

16



(copy on

WP-917 (See

WP-918)

H010/2676

(F)

Marius Naser  
Forestry Tasmania  
79 Melville Street  
HOBART TAS 7000  
November 3<sup>rd</sup>, 2010.

Dear Marius,

***Contract of Sale 917 – take or pay (2009/10)***

I refer to your letter of 25/10/10.

Gunns Limited (**Gunns**) disagrees with your assertion of an entitlement to invoke clause 4.5(a) of CoS 917.

1. During calendar 2009 there was a dramatic downturn in the Asian woodchip market in the wake of the global financial crisis and there were permanent pulp mill capacity reductions implemented in the Japanese industry. The reduced market demand has continued into 2010. This was, and is, a Supervening Event under the Contract of Sale over which Gunns had any control;
2. Gunns has kept FTas fully informed of the loss of sales volumes by reason of the position of our Asian customers and our efforts to mitigate the effects of the downturn on FTas. This has involved among other things:
  - 2.1 substantially reducing Freehold and Private Property native forest volumes and replacing with FTas wood;
  - 2.2 seeking alternative new markets in China at loss making or breakeven pricing in order to sell FTas pulpwood;
  - 2.3 harvesting Freehold plantations to blend with FTas native forest pulpwood to make it saleable despite that destroying value;
3. Pursuant to Recital 6 and Clause 12 of Schedule 13, you were made aware of the requirements of a number of our Japanese end customers (whom we are reliant on for sales of our products and which you are fully aware of) that our products be FSC certified. During 2009 the Japanese industry became very selective on which coupes were acceptable for pulpwood supply due to FTas's inability to provide FSC certification.

Old growth and HCVF were deemed unacceptable in the Japanese market and FTas refused to recognise this as a marketing issue requiring a resolution;

4. Also the low quality of native forest pulpwood supplied from State Forest by FTas has adversely impacted upon our Japanese customers and caused them to reduce volumes from Tasmania. Coupled with a strong \$A, this has made Tasmanian native forest woodchip grades the least preferred raw material to Japanese pulp and paper manufacturers.

5. Pursuant to Recital 6 we have attempted to inform and engage with you in good faith on numerous occasions so that collectively we can find a solution to the problems facing all of us in the industry;

6. It is Gunns view that despite us making you aware of the above circumstances and FTas being able to influence the outcomes resulting from the happening of significant change in markets and circumstances constituting supervening events that you now seek to apply the take or pay provisions of the contract in isolation in seeking to enforce them.

7. You will recall that there have been a number of meetings at various levels between the parties in relation to the matters set out above. At these meetings Gunns personnel raised these issues of concern, which were at the time foreseeable as impacting on our ability to comply with Clause 4.5(a).

8. In light of the matters set out above it is the position of Gunns that Clause 4.5(a) does not apply by reason that the failure to obtain the threshold amount was due to action or inaction FTas such that clause 4.5(b)(ii) applies.

9. Gunns gives notice that it requests that FTas confer with it in good faith to discuss the above.

Yours sincerely,



Bryan Hayes,  
General Manager-Forest Products  
Gunns Limited

4010/2603

177

Phone: 6235 8170  
Your Ref: WF-917-PW and WF-918-PW  
Our File:



27 October 2010



Mr Greg L'Estrange  
Gunns Limited  
PO Box 572  
LAUNCESTON TAS 7250

Dear Greg

**Re: Outcomes of meeting on 20 October 2010**

I would like to confirm the main points discussed at our meeting last week, on 20 October. Please let me know if your understanding on any of these points differs from my own.

1. Gunns is planning to withdraw from all of its native forest harvesting and processing operations, in Tasmania at least, as soon as possible and with the following provisos:
  - (a) Gunns expects to continue to process and sell sawn timber from stock, for a period;
  - (b) an orderly approach to the various "people issues" is important; and
  - (c) the withdrawal must proceed on a basis that meets Gunns' shareholders' expectations.

An independently verified "shutdown plan" has been prepared, but has not yet been discussed with other parties.

2. Forestry Tasmania has a potential interest in the following of Gunns' assets, either through purchase or through lease:
  - (a) the Triabunna chipmill and related facilities;
  - (b) the Southwood sawmill and related facilities;
  - (c) the Massey Greene chipmill, Burnie port facilities and related facilities;
  - (d) one or other of the Scottsdale softwood sawmills and related facilities; and
  - (e) the site of the Smithton sawmill.



3. Gunns is prepared to consider Forestry Tasmania's interest in each of these assets, subject to Gunns' requirement to meet its shareholders' expectations. In this regard, Gunns will provide Forestry Tasmania with such information as is available for each asset, to assist Forestry Tasmania to prepare specific proposals to Gunns with respect to any or all of the assets in which it has a potential interest. Gunns will also cooperate with Forestry Tasmania's requirements for any due diligence investigation into the relevant assets and agreements.
4. Forestry Tasmania will not oppose any endeavours by Gunns to secure Commonwealth government funds in return for Gunns' withdrawal from native forest harvesting and processing, nor any endeavours by Gunns to achieve the support of the State government for such an arrangement.
5. Forestry Tasmania has established a group of industry stakeholders who have agreed, in principle, to a cooperative arrangement for:
  - (a) the ongoing operation of the Triabunna chipmill and related woodchip export sales; and, possibly,
  - (b) the ongoing operation of the Massey Green chipmill and related woodchip export sales from Burnie.
6. Gunns would like to negotiate an agreement for the ongoing supply of hardwood plantation pulplogs by Forestry Tasmania.
7. Bryan Hayes and Mike Farrow are to be responsible for sorting out the outstanding matters related to Forestry Tasmania's existing contracts and agreements with Gunns, including roads, take or pays, current China contract issues etc.
8. Bryan Hayes and Mike Farrow are the respective contact points for discussions about the provision of information about those of Gunns' assets in which Forestry Tasmania has a potential interest, including the conduct of any due diligence investigations that Forestry Tasmania may wish to undertake.
9. Hans Drielsma, Michael Wood and Calton Frame are to be responsible for any matters relating to any change in the two existing wood supply agreements.

Yours sincerely



Bob Gordon  
Managing Director



File: Gunns  
China sale

78



Phone:

6235 8158

Your Ref:

Our File:

14 October 2010



WF-918-01

(copy) WF-917-

Hao/2501

Mr Bryan Hayes  
Gunns Limited  
PO Box 572  
LAUNCESTON TAS 7250

Dear Bryan

I refer to your letter of October 6<sup>th</sup> in relation to the China Sale.

Forestry Tasmania (FT) has made considerable efforts to improve the supply of China wood. In the Southern mill door zone, for example, the Huon district has moved all but one contractor into China coupes.

FT contractors are currently performing at well over 80% of base capacity state-wide. Unfortunately, this does not appear to be the case with Gunns' contractors who appear to be performing at around the 60% mark on State forest.

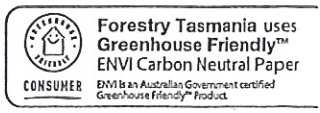
At the time the China sale was agreed, as you correctly state in your letter, the industry was facing a period of extreme difficulty which was being felt by all in the industry, including harvesting contractors.

At this time, FT contractors were operating at around 75% of base quota, however Gunns' contractors were at much lower levels. It is our understanding that a prime objective of the China sale was to lift all harvesting contractors to similar activity levels, particularly Gunns' harvesting contractors who were operating at levels below those of FT contractors. In fact, clause 2.3 Point of Sale makes reference to this: *"Forestry Tasmania expects much of the pulpwood to which this proposal refers will be harvested by contractors engaged by Gunns..."* It is our understanding that Gunns' contractors are still operating at lower levels state-wide.

Our August figures show that Gunns' contractors on State Forest produced 65% of planned China volume. This clearly shows that the current shortfall is not confined to FT contractors alone. What is Gunns doing to increase production of China wood by its contractors on State forest?

As discussed at the most recent KAM meeting, FT believes it will meet full supply under the China sale over the 12 month period of the agreement.

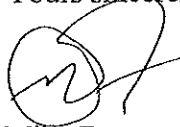
FT maintains its previously stated position that Gunns has acted outside the spirit of the agreement in respect to withholding payment (\$1,739,504) for alleged under-supply, and requests that this money be paid to FT immediately. The amount will attract interest charges for as long as it remains outstanding.



We also do not enjoy these ongoing disputes and must also protect our commercial viability.

I will be pleased to meet with you when you return from your overseas business commitments.

Yours sincerely

A handwritten signature in black ink, appearing to be 'MF' or similar, enclosed within a circular scribble.

Mike Farrow  
General Manager Operations & Sales



(copy on WF-917)



The General Manager Marketing and Sales,

Forestry Tasmania,

GPO Box 207,

Hobart, Tasmania, 7001.

FORESTRY TASMANIA

- 7 OCT 2010

HOBART

WF-918 EU

BS

How 2455

(F)

Attention: Mr. Mike Farrow

October 6<sup>th</sup>, 2010.

Dear Mike,

I refer to your letters of September 1<sup>st</sup>. and October 1<sup>st</sup>. in relation to the China sale.

We are encouraged by the actions proposed to substantially improve your performance and supply the discounted pulpwood for the China sale at the required rate. Regrettably, to date, FTas has over-promised and under-delivered contrary to the agreement that has been reached and to our detriment.

As it currently stands Gunns has been making the shipments in compliance with the agreement, but FTas has not been supplying the discounted wood at anywhere near the required and advised rate of supply. This has resulted in Gunns paying full price to FTas for pulpwood which has then been used to load the China vessels resulting in a very substantial and totally unsustainable financial loss to Gunns. It is not possible to cancel or delay chartered and scheduled woodchip vessels because agreed wood supply cost targets have not been met.

Faced with this situation Gunns has no option but to deduct a pro-rata discount to attempt to mitigate the real cash losses we are incurring, which losses would have been avoided but for your failure to fulfil your obligations under the agreement. A possible remedy to this impasse would be for FTas to immediately reallocate a volume of pulpwood as China pulpwood and balance the ledger.

Regarding the "disappointingly low prices agreed between Gunns and its Chinese buyers for supply during 2010" let me set the record straight. The market price into China was set by other Australian exporters from Bell Bay and Eden who were operating with a level of discounted wood pricing support not afforded to Gunns at that time. You were also aware of these difficulties faced by the industry and that Gunns was a price taker for the 2010 volumes based on pricing set by others on the back of cheap wood supply. In response to an impending industry meltdown due to shrinking markets following the global financial crisis the Minister for Forests at the time intervened and offered wood supply to Gunns at the same price as it was being supplied to our competitors.

GUNNS LIMITED | ABN 29 009 478 148

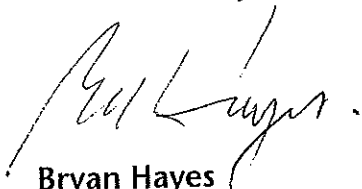
PO Box 572 Launceston Tasmania Australia 7250 | 78 Lindsay Street Launceston Tasmania Australia 7250  
T 03 6335 5201 | F 03 6335 5406 | www.gunns.com.au

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We do not enjoy these ongoing disputes over the operation of the wood supply agreements but we must protect our commercial viability. We note there have been a number of contractual matters in dispute over the last three years and as at today some are ongoing and not resolved. FTas has the ability to affect Gunns' fundamental obligations under the agreements and taking note of your most recent correspondences we hereby put you on notice that Gunns views about the matters in dispute remain the same and in that respect we continue to reserve all our rights.

I would be pleased to meet with you at the earliest convenience to further discuss our position and I suggest in the week beginning October 18<sup>th</sup>. after I return from business commitments in Japan.

Yours sincerely,

A handwritten signature in black ink, appearing to read 'Bryan Hayes', written over a horizontal line.

Bryan Hayes  
General Manager – Forest Products  
Gunns Limited



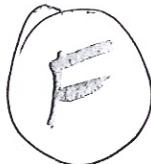
44010/2425

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(03) 62358158

WF-918-PW

WF-917-PW



Mr Bryan Hayes  
Gunns Limited  
PO Box 572  
LAUNCESTON TAS 7250

01 October 2010

Dear Bryan,

**Re: Short payment iro China Sale**

Our records show that Gunns paid Forestry Tasmania \$1,739,504 less than the due amount stated on the July sales invoice. Upon enquiry it was verbally confirmed at the KAM meeting held on the 27<sup>th</sup> September 2010, that the amount retained was related to Gunns' opinion that Forestry Tasmania under performed with supplies under the China sale.

This letter serves two purposes, namely:

- i) Demanding the outstanding amount to be paid within five business days from this date; and
- ii) expressing our disappointment that funds were being withheld from legitimate invoices without notice and/or discussion.

Forestry Tasmania also wants to remind Gunns that the China sale was constructed to predominantly benefit Gunns contractors. Significant discounts of the contractual stumpage and road tolls were reluctantly agree to in order to benefit industry as a whole. Withholding funds due from legitimate invoices are completely contrary to the spirit of the agreement between the parties.

I trust that you will acknowledge the importance of the contents of this letter and will make the necessary arrangements to rectify the position.

If you have any questions on this matter please give me a call.

Yours sincerely,

A handwritten signature in black ink, appearing to be 'MF' followed by a stylized flourish.

Mike Farrow  
General Manager Marketing and Sales

**BRIEFING NOTE****NOTED**

Bryan Green MP  
Minister for Energy and Resources

(Minister)

Date: ..... / ..... / 11

**SUBJECT: NEGOTIATIONS WITH GUNNS RE CONTRACTS 917 & 918****Purpose:**

To inform the Minister that Gunns Limited has advised that it intends to negotiate terms for new agreements to replace Contracts 917 and 918, which Gunns previously gave notice of its intention to terminate.

**Background:**

Gunns Managing Director Greg L'Estrange contacted his Forestry Tasmania counterpart Bob Gordon by phone on 30 June 2011 to advise that Gunns wished to commence negotiations for new agreements, as provided for in Contracts 917 and 918.

This verbal advice has now been confirmed by Mr L'Estrange in writing.

Under the terms of Contracts 917 and 918, Forestry Tasmania is obliged to enter into negotiations for new wood supply arrangements.

*Clause 3.3 (d): If this Contract is terminated pursuant to Clause 3.3(b), then the parties will negotiate in good faith about the terms of a new agreement for the supply of Pulpwood to Gunns.*

An agreement between FT and Gunns might be considered to be contrary to the Statement of Principles.

**Recommendation:**

For noting.

Name: Mr Bob Gordon  
Title: Managing Director

Date: 30 June 2011

81A



30 June 2011

Mr Bob Gordon  
Managing Director  
Forestry Tasmania  
GPO Box 207  
HOBART Tas 7001

Dear Bob

I refer to Mr Kloeden's letter to our Chairman of 4 May 2011 and subsequent conversations between Mr Kloeden and Mr Newman.

**New Agreements**

We agree that under the terms of Contracts of Sale 917 and 918 it is incumbent on the parties to negotiate in good faith for the terms of new agreements for the supply of the Supply Products and Pulpwood to Gunns (New Agreements).

So that there is continuity (operationally or otherwise) in Contracts of Sale 917 and 918, we should commence intended negotiations as soon as possible. Bryan Hayes will be in contact with the relevant Forestry Tasmania staff to begin this process.

As you are aware we are exiting all our hardwood processing facilities as a going concern and the New Agreements will form part of that process.

Yours sincerely

A handwritten signature in black ink, appearing to read "G. L'Estrange", with a long horizontal flourish extending to the right.

**Greg L'Estrange**  
Managing Director



Phone:

03 6235 8225

Your Ref:

Our File:

29 June 2011



Mr Bill Kelty  
C/- Joel Bowden  
[joel\\_bowden@linfox.com](mailto:joel_bowden@linfox.com)

Dear Mr Kelty

**Re: Forestry Tasmania's view of the Signatories Agreement dated 22<sup>nd</sup> June 2011**

In response to your request for feedback from Forestry Tasmania (FT) on the Signatories Agreement (22/6/2011), I provide the following comments:

**General Comments**

FT is not a signatory to the Statement of Principles or the Agreement, but was contracted to provide consultancy services to the signatories in relation to wood resource modelling. The resultant *Evaluation of Wood Resource Scenarios - Final Report to Signatories* (6 June 2011) has been independently verified by Professor Jerry Vancley and provides the best information for determining the feasibility of meeting the reservation and resource supply elements of the agreement.

It is notable that the Agreement is supported by ENGOS, as well as forest industry, unions and timber communities. That is a significant achievement, and distinguishes the Statement of Principles from previous processes that attempted to balance conservation and wood production values. The fact that it has progressed to this stage is in no small part due to your leadership and the assistance of Joel Bowden.

FT recognises that it is ultimately up to the Tasmanian Government, through the Parliament, to determine land use allocation and forest policy. However, it notes that the ENGO identified HCV forests have not undergone any governmental or independent scientific review to determine if they meet any objective criteria that would provide an imperative, rather than a preference, for their protection. It is noted that no criteria has been provided by the ENGOS to determine what might constitute HCV forests. It is also noted that the definition of HCV in FSC does not exclude logging.

**Specific Comments**

The Agreement calls for immediate interim protection of 430 000 ha of land on FT's balance sheet as an asset, with the remainder of the 572 000 ha being put into an Interim Forest Area. However, the *Evaluation of Wood Resource Scenarios Final Report* makes it clear that the minimum supply of high quality sawlog of 155 000 m<sup>3</sup>/y is very unlikely to be met if 430 000 ha is made unavailable. The extent of the shortfall cannot be modelled until the areas that make up the 430 000 ha are delineated on a map.



FT notes that the Agreement indicates that 155 000 m<sup>3</sup>/y of high quality sawlog, 265 000 m<sup>3</sup>/y of peeler billets and 12 500 m<sup>3</sup>/y of special timbers can be maintained if 360 000 to 432 000 ha of ENGO claimed HCV forests were immediately protected. This scenario has not been modelled and is demonstrably inconsistent with the resource modelling undertaken for the *Final Report*. For example, the Industry Scenario in the *Final Report* indicates that, as a minimum, the sustainable supply of special timbers would reduce to 11 500 m<sup>3</sup>/y and if the full 572 000 ha were reserved the supply would fall to 6700 m<sup>3</sup>/y. Similarly, the supply of peeler billets cannot be maintained if substantial areas of regrowth within the ENGO identified HCV Forests were to be reserved. It defies logic that substantial tracts of additional forest can be protected, without reducing the sustainable yield of forest products. The Agreement would certainly not be enduring if it is based on a false premise that the 430 000/572 000 ha claim can be reserved and still meet the minimum supply position of 155 000 m<sup>3</sup>/y of high quality sawlog, 265 000 m<sup>3</sup>/y of peeler billets and 12 500 m<sup>3</sup>/y of special timbers.

FT notes the view that areas agreed for protection should become National Parks. In the interests of efficiency and cost saving, and to ensure adequate fire management, FT would prefer to remain the land manager for any State forests lands to be protected, assuming that funds were provided for the management of these lands, and has demonstrated its capacity as a reserve manager through its protection of some 0.5M ha of State forest that form part of the Tasmanian Reserve Estate.

FT notes that this and the previous agreement refers to "licences", "quotas" and "allocations". None of these exist. All of Forestry Tasmania's arrangements to supply wood or services are through commercial contracts, which have value to FT and FT would expect fair commercial compensation for the compulsory acquisition of assets on its balance sheet or for the loss or breaking its commercial wood supply contracts. Currently, there is current strong market demand for fully certified (PEFC) wood products from Tasmania's forests and any reduction in supply levels represents a missed opportunity.

FT remains willing to act as expert commercial consultant to analyse requests from the parties or governments.

Yours sincerely



Bob Gordon  
Managing Director



Phone: 6235 8170

Your Ref:

Our File:

(83)



WF-917-PW and WF-918-PW

8 June 2010

Mr Greg L'Estrange  
Gunns Limited  
PO Box 572  
LAUNCESTON TAS 7250

Dear Greg

**Re: Amounts Outstanding for Log Supply**

I write to express my disappointment that Gunns has once again failed to make payment for log supply at the time agreed in our wood supply agreements. I refer to payment for logs supplied to Gunns Limited by Forestry Tasmania during April 2010, which payment was due by 5:00pm on 31 May 2010. I am informed of advice from your company that the relevant payment has not been made as of 8 June 2010.

Gunns' repeated tardiness in making payment for log supply as and when due is causing significant problems for Forestry Tasmania's cash flow management. This is not a trivial matter. I urge you to acquaint yourself with Forestry Tasmania's legal rights in these circumstances (reference Clause 11 of Schedule 13 of the relevant wood supply agreements).

I am reviewing our position on this matter and, of course, Forestry Tasmania will be charging interest for the overdue amounts.

Meanwhile, I ask that you advise me in writing whether Gunns is able to give an assurance that it will adhere to the contractual terms of payment in future.

Yours sincerely

  
Bob Gordon  
Managing Director



WF-917-100  
HO10/1153.

964

Phone:

Your Ref:

Our File:

6235 8225



(copy on  
WF-918)

7 May 2010

Mr Greg l'Estrange  
Chief Executive Officer  
Gunns Limited  
PO Box 572  
LAUNCESTON TAS 7250

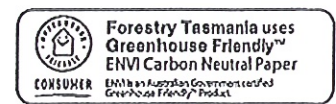
Dear Greg

I refer to our recent meeting. Forestry Tasmania is very concerned that Gunns appears unwilling to address the seriousness of its indebtedness.

Gunns had an opportunity at our meeting to make a proposal for reduction of its debt, but the meeting ended without anything from Gunns other than your suggesting a referral to dispute resolution procedures in respect of a take-or-pay event which is disputed. These procedures are not applicable to the general debt situation, as Gunns must know.

The following situation seems to have evolved:

1. Gunns has serious overdue trade debts to Forestry Tasmania.
2. Gunns' attitude has not encouraged us to believe it will meet future trade debts as they fall due.
3. Gunns has announced a proposal to move assets to another entity, a matter in which all creditors will have an interest and may wish to prevent by recourse to the Supreme Court either before or during any scheme of arrangement or other process that Gunns may pursue.
4. Gunns must be presumed to be in discussions with its bankers about the asset transfer. Other creditors, who are excluded from such discussions and who are not privy to the announced Information Memorandum, must be expected to enquire about those discussions and what effect this scheme has on trade creditors.
5. In particular, they may wish to know:
  - (a) what covenants Gunns has given its bankers;
  - (b) whether the banks know the present state of delinquent trade debts owed by Gunns;





- (c) what proposal to reduce trade debts is contemplated, if any;
  - (d) what notice is Gunns required to give to the banks of default events, for example if Forestry Tasmania gives a notice of suspension or termination under clause 11 of Schedule 13 of Contracts Nos 917 and 918.
6. By not engaging with Forestry Tasmania constructively, Gunns has forced a situation where Forestry Tasmania has to look to its contractual remedies as its only recourse.

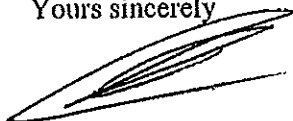
While it is not required to do so, Forestry Tasmania may wish to discuss with the banks, before or after the notice, an orderly recovery of all money outstanding upon issue of such notice.

In addition, and again while it is not required to do so, Forestry Tasmania might be prepared to discuss with your Board what announcement they wish to make under their continuous disclosure and other obligations, upon issue of the notice.

Forestry Tasmania's efforts to assist Gunns have not resulted in co-operation that would have been in everyone's interests. The extent to which the many stakeholders in Tasmania and elsewhere are disadvantaged by the termination or suspension of the contracts between Forestry Tasmania and Gunns is something for which Gunns must accept full responsibility.

With these consequences in mind, Forestry Tasmania is prepared to give Gunns four business days from today to make a written proposal to settle all amounts owing, and for future payments, on a basis satisfactory to Forestry Tasmania.

Yours sincerely



Bob Gordon  
Managing Director

(85)

**From:** Michael Wood  
**To:** Bryan Hayes, Bob Gordon  
**CC:** Darrel Stringer, Paul Smith, Marius Naser  
**Date:** 7/05/2010 2:22 pm  
**Subject:** Terms for shipments to China  
**Attachments:** GUNNS 20100507 deed of variation to CS918.doc

Bryan -

Thank you for Wednesday's copy of Greg's letter about the China sale.

We are still considering the ramifications of the qualification that is made in the second paragraph of the letter. The statement that "it is unlikely that we will achieve a single 800Kt sale at one point in time" indicates a departure from the basis on which the terms of the sale were negotiated between us. Gunns has, until very recently, been adamant that it required the full 800Kt commitment from Forestry Tasmania, in order to finalise terms for 400Kt sales to each of two customers in China. For example, on 5 February you indicated to me by email that "Volume commitments are not strong enough. Gunns seeks a commitment that there will be a total 800,000 gmt ...".

Forestry Tasmania has been prepared to negotiate terms for this sale at the greatly discounted prices that were negotiated between us. This is because of the benefits to Forestry Tasmania of the revenue and continuity of supply for sawlogs, peeler logs and other products that could be harvested in association with the harvest of an additional 800Kt of pulpwood during 2010.

The whole structure of the terms negotiated between us is based on the premises that:

- (i) Gunns is able to secure additional sales in China for the full 800Kt of pulpwood during 2010; and
- (ii) the new sales would result in additional sales of 800 Kt of pulpwood by Forestry Tasmania to Gunns during 2010, and of significant quantities of sawlogs and other products to Gunns and to other parties.

Clearly, your comments about likely total sales quantities during 2010, about buyers that are only prepared to buy on a "spot" basis and about Gunns' proposal to include stock on hand before the agreement was reached, represent significant variations from the terms and intent of the agreement. In particular, they significantly detract from the benefits to Forestry Tasmania.

As indicated at the outset, Forestry Tasmania is considering its other options, in the light of Gunns' advice about the likelihood that it will not be able to secure firm sales for the full 800Kt quantity in 2010. At the very least, this qualification in Greg's letter indicates to me that we will need to revisit the terms that we have negotiated. This is because some of the terms (e.g. 2.1.1 and 2.1.4) are rendered problematic by the uncertainty about forecast sales to China during the period and, therefore, about Gunns' requirements for additional pulplog supply.

In the meantime, I am pleased to provide a final copy of the agreed Deed of Variation to Contract of Sale 918. If you arrange for two copies of this to be signed by the appropriate officers at Gunns, and returned it to me, then I will arrange signing at Forestry Tasmania's end.

Although you and I have been exploring the way in which an agreement on retrospective pricing for Gunns' three currently contracted shipments might be implemented, these discussions have been on a "without prejudice" basis. You should not assume from these discussions that Forestry Tasmania has agreed to a retrospective adjustment related to these shipments.

- Michael

<b>Deed of Variation to Contract of Sale No 918</b>
-----------------------------------------------------

**A DEED OF VARIATION** made this                      day of                      2010

**BETWEEN**

**FORESTRY TASMANIA (ABN 91 628 769 359)**

a corporation established under the Forestry Act and operating as a Government Business Enterprise under the *Government Business Enterprise Act 1995 (Tas)* in the State of Tasmania, the registered office of which is at 79 Melville Street Hobart in Tasmania ("Forestry Tasmania") of the one part

**AND**

**GUNNS LIMITED (ABN 29 009 478 148)**

the registered office of which is at 78 Lindsay Street Launceston in Tasmania ("Gunns") of the other part.

**WHEREAS:**

- A. The parties hereto entered into Contract of Sale No 918 dated 20 December 2007 (in this Deed called "the Principal Agreement"); and
- B. the parties hereto entered a Deed of Variation dated 17 June 2008 to vary Clause 3.3(b)(ii) of the Principle Agreement by replacing "30 June 2008" with "30 November 2008"; and
- C. the parties hereto entered a second Deed of Variation dated 28 November 2008 which specified further agreed variations to the Principle Agreement; and
- D. pursuant to Clause 9 of Schedule 13, the parties hereto have agreed to further vary the Principal Agreement as set out in this Deed of Variation.

**OPERATIVE:**

1. Effective from the date of this Deed the Principal Agreement, as previously amended, is varied as set out in Clauses 2 and 3 of this Deed.
2. Clause 4.2(d) is deleted and replaced with the following:
 

“(d) for HJP, from all Supply Sources:

  - (i). for the period 1 January 2008 to 30 June 2009, 500,000 green metric tonnes per year; and
  - (ii) subject to Clause 4.2A, for each Planning Year commencing subsequent to 30 June 2009, such quantity for that Planning Year as the Parties may agree in writing, and ”
3. The following Clause 4.2A is inserted prior to Clause 4.3:
 

“For the purposes of Clause 4.2(d)(ii) the Parties will use their reasonable commercial endeavours to agree on the quantity of HJP for a Planning Year by 1 April that is three months prior to the commencement of that Planning Year, or failing agreement by that date, such sooner later date as is practicable.”
4. In all other respects the Principal Agreement is hereby confirmed and the Parties' obligations thereunder continued, save so far as expressly modified by the terms of this Deed.



**SEALING CLAUSE**

IN WITNESS whereof the Parties have executed this agreement as a deed on the day and year firstly hereinbefore written.

THE COMMON SEAL OF )  
 FORESTRY TASMANIA )  
 ABN 91 628 769 359 )  
 was hereunto affixed in )  
 the presence of: )

.....  
 R.L.Gordon  
 MANAGING DIRECTOR

on the ..... day of ..... 2010.

THE COMMON SEAL OF )  
 GUNNS LIMITED )  
 ABN 29 009 478 148 )  
 was hereunto affixed in accordance with )  
 its Memorandum and Articles of )  
 Association in the presence of: )

.....  
 J. E. Gay  
 DIRECTOR

.....  
 Signature of Director/Company Secretary

.....  
 Name of Director/Company Secretary

on the ..... day of ..... 2010.

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## Bob Gordon - Dispute provisions within Gunns' wood supply agreement

**From:** Michael Wood  
**To:** Attwood, Tony; Burgess, Lily; Drielsma, Hans; Farrow, Mike; Gordon, Bob; Jeffreys, Ken; Mazengarb, John; Smith, Paul; Stone, Martin; Whiteley, Steve  
**Date:** Thursday, 29 April, 2010 4:39 PM  
**Subject:** Dispute provisions within Gunns' wood supply agreement  
**CC:** Naser, Marius; Stringer, Darrel  
**Attachments:** GUNNS 20100429 Gunns dispute resolution procedures.doc

At yesterday's GM meeting I undertook to distribute a summary of the breach / dispute provisions within the wood supply agreements with Gunns. Here it is.

The contract has certain other provisions relating to specific forms of breach and dispute, but these are not relevant to the current situation (which is simply a failure by Gunns to pay monies that FT considers to be payable and overdue).

- Michael

## **Gunns Wood Supply Agreements - dispute resolution procedures**

Notes prepared by Michael Wood on 29 April 2010

These notes refer to the current situation, whereby Gunns has not paid certain amounts owing to Forestry Tasmania. The notes pass over other rights and obligations related to other forms of breach that are covered by the relevant clauses.

### **Breach**

1. If Gunns commits any breach or default, then Forestry Tasmania may issue a breach notice.  
(Clause 11.1 of Schedule 13)
2. Such a breach notice must nominate a reasonable cure period.  
(Clause 11.1 of Schedule 13)
3. If Gunns does not rectify the breach within the cure period, then Forestry Tasmania may at its option either suspend supply for as long as it determines or terminate the contract.  
(Clause 11.2 of Schedule 13)
4. If a suspension under (3) is in place, Forestry Tasmania may still terminate the contract if it sees fit.  
(Clause 11.6 of Schedule 13)
5. In any case, Forestry Tasmania may terminate the Contract immediately:
  - (a) if distress or execution be levied against any of the property of Gunns and not paid out within seven days; or
  - (b) if an order be made or a resolution be passed winding up Gunns; or
  - (c) if a receiver or a receiver and manager shall be appointed of Gunns' assets or any part thereof; or
  - (d) if any scheme of arrangement is submitted for approval by any Court by Gunns; or
  - (e) if Gunns becomes bankrupt or unable to pay its debts as and when they become due.  
(Clause 11.5 of Schedule 13)
6. Upon termination, Forestry Tasmania may:
  - ...
  - (b) recover from Gunns the amount of any loss or damage sustained as a result of the termination; and
  - (c) be regarded as discharged from any further obligations under this Contract; and
  - (d) pursue any additional or alternative remedies provided by law.  
(Clause 11.7 of Schedule 13)

### **Dispute**

7. Either party may notify the other of a dispute.  
(Clause 13.3 of Schedule 13)
8. Unless agreed otherwise, the parties must each nominate a representative within fourteen days of service of the notice.  
(Clause 13.4 of Schedule 13)

9. The representatives must meet within 21 days of service of the notice, to attempt to resolve the matter. They may seek the assistance of a mutually agreed expert to assist them.  
(Clause 13.4 of Schedule 13)
10. If the representatives can not resolve the matter within 28 days of service of the notice:
  - (a) they may agree to refer the matter to an independent expert; or
  - (b) either party may refer the matter to arbitration.
 (Clause 13.4 of Schedule 13)

### **Independent expert**

11. An independent expert shall be a person with suitable expertise, agreed between the parties. If the parties are unable to agree upon such a person, then each shall nominate an independent expert and those two shall appoint a third person as umpire. If the two can not agree on such an umpire within 30 days of their appointment, then the President of the Law Society of Tasmania shall appoint an umpire.  
(Clause 14.2 of Schedule 13)
12. Each party is to make its written submission to the experts, within 30 days of their appointment, with a copy to the other party. Such submission is to be accompanied by copies of any communications between the parties on the relevant matter. New information may only be submitted in specified circumstances.  
(Clause 14.3 of Schedule 13)
13. Each party shall be able to respond in writing to the other party's submission, within 30 days of receiving that submission.  
(Clause 14.4 of Schedule 13)
14. Neither party may communicate with the experts, other than at the request of the experts for clarification of a relevant matter. Any such clarification must be provided by the relevant party within fourteen days of its having been requested.  
(Clause 14.5 of Schedule 13)
15. The experts shall consider only information submitted to them and may exclude from consideration any information that they consider to be irrelevant.  
(Clause 14.6 of Schedule 13)
16. The experts shall use their best endeavours to reach a decision on the matter, within 30 days of receipt of the submission or clarification last received. The experts may still make a decision, even if all the information that they have requested has not been supplied, if that information has not been supplied within fourteen days of its having been requested.  
(Clause 14.7 of Schedule 13)
17. If the experts can not agree, then they are to refer the matter to the umpire and the umpire shall make a decision within 30 days of that matter being referred to him.  
(Clause 14.8 of Schedule 13)
18. Costs to be borne as directed by the experts and, in the absence of such direction, by the losing party.  
(Clause 14.9 of Schedule 13)



19. Experts are not acting as arbitrators within the meaning of the *Commercial Arbitration Act 1986 (Tas)*.  
(Clause 14.10 of Schedule 13)
20. Experts' decision to be notified as soon as possible and to be final and binding (except for manifest error).  
(Clause 14.11 of Schedule 13)
21. Experts to keep information confidential.  
(Clause 14.12 of Schedule 13)

### **Arbitration**

22. If a matter is to be referred to arbitration, then this may be done within 60 days of the notice of dispute.  
(Clause 13.13 of Schedule 13)
23. It is intended that the parties agree on the arbitrator. If they do not do so, then they each nominate an arbitrator and the arbitrators appoint another party as umpire.  
(Clause 13.5 of Schedule 13)
24. Any such arbitration is to be held in Tasmania and to be subject to the *Commercial Arbitration Act 1986 (Tas)*.  
(Clause 13.6 of Schedule 13)
25. Each party is entitled to have legal representation.  
(Clause 13.7 of Schedule 13)
26. The manner in which the arbitration is to be conducted is specified.  
(Clauses 13.8, 13.9 and 13.14 of Schedule 13)
27. The arbitrators' decision is to be made according to law and advice of that decision is to include the findings on which it is based.  
(Clauses 13.10 and 13.11 of Schedule 13)
28. The arbitrators' decision takes effect seven days after it is delivered. In the meantime, a party may inform the arbitrators of any mistake that they think has been made, and the arbitrators must review their decision forthwith and may amend their decision.  
(Clause 13.12 of Schedule 13)
29. The arbitrators may award interest.  
(Clause 13.15 of Schedule 13)
30. Circumstances and requirements related to an appeal on a point of law to the Supreme Court of Tasmania are defined.  
(Clauses 13.16 and 13.17 of Schedule 13)
31. A matter that the contract allows to be determined at the sole discretion of a party may not be referred for arbitration.  
(Clause 13.18 of Schedule 13)

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Forestry Tasmania  
GROWING OUR FUTURE

## Memorandum

FILE: WF-918-PW

DATE: 04 December 2009

TO: Managing Director

CC: Michael Wood, Hans Drieslma

FROM: Darrel Stringer  
Senior Manager Strategic Corporate Projects

RE: Contract of sale 918: Letter from Gunns CEO dated 30 November 2009

Set out below is my interpretation of the meaning of this letter and its implications with respect to the terms of Contract 918.

1. Gunns states they are not able to maintain a viable business in China for chips due to:
  - strengthening dollar;
  - high freight rates;
  - cheaper alternative supply; and
  - despite numerous trips to China by Gunns staff.
2. Gunns asks that all deliveries to be suspended effective as at 18 December 2009 pursuant to:
  - Recital 6 ("the change clause"); and
  - Clause 12 of Schedule 13 (supervening events).
3. Take or Pay – the letter requests FT to waive take or pay Clause 4.7(a) pursuant to:
  - Clause 4.7(c), which requires Gunns to demonstrate:
    - the deficiency is due to market forces beyond Gunns control;
    - all reasonable endeavours to sell the products made from HJP; and
    - that other potential customers to FT have no better potential to sell the HJP under the same commercial parameters.
  - The letter fails to specify a period where the take or pay is to be waived, however, a reasonable interpretation is that it be waived for 2009/10.
4. Comments on request that "all deliveries" be suspended from 19 December 2009
  - Whilst "all deliveries" under Contract 918 includes HJP and sawlogs, the context of the letter is focussed on woodchips and HJP, and that is how the request is reasonably interpreted.

- There is no provision to force Gunns to take HJP they do not want, and the Contract contemplates (eg Clauses 4.4(b) and 4.7(c)) scenarios where sales of HJP are decreased.
- FT should request that Gunns clarify the proposed term of the suspension that they have requested.
- Under Clause 4.8, FT have rights to sell any pulpwood not used by Gunns. In contrast to Contract 917, there are no "make up" provisions.

#### 5. Comments on take or pay which Gunns claim should be waived

- Gunns have a reasonable case that the take or pay provisions should be waived:
  - the market is certainly unfavourable;
  - Gunns have made significant efforts to make a sale; and
  - whilst Artec have been able to move some chips into China, it could well be argued that we have charged lower stumpage prices for Artec compared to Gunns.

#### 6. Implications if FT rejects Gunns claims

- If FT rejects Gunns claims then either party may refer the matter to the Dispute Resolution provisions of the Contract (Clause 13 of Schedule 13).
- Basically the process is:
  - notice of dispute by either party;
  - parties must meet to try to resolve; and
  - if no resolution then the parties may agree to refer the matter to an independent expert or otherwise it is referred to arbitration.

#### 7. Options for FT

- There are only a few options available to FT including:
  - accept Gunns claim and agree to forego the take or pay provisions for (at least) 2009/10;
  - dispute Gunns claims and push the matter for resolution in accordance with the dispute resolution procedures of the Contract; and
  - neither accept nor reject Gunns claim, and in accordance with Recital 6, seek a meeting to discuss proposed changes in the Contract. This would require FT to develop some options on how it wanted the Contract to look in the future, but may also open the Contract to other proposals from Gunns.

#### 8. Discussion of Options

- It is difficult to imagine a scenario where Gunns will be prepared to pay under the take or pay provisions without using at least the Dispute Resolution provisions of the Contract, and maybe the courts as well.
- There appears little prospect of a significant improvement in markets until well into 2010, but the extent of the recovery is not predictable. If the Japanese woodchip market recovers then Gunns is probably still our best customer.
- My initial view is that we should not yet concede the take or pay position, ie we must write refuting or deferring the current claim, but that a negotiated outcome is likely to be the best for FT.

- Under any option FT needs to clarify with Gunns its proposals with respect to the term for its suspension of deliveries and the period requested for the waiving of take or pay provisions.

## **COPIES OF RELEVANT CLAUSES FROM CONTRACT 918**

### **Recital 6 (the "change clause")**

6. The Parties acknowledge that they have entered into this Contract in the circumstances prevailing at the date of this Contract, and:
- (a) that each of them relied on its own assessment of the market, economic, political and other conditions which affected or might reasonably affect its performance under this Contract; and
  - (b) that each of them recognises that, if there is:
    - (i) a significant change in markets or in economic or political circumstances;
    - (ii) a significant technical advance; or
    - (iii) any other significant change in circumstances,
 that affects the business environment within which either Party operates, then the Parties will confer in good faith to discuss any changes to this Contract that might be proposed by either or both of them arising from those factors.

### **Clause 4.7(c)**

- (c) If:
  - (i) the actual quantity of HJP obtained by Gunns in any Planning Year is less than 75 per cent of the total quantity of HJP to which it is entitled in that Planning Year under this Contract due to market factors beyond the control of Gunns; and
  - (ii) where Gunns can demonstrate that they have used all reasonable endeavours to sell products made from HJP; and
  - (iii) it can be demonstrated by Gunns that other potential customers to Forestry Tasmania have no better potential to sell the HJP under the same commercial parameters,
 then the provisions of Clause 4.7(a) (or a pro rata part thereof, if Gunns demonstrates a partial inability to sell products produced from HJP) will be waived by Forestry Tasmania .



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## 12. SUPERVENING EVENTS

12.1 The definitions contained in this Clause 12.1 of Schedule 13 apply in this Clause 12 of Schedule 13:

“government” includes any arm or authority of government;

“law” means legislation, subordinate legislation, ministerial charter, rules, statutory rules, regulations, directions, orders and orders-in-council with which a Party is legally required to comply; and

“suspension period” has the meaning given in Clause 12.6 of this Schedule 13.

12.2 To the extent set out in this Clause 12 of Schedule 13 only, a Party (referred to in this Clause 12 of Schedule 13 as the “affected Party”) shall be relieved of its non-financial obligations to perform under this Contract if prevented from performing by a supervening event described in Clause 12.3 of this Schedule 13.

12.3 A supervening event is an event which:

- (a) is beyond the affected Party’s control provided that a Party is not hereby required to settle any strikes, lockouts and other industrial disputes or disturbances on terms contrary to its interest (as to which it shall be the sole judge);
- (b) is not caused by the affected Party’s fault or negligence;
- (c) is not caused by a lack of funds;
- (d) if an act of government, may include making of a new law, the amendment or repeal of any law and administrative action which is taken pursuant to any law or otherwise than in accordance with any law; and
- (e) is directly or indirectly the cause of the affected Party’s failure to perform an obligation (in whole or in part) other than an obligation to make a money payment.

12.4 If a supervening event occurs then the affected Party may:

- (a) give the other Party written notice of the event with reasonable particulars;
- (b) declare in the notice that it is relieved of its relevant obligations, in whole or in part, during such time as the supervening event continues to prevent their performance; and
- (c) give supplementary written notices modifying any previous notice.

12.5 If a supervening event occurs the obligations of the affected Party are suspended, without incurring any penalty or disadvantage, in accordance with any declaration given in a notice under Clauses 12.4(a) or 12.4(b) of this Schedule 13.

12.6 A suspension under Clause 12.5 of this Schedule 13 shall continue while the supervening event continues to prevent performance of the obligations (in this Clause 12 of Schedule 13 referred to as a “suspension period”) but, subject to Clause 12.7 of

this Schedule 13, the term of this Contract shall not be extended or shortened by the suspension period and a shortfall in supply caused by a supervening event shall be excised from the quantity of Pulpwood to be Made Available under this Contract.

- 12.7 If the obligations of the affected Party remain suspended under this Clause 12 of this Schedule 13 for more than eighteen months in respect of an average of 50 per cent or more of the quantity of Pulpwood to be Made Available under this Contract during that period then either Party may by three months' written notice to the other terminate this Contract without prejudice to the affected Party's relief from performance during the suspension period but preserving any claims that arose out of events other than supervening events.
- 12.8 A suspension period under this Clause 12 of this Schedule 13 is ended for all purposes of this Contract by the expiry or termination of this Contract.
-

(68)

03 6233 8171 (Marius Nesar)

WF-917-PW

15 May 2009

Mr Bryan Hayes  
Gunns Limited  
PO Box 572  
LAUNCESTON TAS 7250

Dear Bryan,

**Contract of Sale 917 – Clause 4.5 (Take or pay)**

Clause 4.5 in Contract of Sale 917 states that “ if the actual quantity of Pulpwood obtained by Gunns in any Planning Year is less than 85 per cent of the total quantity of Pulpwood to which it is entitled in that Planning Year under this Contract (referred to in this Clause 4.5 as the “threshold amount”) then the amount calculated as follows will become due and payable by Gunns to Forestry Tasmania upon the issue of a relevant tax invoice by Forestry Tasmania to Gunns”.

Our sales records show that, at the period ending 30 April 2009, Gunns has purchased a total of 1,020,409 green metric tonnes from FT under CoS 917. This effectively indicates that pro rata sales for 10 months of the 2008/9 financial year have dropped to a level below 85 per cent. With scheduled closures announced by Gunns, we are concerned that the current downward trend may continue and that a similar result will be imminent at the end of 12 months.

As a responsible party, we feel it our duty to make you aware of our observations and trust that you will endeavour to meet or exceed the required level to prevent activation of the contractual obligations.

If you have any further queries please do not hesitate to contact me.

Yours sincerely,

Marius Nesar  
Manager Forest Product Sales

Cc Bob Gordon