusing other parties for this development. Wescorp does not have a position on who is responsible for this unfortunate development but is very concerned for the future of the industry and reputation of the sandalwood industry in Western Australia. We have been very proud that WA has the only sustainable harvesting system in the world and see it as highly important that illegal harvesting and sale is stopped and preventative measures put in place at State and Federal Government level. Most other countries that supply the sandalwood market have exhausted their own supplies and this has put enormous pressure on the WA resource. Under the appropriate Government bodies the Western Australian sandalwood resource has been managed extremely well and is seen throughout the world as an example of how a natural resource should be managed for the benefit of the State.

We believe in the last 12 months there has been more illegal sandalwood taken from the State than the legal harvest from the State. We have seen it in the market place, boldly advertised on local sandalwood company websites and confirmed to us by stakeholders including DEC, FPC, ASN, Pastoralists and operators in the rangelands of Western Australia.

Complaints from long term customers of FPC (many of whom are third generation) in Asia have been extensive. One particular country has reduced its importation of FPC sandalwood products by 46% for the same period in 2011 compared to 2012. The FPC agents recently confirmed that this has been caused by the large importation of illegal discounted sandalwood to their country from Western Australia. This is causing significant downward price pressures on the FPC prices and destroying the excellent reputation that Western Australia has enjoyed for sustainable harvesting.

In financial terms this means that the State is missing out on over \$12 million of income annually which could be put to managing this special resource.

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Indications that charges will be laid by the Department of Environment and Conservation against Sandalwood thieves following the recent seizures of illegal sandalwood are encouraging.

Plantation Sandalwood

As discussed in some of the submissions there is in excess of 15,000 hectares of Australian Sandalwood (*Santalum spicatum*) in plantation in Western Australia. Unfortunately, the initial plantations were commenced by Managed Investment Scheme (MIS) companies that promoted false returns and shortened periods of harvesting to encourage investment in their schemes. Many of these companies no longer exist; however those remaining in the industry still promote the idea that these plantation trees can be harvested in less than 20 years and provide a sound return on initial investment.

The MIS companies also quote prices that are only achieved from the wild sandalwood trees that are over 65 years old and growing in harsh natural conditions that promote heartwood with good yields of oil. It is misleading to compare plantation grown sandalwood at age 20 to mature wild sandalwood.

Wescorp has employed a full-time research chemist for over five years and with the extensive library (probably the largest in the sandalwood world) we have tested samples from all over the world and various aged plantations. These results have clearly demonstrated that the quantity and quality of the sandalwood is very much lower than most of the claims.

We believe plantations are the way of the future and the returns can be justified to investors if the correct information is provided, particularly the time of harvesting. For this reason it is very important that the harvesting of sandalwood from the rangelands continues for many more years to come so the market is not lost to WA before the plantations are mature to harvest and generate commercial returns to the investors.

It is worthy to note that many of the sandalwood plantation investors are farmers who have grown small areas on their properties as an alternative source of income in their retirement.



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Sustainable Harvesting

It is not Wescorp's role to provide advice to the Government on which Department or Agency should be managing the State's sandalwood resource. Our only observation is that it can only be done by a Government body that has the resources for research, controlling and monitoring of the resource. Certainly without the work of FPC and the development of the regeneration programme known as "operational woylie", no one could safely say that the resource was being managed sustainably. The work done towards developing this regeneration programme has been a great success and is a credit to those involved.

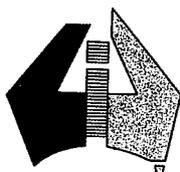
We will be the first ones to admit, that there is a "wall" between two of the Government bodies responsible for the management and harvesting of sandalwood. This is a pity as they seem to be very competitive for justification of their roles and should be looking more at the return and protection of the State resource. This is probably more at a lower management level which I would think is quite normal under the current unstable circumstances. Any planned changes to the management of the sandalwood resource should concentrate on a more focused and commercially effective arrangement. The current situation whereby research is housed in the Department of Agriculture and Food, operational management is conducted by FPC and the regulatory role is conducted by DEC seems overly bureaucratic and inefficient.

Exit of Experience from FPC

In the 18 years Wescorp has been involved in the industry, there have only been three managers of the Sandalwood Branch. Peter Jones up until 2004, (and is now involved in sandalwood plantations in private enterprises); Grant Pronk who worked under Peter Jones for eight years prior to becoming manager for seven years until 2011 (and now has his own forestry company); and the current manager, who has been in the sandalwood division working under Grant Pronk for over 8 years. Compared with many businesses this is stable and solid succession management. Wescorp, as the agent for FPC, works strictly to its contract requirements under close management and supervision of the FPC's Sandalwood Manager.

Access to Suitable Oil Extraction Sandalwood

Access to green sandalwood for the extraction of sandalwood oil has been difficult or impossible for most Western Australian companies other than Mount Romance Australia (MRA) who have an enviable contract arrangement with the State Government.



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The most sort-after product in the range of green sandalwood products is called Uncleaned Logs (UCL). In 2001, FPC exported 399 tonne of UCL to the overseas market. For the same period in 2011, FPC exported less than 22 tonne to that same market. This is due to the option contained in the MRA contract for taking a monopoly share of the green sandalwood at the exclusion of overseas buyers or other Western Australian producers. Of the green sandalwood that is harvested, there is very little left after the contract to MRA is fulfilled. In 2008, MRA aggressively took FPC to court due to a short supply of about 140 tonne for a specific period and joined Wescorp in this action. Fortunately this was thrown out of the Federal Court after an expensive two years of litigation, with the following comment in the judgement:

76 For all these reasons I am of the opinion that MRA's action against Wescorp under s 46 of the TPA was always hopeless such that it had no real prospect of success. It was, at least, unreasonable of MRA to institute and continue with those proceedings. It was particularly unreasonable of MRA to pursue interlocutory relief seeking to restrain Wescorp from acting as agent for the FPC and thereby, to its knowledge, effectively put Wescorp out

of business. Properly advised, in my view, MRA could not have concluded that Wescorp had any substantial power in the market for the supply of harvested or harvested and processed sandalwood or in the market for the supply of sandalwood oil. The known and undisputed facts fall well short of being capable of establishing either of these threshold requirements.

The simple fact is that there is not any more suitable sandalwood available to other interested local parties while the MRA contract is in force and the sandalwood harvest is set at the current sustainable levels.

Whilst the current contract arrangement advantages MRA over any other prospective Western Australian company it is also resulting in annual losses to State royalties to the order of \$5 million annually due to the subsidies contained in the contract.

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Utilisation

Rightly, FPC has adopted a full utilisation technique and harvests, processes and sells “the entire tree”, except for the leaves and the bark. This has been a huge step forward in utilisation of the sandalwood resource. There is minimum wastage and many other forestry industries around the world are very jealous of this method. To do this, it has meant that Wescorp has invested enormous capital in machinery and processes to provide a product that is suitable for the market. The butt and the UCL are the most valuable part of the tree, and there is very little of this available to the overseas market. Without this high grade product it is very difficult to get customers to buy the lower grade products, which is the majority of FPC sales to the export market.

Summary

Wescorp is very willing to host a visit to our operation in Canning Vale by the Standing Committee. Wescorp is also willing to offer its services to the Committee for any participation required by stakeholders at the Committee’s discretion.

We would value the opportunity to discuss ways of making this well-managed, sustainable industry fairer to Western Australian oil producers and more profitable to the State.

Yours sincerely,

Tim Coakley
Executive Chairman
Wescorp Group of Companies

30 August 2012

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