

42



18 April 2011

Mr Mike Farrow
General Manager
Forestry Tasmania
79 Melville Street
GPO Box 207
HOBART 7001
Tasmania

EMAILED TO MIKE FARROW

WITHOUT PREJUDICE

Dear Mike,

Contract of Sale 917
2009/10 Take or Pay dispute resolution

I refer to my email to you on 13 April 2011.

Pursuant to the dispute resolution process under Contract of Sale 917 (CoS 917) initiated by Forestry Tasmania on 9 February 2011 and our agreement to ventilate our respective positions in an effort to resolve this dispute informally, I set out below Gunns' response to Forestry Tasmania's Take or Pay claim for the 2009/10 Planning Year.

For the avoidance of doubt, this letter does not address Gunns' counter claims against Forestry Tasmania arising from Forestry Tasmania's breaches of CoS 917 and other wrongful conduct. We will raise those issues with you separately.

Calculation of Gunns' Entitlement

We disagree with Forestry Tasmania's assertion that Gunns' entitlement for the 2009/10 Planning Year was 1,650,000 GMT. While Gunns requested that amount by its Annual Notice on 31 March 2010, Forestry Tasmania refused to supply this volume by its Final Annual Notice dated 23 June 2009. Gunns accepted the Annual Supply proposed by Forestry Tasmania and thereafter was not entitled to supply in excess of that amount.

In circumstances where the parties agreed on Gunns' entitlement through the Annual Supply regime, and Gunns accepted Forestry Tasmania's proposal and conducted itself in reliance on that agreement, Forestry Tasmania cannot now assert that Gunns' entitlement was different to the base quantity stated in Forestry Tasmania's Final Annual Notice.

Gunns considers that the threshold amount is 85% of the base quantity prescribed in Forestry Tasmania's Final Annual Notice.

Calculation of the quantity obtained by Gunns

1. Gunns has reviewed the quantity of pulpwood which it obtained under CoS 917. It appears from this review that Forestry Tasmania has failed to include the following quantities of pulpwood obtained by Gunns pursuant to CoS 917:

Pulpwood from Schedule 5 coupes accepted by Gunns under CoS 917

2. By email dated 28 May 2009, Mr Peter Volker of Forestry Tasmania informed Gunns that "FT could substitute some 918 wood into 917 volumes." Gunns subsequently accepted wood from schedule 5 coupes (CoS 918 wood) as satisfying Forestry Tasmania's obligation to deliver pulpwood under CoS 917 from the Mill Door Supply Zone. In particular:
 - 2.1 In the period 1 July to 27 December 2009, Forestry Tasmania supplied a disproportionate quantity of wood from schedule 5 coupes, which was accepted by Gunns as (defective) performance of Forestry Tasmania's obligations under CoS 917. In total, Gunns accepted delivery of 36,063 GMT of Schedule 5 pulpwood under CoS 917 in order to achieve the expected balance between CoS 917 and CoS 918 wood.
 - 2.2 Further, on 30 November 2009, Gunns informed Forestry Tasmania that it would no longer accept any wood under CoS 918 from 27 December 2009. All wood from schedule 5 coupes supplied by Forestry Tasmania after 27 December 2009 was accepted in substitution for CoS 917 wood. The total quantity of schedule 5 wood accepted by Gunns under CoS 917 during this period was 43,431 GMT.
3. Gunns accepted delivery of these volumes of pulpwood from schedule 5 coupes in reliance on Forestry Tasmania's express assertion that the wood could be accepted in substitution for pulpwood under CoS 917. Forestry Tasmania cannot now assert that these quantities of pulpwood cannot be substituted for pulpwood under CoS 917 for the purpose of the CoS 917 take or pay provisions.
4. These volumes must therefore be included in the volume of wood "obtained" by Gunns under CoS 917.

Pulpwood acquired from Forestry Tasmania's Huon Wood Centre.

5. It appears that Forestry Tasmania has failed to include in its calculation the 33,521 GMT of woodchip acquired from Forestry Tasmania's merchandisers at the Huon Wood Centre through Southwood. No reason has been given for excluding this quantity of pulpwood from Forestry Tasmania's calculation of pulpwood taken by Gunns.
6. For the avoidance of doubt, the woodchip sourced from Southwood:
 - 6.1 Was acquired from Forestry Tasmania's merchandisers at the Huon Wood Centre; and
 - 6.2 Was from a "source from which the supply of Timber (was) controlled by Forestry Tasmania."
7. This woodchip was therefore pulpwood supplied under CoS 917 (clause 7.1(iii)) and must be included in the volume of wood "obtained" by Gunns under CoS 917.

Shortfall caused by Forestry Tasmania

8. Finally, the shortfall between the volume of wood acquired by Gunns and the threshold quantity under the take or pay clause was:
 - 8.1 caused by Forestry Tasmania's failure to make CoS 917 coupes available in accordance with the Wood Production Plan (supplied by Forestry Tasmania pursuant to clause 4 of schedule 11 of CoS 917) in the Stumpage Zone.
 - 8.2 by Forestry Tasmania's failure to deliver wood meeting the quotas set by Gunns in the Mill Door Zone.

Mill Door Zone:

9. Supply in the Mill Door Zone was controlled by Forestry Tasmania. Gunns set Forestry Tasmania weekly quotas and Forestry Tasmania was responsible for harvesting and delivering to the Points of Sale, volumes meeting the quotas set by Gunns (Clauses 7.3 and 7.4).
10. Forestry Tasmania's allocated quotas and actual supply for 2009/10 were as follows:

	Allocated Quota	Actual Supply	Deficit
Triabunna	204,158	208,743	0
Burnie	145,866	123,664	22,202
Tamar	119,171	111,017	8,154
Total Deficit			30,356

11. Gunns' failure to obtain this 30,356 GMT shortfall was entirely caused by Forestry Tasmania's failure to perform the contract. In addition to demonstrating that Forestry Tasmania was not ready willing and able to perform its obligation to make pulpwood available in the Mill Door Zone in accordance with the Annual Notice, Forestry Tasmania's failure to supply its Mill Door quota entitles Gunns to relief pursuant to clause 4.5(b)(ii) of CoS 917.

Stumpage Zone

12. Under Schedule 11 clause 4.1, Forestry Tasmania was required to deliver to Gunns a Wood Production Plan setting out the schedule of coupes from which Forestry Tasmania proposed to make available the Annual Supply of pulpwood. Gunns was entitled to rely on the Wood Production Plan for the purpose of planning its Forestry Operations.
13. Forestry Tasmania provided a Wood Production Plan for the 2009/10 Planning Year on 17 June 2009 but subsequently failed to provide the coupes specified in the Wood Production Plan. To date, we have identified the following shortfalls directly caused by Forestry Tasmania's failure to provide coupes in accordance with the Wood Production Plan.

14. Shortfall by Bishop due to scheduling changes:

14.1 In June 2010, Forestry Tasmania:

14.1.1 changed Coupe KA006D from clearfell to partial harvesting;

14.1.2 Withdrew coupe TE004H and Informed Gunns that Coupe FR013A was delayed; and

14.1.3 Had to make CH013F available "to buy some time".

14.2 These last minute changes in scheduled coupes adversely affected the harvesting operations of Gunns contractor, Bishop. As a consequence Bishop fell short of its allocated quota by 5,488 GMT. Had coupes been made available in accordance with the Wood Production Plan, this shortfall would not have occurred.

14.3 Further, due to the timing of the changes and Gunns' obligation under CoS 917 to treat its contractors equitably, Gunns was unable to procure make-up supply from any other contractor. This shortfall of 5,488 GMT was directly caused by Forestry Tasmania's failure to make pulpwood available by providing coupes in accordance with the Wood Production Plan. Accordingly, Gunns is entitled to relief pursuant to clause 4.5(b)(ii) of CoS 917.

15. Provision of non-complying coupes:

15.1 Coupes LW009D, RR103C, BW113D, GC100B, JV107B, KA008C, MF057A, NL111F, TY042L, UR003C, FR026B, MX280Y, MZ135U, MZ144W were provided to Gunns as CoS 917 coupes. However, 2,848 GMT of pulpwood harvested from these coupes was diverted to supply Artec, a competitor of Gunns, because it failed to meet the specifications of pulpwood under CoS 917.

15.2 The diversion of the wood harvested by Gunns contractor caused that contractor to fail to deliver its full quota of pulpwood to Gunns and caused 2,484 GMT of Gunns shortfall. Gunns is therefore entitled to relief in relation to this 2,484 GMT pursuant to clause 4.5(b)(ii) of CoS 917.

16. Delay of Coupe VD009A:

16.1 The Murchinson roading FPP for coupe VD009A was due on 1 December 2009 but was not certified until February 2010. As a result, it was not possible to construct roads to harvest VD009A in the 2009/10 Planning Year as anticipated.

16.2 Gunns contractor, Casegrande, was scheduled to harvest coupe VD009A. As a result of the delay and absence of alternative coupes, Gunns was forced to put Casegrande on a private forest coupe. The private coupe was a clearfell coupe comprising 4,200 GMT pulpwood. Had sufficient coupes been available on state forest, this volume would have been procured under CoS 917.

16.3 In addition to demonstrating that Forestry Tasmania was not ready, willing and able to perform its obligation to make coupes available containing sufficient pulpwood to satisfy Gunns' entitlement under the Annual Notice, Forestry Tasmania's failure to make sufficient coupes available entitles Gunns to relief pursuant to clause 4.5(b)(ii) of CoS 917.

17. Delay and Unavailability of Derwent East Coupes:

17.1 In email correspondence from Forestry Tasmania's planning staff on 19 May 2009, it was acknowledged that Forestry Tasmania were aware of the Derwent District

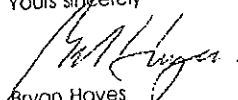
shortfall in the Outer Stumpage Zone for 2009 - timber locked up by the swift parrot being a significant contributor to the shortfall in the East.

- 17.2 In minutes to a meeting on 22 July 2009 it was noted that coupe MC014D was delayed. Gunns' contractor A&B Nominees was scheduled to harvest that coupe and had to be moved to private forest due to a lack of readily available substitute state coupes. Similarly, Gunns' contractor Iles was restricted from harvesting state forest coupes in Derwent East due to restrictions on coupe availability caused by swift parrot habitat during Planning Year 2009/2010 and the lack of readily available coupes in Derwent East.
 - 17.3 A&B Nominees harvested 10,331 GMT from private forest and Iles harvested 7,725 GMT from private forest. These volumes would have been sourced under CoS 917 had Forestry Tasmania made available either MC014D or suitable alternatives.
 - 17.4 Again, this lack of alternative coupes both demonstrates that Forestry Tasmania was not ready willing and able to perform its obligation to make wood available in the Stumpage Zone and entitles Gunns to relief pursuant to clause 4.5(b)(ii) of CoS 917.
18. Inability to place Gunns contractors in Derwent District:
- 18.1 At a scheduling meeting in February 2010, Forestry Tasmania operations staff confirmed that Forestry Tasmania was unable to provide additional 917 coupes. Three of Gunns' contractors, ETL, Oakley and EA Triffett were allocated to roadlines as these were the only 917 coupes available.
 - 18.2 As you are aware, roadline coupes are less efficient to harvest than clearfell coupes. As a result, Gunns contractors fell short of their quota allocation by 2,534 GMT. This shortfall was directly caused by Forestry Tasmania's failure to provide coupes as scheduled in the Wood Production Plan and Gunns is entitled to relief in relation to the shortfall.
 - 18.3 Further, due to the shortage of 917 coupes and relying on Forestry Tasmania's assertion that it could not make any further 917 coupes available, Gunns placed 4 of its contractors, Iles, Scott, W. Triffett and Wiggin and Dean, on private forest. These contractors harvested a total of 13,189 GMT pulpwood from private forest which would have been sourced under CoS 917 had coupes been available.
 - 18.4 Again, Forestry Tasmania's failure to provide sufficient coupes and/or provide coupes in accordance with the wood production plan both demonstrates that Forestry Tasmania was not ready willing and able to perform its obligation to make wood available in the Stumpage Zone and entitles Gunns to relief pursuant to clause 4.5(b)(ii) of CoS 917.

I do not consider that the factual matters that lie behind Gunns contentions set out above should be the subject of any dispute. If this is not the case then please provide a comprehensive response so that the areas of dispute can be narrowed and, hopefully, resolved between us.

I look forward to hearing from you.

Yours sincerely



Bryan Hayes
General Manager - Forest Products
Gunns Limited

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April 18, 2011

Mr. Mike Farrow,
General Manager Operations and Sales,
Forestry Tasmania,
GPO Box 207,
Hobart, TAS., 7001.

Dear Mike,

Variation Notice – 1 April 2011

Further to your letter of April 6th, and our subsequent meeting on Friday 8th April, I confirm my letter of April 1st is a notice of variation to the annual supply volume for 2010-11 due to the cancellation of previously confirmed shipping to China and the subsequent closure of Triabunna Mill.

Regarding the 4 points referred to in your letter we respond as follows:

1. We recognise the potential impacts of reduced pulpwood harvesting on the rate of production of sawlog from fully integrated operations. However we do not understand which provision of CoS 918 allows for Gunns to be inequitably treated in regard to the supply of sawlogs as a result. On a year to date pro-rata basis Gunns would have an entitlement to HQSL (excluding Southwood) supply of 85,857 m³ based on the formula at Clause 4.3(b)(i). To date Gunns has received only 51,424 m³ leaving a current shortfall of 34,433 m³ against the pro-rata entitlement to HQSL derived taking account of the reduced pulpwood offtake. Is Forestry Tasmania proposing that your letter of April 6th constitutes a notice of variation of the base quantity of HQSL or of the annual supply volume? Please clarify your intention in this regard.
2. We have provided to you copies of notices provided to each individual harvesting contractor which details our requirements for an orderly shutdown of forestry operations to ensure the obligations imposed by the Forest Practices Act are met. Our field supervisors have been charged with the responsibility to ensure requirements are met and we are confident that that has been achieved. If you have any concerns to the contrary please ensure appropriate operational staff communicate promptly with Gunns Triabunna management to resolve the issue.
3. We agree that it is prudent for us to agree to bring to an end the current China Sales Agreement. An analysis of deliveries against wood supply zones and contracts of sale has been commenced as a first step and will be provided to you as soon as it is completed. Following that I suggest

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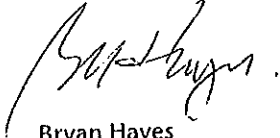
we meet and discuss the volume performance and the various financial matters that arise from it. From Gunns perspective there are several financial matters that need to be resolved in addition to the \$1.74 M of stumpage withheld by Gunns as an offset against these other matters.

4. Gunns will continue to provide variation notices for the 2010-11 annual supply volume that reflect market changes beyond Gunns control that impact our woodchip sales activity levels from time to time.

In addition to the above we have provided to you a formal proposal requesting discussions pursuant to Recital 6 about contract amendments that we believe are necessary to reflect the radically altered operating environment currently being experienced.

We await your response in due course and look forward to commencing those discussions at a mutually acceptable time.

Yours sincerely,



Bryan Hayes
General Manager-Forest Products
Gunns Limited

(44)

16 MAY 2011

1600

16 May 2011



WF-917-PW/2

B/S

WF-918

H011/900

Mr Mike Farrow
General Manager Operations and Marketing
Forestry Tasmania
GPO Box 207
Hobart TAS 7001

Dear Mike

Re - Reconciliation of China Sales Agreement volume and value

Please find attached our reconciliation of the volume and value of pulpwood supplied to Gunns under the 2010 China Sales Agreement up to end April 2011.

In summary, Gunns has sold 952,861gmt of chips to the Chinese customer at the discounted sales price in the period, well in excess of the agreed 800,000gmt supply volume.

FTas has supplied only 573,959gmt of discounted price pulplogs in the period, and the quantum of the discount did not meet the target provided for under the agreement causing direct loss to Gunns.

The volume shortfall of discounted pulplogs has been replaced by fully priced pulplogs, causing further loss to Gunns.

We have calculated the direct financial loss to Gunns \$5,673,322. That amount is claimed by Gunns from FTas consistent with the terms of the China Sales Agreement. We have withheld payment of \$1,700,000 against this cost to date so the nett amount of the claim is \$3,973,322.

Please provide a response to our claim within 14 days in order to close this matter in a timely manner.

Yours sincerely

A handwritten signature in black ink, appearing to read "Bryan Hayes".

Bryan Hayes
General Manager
Forest Products

Attachment

ACTUAL SALES	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
SALES	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Net Profit	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Net Profit	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336

For My Reporting China Sales Agreement as at:

Apr-11

Volume sold to China	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Expected Volume	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Expected Sales Cost	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Expected Total Cost	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Actual China Volume	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Actual Sales Cost	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Actual Total Cost	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Expected Volume Adj	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Expected Sales Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Expected Total Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
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Actual Total Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
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Expected Sales Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Expected Total Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
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Actual Total Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000

Volume to EUR

Apr-11

Volume to EUR

800,000	800,000	800,000
1,104,100	1,104,100	1,104,100
1,104,100	1,104,100	1,104,100
1,104,100	1,104,100	1,104,100

Expected Volume Adj	41,841	41,847	42,812	10,747	41,820	44,213	41,464	41,117	41,318	0	347,336
Expected Sales Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Expected Total Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
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Actual Sales Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000
Actual Total Cost Adj	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	1,104,100	0	11,041,000

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(45)



ELS

WF-917-PW/2

4011/892

16 May 2011

Mr Mike Farrow
General Manager Operations and Sales
Forestry Tasmania
GPO Box 207
Hobart TAS 7001

Dear Mike

Re - Contract of Sale 917 - 2009/10 Take or Pay Dispute

Thank you for your letter of 20 April 2011 in reply to my letter of 18 April 2011.

I understand that these matters were the subject of recent correspondences between our Boards. As such I believe it is prudent to await the final outcome of all discussions at that level before proceeding further with ours.

Notwithstanding, we will await your response to our detailed offset amounts and we remain ready to meet at an appropriate time to further progress those aspects of this matter.

Yours sincerely

A handwritten signature in black ink, appearing to read "Bryan Hayes".

Bryan Hayes
General Manager
Forest Products

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46

Phone:

Your Ref: 6235 8225

Our File:



Forestry Tasmania

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.

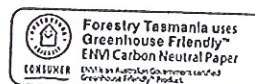
Gunns had an opportunity at our meeting to make a proposal for reduction of its debt, but the meeting ended without anything from Gunns other than your suggesting a referral to dispute resolution procedures in respect of a take-or-pay event which is disputed. These procedures are not applicable to the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



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www.forestrytas.com.au



- (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.

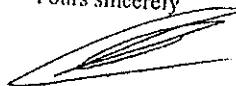
While it is not required to do so, Forestry Tasmania may wish to discuss with the banks, before or after the notice, an orderly recovery of all money outstanding upon issue of such notice.

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

47



12 May 2010

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

Dear Bob

Thank you for your letter dated 7 May 2010.

Firstly let me clarify our discussions of 27 April 2010. The meeting was requested by Gunns to attempt to bring to a conclusion two long term issues between Gunns and Forestry Tasmania.

These discussions were pre-empted by discussions on the recent agreements around the sale of 800,000 green metric tonnes of woodchip, announced by then Minister Llewellyn in February 2010. Your position at the meeting was to 'withdraw' that offer as Gunn's had not been able to make the required sale in one 'single order'. We expressed our extreme disappointment in your position and the lack of 'good faith' in such dealings.

It was under this level of trust, that we advised that we would be unlikely to have 'good faith' negotiations on these two outstanding issues and that we should immediately refer them to mediation to resolve these matters. We would abide by that process and its outcome. This is a normal commercial process when the parties are unable to negotiate within a commercial framework.

With regard the amounts outstanding by Gunns; we advise the following:

1. That \$2,565,040.19 will be paid on 11 May 2010 and \$1,095,683.20 will be paid on 13 May 2010
2. That at this date the following will remain outstanding:
 - I. Sawlog dispute \$354,000
 - II. Take or Pay dispute \$841,000
 - III. Interest on disputed amount \$273,000
 - IV. Sundry adjustment items (FT to provide particulars - details sought on 15 March 2010 and remain outstanding) \$296,000

03 6235 8225

48

4 May 2011

Mr Chris Newman
Chairman
Gunns Limited
PO Box 572
LAUNCESTON TAS 7250

Dear Chris

Thank you for your letter of April 18, regarding the contractual relationships with Forestry Tasmania (FT). Your letter constitutes a notice to terminate the contracts under their terms or, if FT agrees, to do so under alternative terms that you have proposed. FT acknowledges this notice. Under the terms of the contract, it is incumbent on the parties to attempt to negotiate in good faith terms of a new agreement for supply. It is unclear whether your alternative proposal for "full release and indemnity" envisages such further negotiation or not. In any event, we would be pleased to meet with you to seek to resolve the outstanding issues at Board level. For our part, I would propose to have three directors involved, including the Managing Director.

You have outlined your understanding of various developments that are the basis for your assessment of the current relationship and your decision to terminate the contracts. I can not allow the relevant comments in your letter to go unanswered, as they seriously misrepresent the activities of FT and of its officers. You should be aware that the Board has been fully informed of all aspects of the emerging issues between our two companies, and we have full confidence in, and strongly support the actions taken to date in seeking to resolve them.

We remain gravely concerned at Gunns' apparent casual disregard for FT's entitlements to fair and timely payment under the terms of the contracts, or at the very least the courtesy of timely notice and advice when circumstances prevented such timely payment. I refer in particular to the recurring pattern of failure to pay debts owing by due dates, and then, over the last year at least, only in dribs and drabs...usually without notice or explanation, or contrary to such notice when on occasion it has been given. We have been unable to assess whether this has been a deliberate stratagem to avoid Gunns' commitments or represents a fundamental inability on Gunns' part to pay debts as and when they fall due.

We would be quite justified in interpreting this as a hostile approach, particularly in the context of the numerous, but empty, assurances that have been offered over a period of years to address the situation. In particular, I would draw your attention to the correspondence attached.

The pursuit of our Take or Pay entitlements should be viewed in this context, including the unilateral refusal on Gunns' part to pay monies owed in respect of volumes supplied in good faith under the "China sale". At no stage prior to FT raising these matters has Gunns sought to notify us of its concerns about the structure of the agreement, or to seek a renegotiation, and we find no merit in now attempting to do so. As has already been made clear to Gunns in separate correspondence, we intend to further pursue these matters, together with such Take or Pay entitlements that arise from the 2010-11 year. You should be aware that this further amount is estimated by us as in the order of \$7M.

I assure you that each and every one of your assertions about FTs alleged actions or inactions are false and will be contested vigorously in any forum in which Gunns might choose to repeat them.

1. While there is little doubt that global events have resulted in a significant decline in the Japanese woodchip market, it is not clear that this decline is permanent, nor even that demand for native forest woodchips in Japan might not recover to some extent. While I share your views about the current difficulties of operating in the Japanese market, in particular, I think it is too early to draw the conclusion that you draw. You have also overlooked the significant current potential for growth in woodchip exports into the Chinese market, although I note the challenges in meeting our respective price expectations in that market.
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original indications that it would facilitate FT in an orderly transition to alternative sales arrangements.

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10. I confirm FTs strong and unambiguous support for Gunns' proposed pulp mill.
11. I refute your assertion of FTs "unwillingness and/or inability to comply with its contractual obligations" under Contracts 917 and 918. While these contracts are complex, and their obligations on each party extensive and demanding, all officers (i.e. FTs and Gunns') have generally worked diligently and in good faith to resolve any operational difficulties that have arisen. The contracts represented a significant shift in management responsibilities, and each party recognised at the time that it would take some time, and goodwill on both sides, to achieve the changes. The changes also involved third parties (e.g. contractors), whose cooperation had to be achieved by consensus rather than by direction. These factors, recognised at the time, together with the ongoing delays in the commencement of the pulp mill development and, more recently, volatility in Gunns' demand for pulpwood, have led to a very difficult operating environment that has tested all officers directly involved. It is a credit to each of them (including both Gunns' and FTs officers) that they have been able to work through the great majority of the issues that have arisen over the period since the contracts commenced in January 2008.
12. I do not accept your assertions that FT has in some way failed in its obligations to Gunns (and to the Tasmanian woodchip export industry) by not achieving FSC certification, or by "refusing to assist Gunns obtaining FSC certification", or by "indifference", given that Gunns itself has equally been unable to achieve such certification for any of its forest assets in Tasmania. I refute any such assertions, in the strongest possible terms. Despite this, FT has actively cooperated with Gunns' only recently initiated attempts to achieve FSC certification, and can in no way be held responsible for Gunns' own failure to do so. You may be unaware that FT has, in fact and for some time, been supplying pulpwood from State forest to Gunns that meets FSC requirements for controlled wood, and has in fact gone to some lengths to facilitate specific sourcing strategies within State forest to achieve it. FTs officers have worked very closely with Gunns' relevant officers and its Japanese customers on this matter, for many years. I need not add that FTs forests, and their management, are certified under the Australian Forestry

Standard. When it comes to market preferences for FSC or PEFC (including AFS), there are many complex external factors influencing the relevant market behaviour. Most of these are beyond the control of any law abiding citizen, and none can be laid at Forestry Tasmania's door. At a broader level, FT has consistently co-operated with Gunns in addressing customer concerns, including participating, at its own expense, in in-market visits and presentations, the hosting of customer visits to Tasmania and the implementation of active communication programs. Your suggestions to the contrary are wrong.

13. I strongly refute any assertion or inference that FT has any sort of contractual obligation to pursue FSC certification. In fact, Recital 4 of the Contracts acknowledges the following.

The forest management practices of each of the Parties are certified under the Australian Forestry Standard. Each of the Parties is committed to maintaining its certification under that standard.

14. Finally, you have attributed a value of \$200M to various infrastructure that might be transferred to FT upon the termination of the contracts. In the first instance, the observation is irrelevant as there is no link between the reversion of assets to FT following conclusion of the contract, and the financial obligations that arise under the contract, including Take or Pay liabilities. Irrespective of any other matters, the contracts make clear that on termination, any assets remaining on State forest after a period of 45 days, revert, as of right, to FT. In the second instance, the valuation is without factual basis. It overlooks the current condition of many of the roads and bridges built and used by Gunns on State forest, and Gunns' contractual obligations with respect to the care and maintenance of those roads and bridges. It also bears no relation to the value of those assets based on their ability to generate income. Suffice to say that FT attributes little value to these assets, and in fact is concerned at the liability they would represent should Gunns fail to rehabilitate or restore them to a stable condition within the requirements of the Forest Practices Act.

On behalf of the FT Board, we remain available at short notice to meet with Gunns' directors, as outlined at the beginning of this letter to seek to resolve the matters between us on fair commercial terms, consistent with our rights and responsibilities under the two contracts in question.

Yours sincerely



Adrian Kloeden
Chair, Forestry Tasmania

file
H011/990

49



(copy)
WF-9.17

Phone:
Your Ref:
Our File:

File WF-918-PW

A

24 May 2011

Mr Bryan Hayes
Gunns Limited
PO Box 572
LAUNCESTON TAS 7250

Dear Bryan,

Reconciliation of China Sales Agreement volume and value

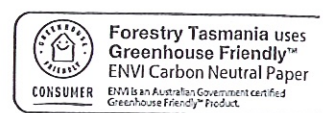
I acknowledge your letter of 16 May 2011.

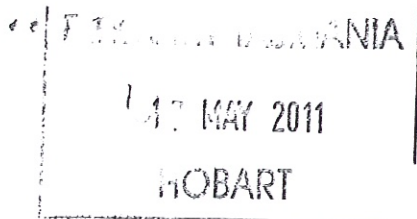
For the record FT refutes any claims made by Gunns against it under this sale, and considers your analysis flawed and biased.

I will respond in more detail addressing your claims in due course.

Yours sincerely

Mr Mike Farrow
Chief Operating Officer
Forestry Tasmania





(50)

BS

WF-917-Pu
WF-918-

H011/89.
(F)

16 May 2011

(Mr Mike Farrow
General Manager Operations and Sales,
Forestry Tasmania
GPO Box 207
Hobart TAS 7001

Dear Mike

Re - Formal proposal to amend Contracts of Sale 917 and 918

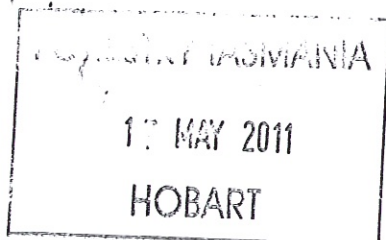
Thank you for your letter of 20 April 2011 in response to our proposal.

When we met on 8 April 2011 we agreed to provide to you a formal proposal for your consideration. This is what we have done.

I have subsequently been advised that the ongoing tenure of the contracts between Gunns and Forestry Tasmania is the subject of Board to Board discussions and for that reason we believe that the issue of contract amendments should be deferred until we better understand the outcome of those discussions.

Yours sincerely

Bryan Hayes
General Manager
Forest Products



51

BS

WF-917-

4011/892

16 May 2011

Mr Mike Farrow
General Manager Operations and Sales
Forestry Tasmania
GPO Box 207
Hobart TAS 7001

Dear Mike

Re - Contract of Sale 917 - 2009/10 Take or Pay Dispute

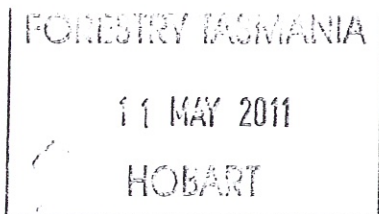
Thank you for your letter of 20 April 2011 in reply to my letter of 18 April 2011.

I understand that these matters were the subject of recent correspondences between our Boards. As such I believe it is prudent to await the final outcome of all discussions at that level before proceeding further with ours.

Notwithstanding, we will await your response to our detailed offset amounts and we remain ready to meet at an appropriate time to further progress those aspects of this matter.

Yours sincerely

Bryan Hayes
General Manager
Forest Products



10 May 2011

52

WF-917
WF-918

H011/833

Mr Mark Pettit
Manager Domestic Forest Products Sales
Forestry Tasmania
GPO Box 207
Hobart TAS 7001

Dear Mark

Re - Contracts of Sale 917 and 918 – Annual Supply Notice for 2011/12

Thank you for your prompt response and proposed pulpwood allocation under the contracts for 2011/12.

Since I wrote to you with our initial proposal and subsequent notice of variation I have been advised that the ongoing tenure of the contracts is now the subject of Board to Board discussion that may obviate this process entirely.

Notwithstanding that we do agree to meet when convenient to discuss the proposed volumes, the pricing mechanism for China sales, the sourcing and details of the classes of pulpwood and harvest systems in accordance with Schedule 6.

Please advise when you would be ready to discuss this level of detail and unless events overtake us we shall meet at an agreed time.

Yours sincerely

Bryan Hayes
General Manager
Forest Products

Phone: 03 6235 8225

Your Ref:

Our File:

53

**PRIVATE &
CONFIDENTIAL**



4 May 2011

Mr Chris Newman
Chairman
Gunns Limited
PO Box 572
LAUNCESTON TAS 7250

Dear Chris

Thank you for your letter of April 18, regarding the contractual relationships with Forestry Tasmania (FT). Your letter constitutes a notice to terminate the contracts under their terms or, if FT agrees, to do so under alternative terms that you have proposed. FT acknowledges this notice. Under the terms of the contract, it is incumbent on the parties to attempt to negotiate in good faith terms of a new agreement for supply. It is unclear whether your alternative proposal for "full release and indemnity" envisages such further negotiation or not. In any event, we would be pleased to meet with you to seek to resolve the outstanding issues at Board level. For our part, I would propose to have three directors involved, including the Managing Director.

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We remain gravely concerned at Gunns' apparent casual disregard for FT's entitlements to fair and timely payment under the terms of the contracts, or at the very least the courtesy of timely notice and advice when circumstances prevented such timely payment. I refer in particular to the recurring pattern of failure to pay debts owing by due dates, and then, over the last year at least, only in dribs and drabs...usually without notice or explanation, or contrary to such notice when on occasion it has been given. We have been unable to assess whether this has been a deliberate stratagem to avoid Gunns' commitments or represents a fundamental inability on Gunns' part to pay debts as and when they fall due.

We would be quite justified in interpreting this as a hostile approach, particularly in the context of the numerous, but empty, assurances that have been offered over a period of years to address the situation. In particular, I would draw your attention to the correspondence attached.



79 Melville Street Hobart TAS 7000, GPO Box 207 Hobart TAS 7001.
Phone (03) 6233 8203 International 61 3 6233 8203 Facsimile (03) 6233 8444
ABN 91 628 769 359

www.forestrytas.com.au



The pursuit of our Take or Pay entitlements should be viewed in this context, including the unilateral refusal on Gunns' part to pay monies owed in respect of volumes supplied in good faith under the "China sale". At no stage prior to FT raising these matters has Gunns sought to notify us of its concerns about the structure of the agreement, or to seek a renegotiation, and we find no merit in now attempting to do so. As has already been made clear to Gunns in separate correspondence, we intend to further pursue these matters, together with such Take or Pay entitlements that arise from the 2010-11 year. You should be aware that this further amount is estimated by us as in the order of \$7M.

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instrumental in ensuring that a potential purchaser of hardwood residues for a recently proposed new silicon smelter in Tasmania was introduced to Gunns' officers for them to discuss potential supply. Please be assured that there are many more examples, from the very recent past and from preceding years.

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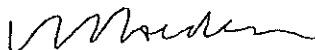
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Yours sincerely



Adrian Kloeden
Chair, Forestry Tasmania

Premier

Level 11, Executive Building, 15 Murray Street, Hobart TAS
GPO Box 123, Hobart, TAS 7001 Australia
Ph +61 3 6233 3464 Fax +61 3 6234 1572
Email Premier@dpac.tas.gov.au Web www.premier.tas.gov.au

54



WITHOUT PREJUDICE

26 AUG 2011

Mr A J Kloeden
Chairman
Forestry Tasmania
GPO Box 207
HOBART TAS 7001

Dear Mr Kloeden

As you are aware, the Tasmanian Forests Intergovernmental Agreement (TFA) was signed on 7 August 2011.

The State has determined under this Agreement and based on Crown legal advice that it is appropriate to make an offer of payment to Forestry Tasmania, in return for particular commitments to enable essential processes that are required to give effect to the TFA's objectives, to be immediately progressed.

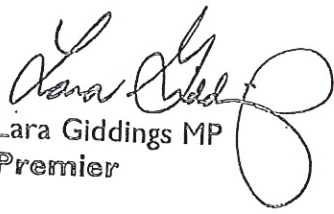
In accordance with Clause 34 of the TFA, the State is offering to pay Forestry Tasmania an amount of \$12.650 million (GST included). In return for this payment, Forestry Tasmania must sign the attached two Deeds of Release and agree to the conditions contained within.

A copy of the Deed of Release between the Crown and Gunns Limited has also been attached for information.

A pre-condition of this offer is that the State will also procure, by agreement with Gunns Limited, the release of Forestry Tasmania from any right or obligation under Contracts 917 and 918 and the China Sale Agreement. Please also note that the offer of payment to Forestry Tasmania is only activated if and when Gunns Limited executes its Deed of Release.

Forestry Tasmania has until close of business on 2 September 2011 to accept this offer. If acceptance is not received by way of signing the two Deeds of Release by that date, the State will pursue other avenues to achieve the TFA objectives.

Yours sincerely


Lara Giddings MP
Premier

Encl



Phone: 62358143

Your Ref:

Our File: WF-917-PW, WF-918-EU

29 April 2011

Mr Bryan Hayes
Gunns Limited
PO Box 572
LAUNCESTON TAS 7250

Dear Bryan,

Contracts of Sale 917 and 918 – Annual Supply Notice for 2011/12

Thank you for your letter to Mike Farrow dated 01st March 2011, followed by a further letter of variation dated 7th March 2011, in relation to the Gunns Annual Supply notice for 2011/12.

Forestry Tasmania has considered your notice under the Long Term Pulpwood Supply Agreement COS 917 and the Sawlog and Other Products Supply Agreement COS 918. Following a review of the resource available, Forestry Tasmania confirms the ability to meet the annual supply notice of **873kt in total** and proposes the following change to the forecast allocation of The Southern Mill Door volume supply to Triabunna:

1. Derwent West: 100kt
2. Huon: 360kt

I trust that the above proposed changes, made with reference to Schedule 11; Clause 1.4 (a) of CoS917, is acceptable to Gunns.

I note that Gunns have not yet requested any eucalypt sawlog supplies for 2011/12.

I propose a meeting of relevant staff to discuss the above.

Forestry Tasmania reserves all of its rights under all of its contracts and agreements with Gunns and nothing in this letter, including the above acceptance of the supply notice volumes which are considerably below the annual base quantity, constitutes a waiver of any of those rights.

Yours sincerely,

Mark Pettit
Manager Domestic Forest Product Sales
Forestry Tasmania

Phone: (03) 6235 8129

Your Ref:

Our File: WF-917-PW

56



W/F 917

20 April 2011

Mr Bryan Hayes
General Manager – Forest Products
Gunns Ltd
PO Box 572
LAUNCESTON TAS 7250

Dear Bryan,

**Contract of Sale 917
2009/10 Take or Pay Dispute**

Thank you for your letter of 18 April 2011 on this subject.

Forestry Tasmania will carefully investigate each of the claims in your letter, and respond in due course. For the record, I advise that, at this stage, Forestry Tasmania does not agree with any of your claims.

I note with surprise your statement that Gunns will raise separately "Gunns counter claims against Forestry Tasmania arising from Forestry Tasmania's breaches of CoS 917 and other wrongful conduct." You have not previously raised this matter, and I seek your urgent advice on a timetable for providing substantiation of this claim to Forestry Tasmania. Early receipt of the details of this claim will facilitate progress on the other matters we have been discussing relating to Contract 917.

Yours sincerely,

Mike Farrow
General Manager Operations and Sales



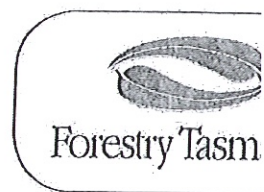
W/F 917

Phone: (03) 6235 8129

Your Ref:

Our File: WF-917-PW

57



20 April 2011

Mr Bryan Hayes
General Manager – Forest Products
Gunns Ltd
PO Box 572
LAUNCESTON TAS 7250

Dear Bryan,

re: Formal proposal of 10 April 2011 by Gunns Limited -
to amend Contracts 917 and 918

Thank you for your proposal of 10 April 2011, on the above subject.

Forestry Tasmania acknowledges its obligations under Recital 6 of the Contracts to "confer in good faith to discuss...changes...proposed" by Gunns. However, it is appropriate to point out that there is no requirement to change the Contracts and no requirement to refer a stalemate to any form of dispute resolution mechanism.

I also note your quotation from Recital 6 omits the statement that each party to the Contract "relied on its own assessment of the market, economic, political and other conditions which affected or might reasonably affect its performance under this Contract".

By separate letter, I have noted my surprise about the statement in your letter of 18 April 2011, on the current 2009-10 take or pay dispute, that Gunns will raise separately "Gunns counter claims against Forestry Tasmania arising from Forestry Tasmania's breaches of CoS 917 and other wrongful conduct." It appears premature and inefficient to commence discussions on varying either Contract, when Contract 917 is the subject of such potential claims.

Accordingly, once Forestry Tasmania has received Gunns' counterclaims in detail, and had an opportunity to review that information, it will revert in regard to your request of 10 April 2011 to confer in good faith.

Yours sincerely,

Mike Farrow
General Manager, Operations and Sales



Phone: (03) 6235 8129

Your Ref:

WF-917-PW

Our File:



Forestry Tasmania

19 April 2011

Mr Bryan Hayes
General Manager – Forest Products
Gunns Ltd
PO Box 572
LAUNCESTON TAS 7250

Dear Bryan,

re: Formal proposal of 10 April 2011 by Gunns Limited -
to amend Contracts 917 and 918

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Yours sincerely,

Mike Farrow
General Manager, Operations and Sales



Phone: (03) 6235 8129

Your Ref:

WF-917-PW

Our File:



19 April 2011

Mr Bryan Hayes
General Manager – Forest Products
Gunns Ltd
PO Box 572
LAUNCESTON Tas 7250

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**Contract of Sale 917
2009/10 Take or Pay Dispute**

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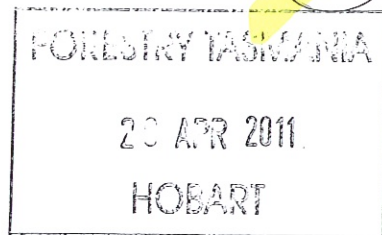
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Yours sincerely,

Mike Farrow
General Manager, Operations and Sales



18 April 2011



WF-917
WF-918

H011/725

Adrian Kloeden
Chairman
Forestry Tasmania
79 Melville Street
HOBART Tas 7000

Dear Adrian

Re - Gunns Limited and Forestry Tasmania

Thank you for taking the time to meet with me on 12 April 2011.

I am encouraged by your comment that FT's official position and history is one of continuing support for our development of the pulp mill.

I reiterate my comment that it is clear to me that the relationship between Gunns' and FT's management has become strained. Efforts to resolve the various disputes between the parties at management level have been unsuccessful. Therefore, while I note that the FT board are precluded from taking a pro-active role in the activities of FT, I propose that we take steps to resolve the dispute at board level. To this end, I set out in this letter Gunns' proposal for the termination of Contracts of Sale 917 (**CoS 917**) and 918 (**CoS 918**) and the resolution of all outstanding issues between our organisations.

I have outlined below some of the developments that have occurred in recent past to provide context for my candid assessment of the current relationship and Gunns' settlement proposal.

Take or Pay

FT has been pursuing a claim for \$8.98 million under the take or pay provision of CoS 917.

It is clear that the combination of global and domestic events has resulted in the decimation of the woodchip export market. Its impact on industry participants in Tasmania is well documented, and in fact was recognised by FT in FT's *Incoming Government Brief* dated March 2010.

We have initiated a number of meetings between the Managing Directors and senior management of Gunns and FT, seeking the cooperation and assistance of FT to address these difficult market conditions. Unfortunately, these meetings have not been constructive.

Gunns has made numerous proposals to protect Tasmania's woodchip export markets but FT management have not been receptive to these proposals, nor have they made any counter proposals. Instead, FT management have been preoccupied with extracting payment from Gunns under the take or pay penalty regime. The result has been the forced closure of sawmills and significant job losses in the industry.

Gunns has had a long and productive relationship with FT. This relationship formed the basis of CoS 917 and 918. The contracts contemplate that the parties will perform their contractual obligations in a cooperative manner, particularly in the face of tough economic conditions. Based on mutual good will, our management have sought to work with FT to resolve any issues that have arisen.

However, Gunns efforts at good faith negotiation have not been reciprocated. FT management have adopted an approach which has strained the relationship between FT and Gunns and could lead to irreconcilable conflict. The initiation of the formal dispute resolution process pursuant to CoS 917 is typical of the hostile approach taken by FT management. The parties' nominated representatives are due to exchange detailed submissions on the sum involved. I will not burden you with our views here but confirm that there are a myriad of factors (most of which are directly due to FT's conduct) which contributed to our inability to take up the volume previously contemplated.

FT's intention to enter the woodchip export market

I note your comment that Gunns has been a large customer of FT and that FT wishes to diversify its customer base. FT has the flexibility to do this under CoS 917 and 918. However, FT must also recognise FT's dominant role in the market place. FT is a large supplier to Gunns and Gunns has been a captive customer, both in terms of available native forest pulpwood and also as a result of Gunns' obligation under the take or pay provisions of CoS 917 and 918.

We have been significantly disadvantaged by FT's decision to sell directly and indirectly into China and Japan in direct competition with us. Our agreement with FT requires that we disclose our selling price into these markets to FT and it appears that FT has inappropriately used that information to undercut Gunns' prices. This has resulted in a deterioration of our market share. Further, FT now seeks to make a windfall from its direct and indirect export sales in competition to Gunns by enforcing the take or pay regime.

We also understand that senior managers of FT have been approaching some of our customers directly, seeking to establish a trading relationship with them. During the course of soliciting our customers, FT management have been making false, adverse comments about Gunns' business which inevitably jeopardises our relationship with those customers and actively dissuades any future business opportunities we may have with them. Gunns' investment in, and capacity to bring the pulp mill development to fruition, has been at the core of FT's adverse comments.

This conduct is misleading and defamatory and is causing Gunns significant embarrassment and prejudice. It is also clearly inconsistent with FT's statements of support for our construction of the pulp mill.

General performances under CoS917 and 918

Since the commencement of CoS 917 and 918, we have been faced with numerous difficulties due to FT's unwillingness and/or inability to comply with its contractual obligations. I will not recount Gunns' various complaints of defective performance and non-performance by FT but I wish to highlight one issue which has caused Gunns significant loss of market share: FT's refusal to assist Gunns obtaining FSC certification.

The ongoing campaign by ENGOs against native and old growth logging in Tasmania posed a clear risk to the brand of Tasmanian native forest woodchip. The reputation and marketability of Tasmanian native forest woodchip products is, and has always been, directly affected by FT's forestry management practices and only FT had the power to alleviate the concerns of our woodchip customers. In the circumstances, it was incumbent on FT to take steps to protect the reputation of Tasmania's woodchip export industry. As I have noted previously, its failure to do so has caused Gunns to lose export sales, resulting in the significant job losses and mill closures that the industry has suffered in recent years.

FT was aware of the damage that its forestry practices were causing to the reputation of Tasmanian woodchip products and had the opportunity to address the problem. Our Japanese customers raised concerns (both with us and FT) over a number of years about the need for our product to be sourced from FSC certified forests. Gunns worked with its customers to achieve an acceptable position but our attempts to do likewise with FT were met with indifference. Notwithstanding the parties express undertaking to adapt CoS 917 and 918 to meet changing market conditions, FT management has taken the position that they are guaranteed sales revenue under the take or pay provision and therefore have no interest in maintaining actual sales volumes.

Due to the change in market conditions, CoS 917 and 918 reflect outdated standards and do not permit us to meet our customer needs. We have now lost those customers. While I note that FT has now chosen to go down the same certification path, this decision is 18 months too late and the damage is already done.

Termination of CoS917 and 918

In light of the decimation of the market for Tasmanian native forest woodchip, and the deterioration of the relationship between FT and Gunns, it seems desirable that Gunns and FT separate. Gunns therefore wishes to terminate CoS 917 and 918, noting our agreement that construction of the pulp mill did not commence by 30 November 2010.

To the extent that FT requires formal notice, please treat this letter as notice of termination under clauses 3.3(b)(i) of CoS917 and 3.3(b)(ii) of CoS918.

While Gunns remains ready, willing and able to perform its contractual obligations under CoS 917 and 918 during the notice period, we consider that an immediate separation would be in the best interests of Gunns, FT and the Tasmanian forestry industry generally.

In particular, I am cognisant of the outstanding disputes between the parties and the further disputes that are likely to arise if CoS 917 and 918 continue in force during the notice period. Unless a commercial resolution can be reached, I fear that these disputes will ultimately result in court proceedings. I do not believe that this is the desired course for either of our organisations.

I therefore propose that CoS 917 and 918 be terminated immediately on a full release and indemnity basis in respect of any and all outstanding issues.

Settlement on this basis would immediately free up volumes for FT to utilise in pursuing the Chinese woodchip export market. Gunns is willing to assist FT develop its position in this market by providing FT with introductions to our existing customers if FT requires. At the same time, FT will receive the benefit of substantial infrastructure, worth in excess of \$200 million, established by Gunns in anticipation of harvesting pulpwood from State Forests pursuant to CoS 917 and 918.

If you are open to this proposal please let me know as soon as possible so our respective boards can give appropriate instructions to our senior executives to work together on an end date for all operations.

I look forward to your cooperation in separating the interests of our respective organisations for the mutual benefit of each.

Yours sincerely

A handwritten signature in black ink, appearing to read 'C J Newman', written in a cursive style.

Chris Newman
Chairman