

19 October 2007

Company Announcements Platform
Australian Stock Exchange Limited

ASX Release

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WAYNE CHAPMAN
COMPANY SECRETARY

ASX RELEASE

Bell Bay Pulp Mill Heads of Agreement with Forestry Tasmania

Gunns Limited has reached an in principle agreement with Forestry Tasmania, the manager of State-owned hardwood forests in Tasmania, for the long-term supply of regrowth and plantation forests for the proposed Bell Bay Pulp Mill.

The commercial terms of the agreement are consistent with the Company's feasibility assessment of the project, and in line with international benchmarks. Importantly;

- The agreement provides for a 20-year supply of 1.5 M tonnes per annum of regrowth and plantation forests to the pulp mill.
- Stumpage prices under this agreement to be paid to Forestry Tasmania will reflect the value of market pulp through a price adjustment mechanism.
- Consistent with Gunns' stated commitment, no supply from old growth forest coupes will be supplied under this pulp mill agreement.
- Pricing and commercial arrangements prior to the proposed pulp mill operations will be consistent with current supply arrangements.

All supply under this agreement will come from regrowth or plantation forests that will be regenerated as forests into the future following internationally accredited sustainable forest management principles.

Gunns Limited believes that the principles reached in this agreement reflect the benefit to the Tasmanian public from downstream processing in Tasmania compared to the current position of exporting raw woodchips. Further, the proposed pulp mill would provide security for the industry in Tasmania through this 20 year agreement.

In line with the feasibility assessment for the project, further supply requirements for the pulp mill will come from a combination of Gunns owned or managed regrowth and plantation forests, or private property regrowth and plantation forests.

The Heads of Agreement that has been signed with Forestry Tasmania is attached, with a final contract expected to be completed by the end of November 2007.

Contact:
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HEADS OF AGREEMENT
LONG TERM PULPWOOD SUPPLY AGREEMENT (“LTPSA”)

18 October 2007

Parties: Gunns Limited
Forestry Tasmania

This document reports the current agreed position of the negotiations to date for a Wood Supply Agreement for the Bell Bay Pulp Mill. It may be necessary to amend, add or omit items in the ongoing negotiations to facilitate the expectation of the parties to achieve a binding legal agreement by 30 November 2007.

1. Extent
 - The LTPSA will cover the supply to Gunns by FT of native forest and hardwood plantation pulpwood from TB coupes (being those coupes agreed between the parties as suitable for the production of pulpwood for the pulpmill). [The final agreement will identify such coupes and a process to review the identification process over time.]
2. Term
 - The term of the agreement will be 20 years commencing on 1 Jan 2008 and ending on 31 Dec 2027. The term of the agreement may be extended by the parties, on such terms as they may then agree, at any periodic review of the agreement scheduled after 1 Jan 2018.
3. Quantity
 - 3.1. Quantity of Pulpwood
 - The quantity of hardwood pulpwood to be made available to Gunns under the agreement is 1.5 M GMT log equivalent pa.
 - 3.2. Additional Quantity of Pulpwood
 - The quantity of hardwood pulpwood to be made available to Gunns under the agreement will be increased by 100,000 GMT log equivalent pa (“the Extra Quantity”) from the deemed commencement date of the pulp mill provided that Gunns commits to and executes the construction of a rotary peeled veneer mill, however, this offer will lapse if the proposed rotary peeled veneer mill is not substantially operational by 1 July 2013.
 - The increased quantity of hardwood pulpwood will not need to be segregated.
 - If:
 - in the previous 2 years Gunns has purchased at least 90% of the maximum quantity of pulpwood made available under the agreement;
 - and

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- FT has identified for any reasonable period additional quantities of peelers (provided that Gunns is at that time operating a rotary peeled veneer mill) or pulpwood from the Stumpage Zone not required to meet commitments to Gunns or other existing (or otherwise minor) customers (the latter to be limited to volume levels to be specified in the agreement, consistent with existing off take levels, currently estimated at around 300,000 GMT pa plus category 1 and 3 sawlogs plus sliced veneer logs),

then FT will offer that additional quantity to Gunns. At FT's discretion, this may be in exchange for similar volumes supplied under the agreement from the Mill Door zones. This clause also relates to additional supply that may become available in the stumpage zone in the event that existing processing plants reduce or cease operations in the long term. For the avoidance of doubt, the parties acknowledge that if Gunns entitlement to the Extra Quantity lapses then FT may deal with that Extra Quantity as it sees fit.

3.3. Grade/quality of pulpwood

- Pulpwood from native forests will be sold as a single grade, although it may be delivered in different grades to facilitate efficient processing.
- Pulpwood from hardwood plantations will be sold as a separate single grade, unless the parties agree otherwise.

3.4. Source of pulpwood

- Any State forest and other source throughout Tasmania where timber supply is controlled by FT including merchandising yards.
- The maximum quantity of pulpwood to be supplied from merchandising yards is 100,000 GMT log equivalent pa unless otherwise agreed between the parties. For the purposes of the agreement pulpwood from merchandising yards may be supplied in the form of woodchips and/or short logs at FT's discretion (although the agreement will continue to use the term pulpwood to also describe this material).

3.5. Use of pulpwood

- Gunns may process the pulpwood they purchase at such of their facilities as they so desire, provided that they keep FT fully informed of all pulpwood they receive and the quantities processed at each facility.

3.6. Use or lose

- FT can 'claw back' the smallest annual shortfall quantity in a relevant 3 consecutive year period if Gunns fails to take 85% of the maximum agreement quantity in each of 3 consecutive years – Gunns can carry over shortfall volumes within this 3 year period, up to a cap of 10% of the smallest allowable annual cut in the relevant 3 years.
- Without compromising Gunns ability to carry over shortfalls, FT may sell to other parties pulpwood made available to Gunns which Gunns either:
 - advises is not required during the planning process; or
 - does not purchase as planned.

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3.7. Ensuring supply for existing domestic processing

- Supply of Milling Timber (VQ, Cat 1, 2, 3 & 8) and existing contracts for peelers (from merchandiser logs) to the Huon and proposed Smithton rotary peeling plants and pulpwood to domestic pulp and paper plants at Wesley Vale and Boyer will be assured under the agreement.
- Harvesting operations must achieve satisfactory segregation of timber in accordance with reasonable guidelines issued by FT.
- Provision for a reasonable and transparent approach to the charging of other FT customers for harvesting and transport services, following the same principles as adopted when FT delivers timber to Gunns. A mechanism for the resolution of disputes on delivered charges will be agreed.

3.8. Determining annual supply

- Existing provisions will continue for the purposes of determining the annual supply of pulpwood ie Gunns advise requirements, then FT responds, plus a timely process to resolve any differences.
- The annual supply will be based upon the commitments in the agreement and FT's 3-Year Plan of operations (specific to supply zone level).
- The parties acknowledge that in order to meet the quantity commitments in the agreement significant quantities of hardwood pulpwood must be obtained from a range of sources including cable harvesting, thinnings and locations distant from Bell Bay.
- A matrix of quantities to be supplied in the various supply zones/harvesting will be included in the agreement and apply from the start of the agreement. This will be referred to as the Base Distribution of Pulpwood or "BDP".
- Rebalance of Pulpwood Distribution: See Clause 10.
- The 3 Year Plan of Operations will nominate a fair source of timber to Gunns taking into account the availability of timber by sources and supply commitments to Gunns and FT's other customers.
- FT will ensure that the requirements of the LTPSA will be met in the 3 Year Plan of Operations including the principle that if the annual supply to Gunns varies from the agreement maximum then the annual supply should be the basis of a fair test of whether Gunns or FT have met their obligations. Thus:
 - Annual statewide supply total must be equal or greater than the Annual Supply (the "AS") determined in accordance with the agreement. (initially 1.5 Mt, and then 1.6 Mt, if Gunns requires the total quantity to be made available by FT);
 - Annual statewide supply total from Stumpage zone to be at least 95% of total agreement stumpage zone supply pro rata to Gunns total planned offtake (ie agreement stumpage zone supply multiplied by AS divided by 1.5 Mt);

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- Annual 'inner' zone (inner zone equals Bass and Mersey Districts) total supply to be at least 85% of total agreement inner stumpage zone supply pro rata to Gunns total planned offtake;
- Annual High quality supply (by coupe in a planning context) at a statewide level to be at least 85% of total agreement high quality supply pro rata to Gunns total planned offtake] NB: this clause is dependent on conclusion of discussions regarding the practicality of sale and sampling protocols for NF pulpwood; and
- Annual Cable harvesting at a zone (stumpage, mill door zones) level to be within 25% of total agreement cable harvesting supply pro rata to Gunns total planned offtake.

3.9. Minimum supply from certain supply zones/fair share for FT contractors/fair use of cable and distant wood

- The 3 Year Plan of Operations will stipulate planned quantities in each year of the plan from particular sources consistent with the guidelines set out in clause 3.8.
- Gunns commits to obtain pulpwood consistent with the 3-Year Plan of Operations supply levels.
- The 3 Year Plan of Operations will set out minimum quantities to be obtained by Gunns in each year as follows:
 - 85% of planned quantity from Southern MD zone;
 - 85% of planned quantity from NW MD zone;
 - 85% of cable harvesting by zone (stumpage, mill door zones);
 - 85% from Merchandising yards; and
 - 85% from NF thinning.
- If minimum quantities are not achieved then Gunns must take extra quantities from the relevant source in the next year. If the quantity is not made up over any 3 year period then FT may reduce the quantity to be made available from the other sources for all future years by the extent of the shortfall.
- In times of market downturn Gunns will treat FT contractors equitably in scheduling pulpwood supply.

4. Price - See Attachment 1

4A. Transitional Arrangements

- Whilst the proposed pulp mill is expected to be operational in the second half of 2009, the parties agree that for the purposes of the agreement the mill will be deemed to commence on 1 July 2009 (the "MCD").
- until the MCD:
 - clause 3.2 (the Extra Quantity) will not apply; and
 - that part of clause 3.6 (use or lose) enabling FT to "claw back" quantity will not apply, but FT's ability to sell wood not required by Gunns to other parties will apply; and

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- pricing will be based on arrangements stated to apply until the deemed commencement date of the pulp mill.
- From the MCD and forward:
 - the agreement will operate as if the pulp mill were fully operational except for those provisions which are dependent on the specified milestones relating to the construction or operation of the pulp mill eg some conditions precedent.

5. Stumpage/mill door split (harvesting responsibility)

- Within the Stumpage Zone, Gunns will be responsible for harvest and haulage operations from native forest and hardwood plantation coupes where they are the major recipients of product. For clarity of understanding, harvest and associated roading operations would not be expected to be Gunns' responsibility for the following areas:
 - the area in Derwent Central where Norske Skog is the roading authority;
 - hardwood plantations in the Wentworth, Bradys, Forestier, Koonya and Taranna blocks which will likely be required to supply existing domestic processing industries in the south of the State;
 - silvicultural and other regrowth harvesting in the Wentworth, Bradys, Forestier, Koonya and Taranna blocks where the majority of the product is required to supply existing domestic processing industries in the south of the State;
 - softwood plantations; and
 - hardwood plantations where the ownership is wholly or partly held by a party other than FT.
- FT will deliver at mill door (or other central delivery/receival point as subsequently agreed) from the mill door zone.
- Gunns/FT will treat each other's deliveries equitably when scheduling the supply of pulpwood, particularly in times of market downturn.

6. Transition to proposed stumpage/mill door split

- The proposals involve change for some existing contractor arrangements. The parties agree to work together over the period commencing 1 January 2008 to 30 June 2008 to consider and advise on an agreed plan to achieve the transition, efficiently and with minimum disruption to contractors, as necessary to achieve the changes. Prior to the work commencing the parties will agree on firm guidelines, timetables and agreed means of resolving deadlocks.
- A date prior to the deemed commencement of the pulp mill for transition will be agreed.

7. Road responsibilities and transfers

- Unless otherwise advised by FT, Gunns will be responsible for new roading within the Stumpage Zone to coupes they plan to log. In addition at such times the parties will review ownership of the existing roads associated with the new road, and effect transfers of ownership if they agree terms. This will likely see a gradual change in road ownership across the stumpage zone.

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- The parties agree to work together to further consider and advise, by December 2008 on a plan to rationalise road assets with a view to keeping harvesting and roading with the same entity in each of the respective supply zones.

8. Gunns Plantations

- Consistent with any obligations under MIS and other legal obligations Gunns will provide FT with reasonable notice of planned harvesting of Gunns MIS hardwood plantations within the 2 mill door zones to provide FT with an opportunity to express any interest in the purchase of that wood.

9. Conditions precedent

- Construction to commence by June 2008.
- Construction not to cease for longer than 6 months.
- Mill to commence by December 2010.
- If the conditions precedent are not satisfied by the specified date (or other date as agreed) then the agreement terminates in 6 months, if either party gives notice to the other, and the parties agree to negotiate in good faith on a new agreement on such terms as they may then agree.

10. 5 yearly review of agreement

- The parties will review the operation of the agreement in the 6 month period leading up to each 5 year anniversary of the commencement date. The review will encompass any aspect of the agreement raised by either party, but will specifically address the following matters:
 - Rebalance of Pulpwood Distribution: The BDP will be recalculated by FT, after consultation with Gunns, to take into account:
 - * changes in information available regarding aspects of forest management including inventory and regulation and road access; and
 - * the offtake history of Gunns and how that might affect the distribution of the available pulpwood resource.
 - a review of the quantity of pulpwood to be made available under the agreement in all future years which will take into account:
 - * the ability of Gunns to market the quantity of pulpwood and a demonstration of their reasonable commercial endeavours to do so if Gunns claim an inability to market the quantity previously made available; and
 - * the ability of FT to supply the quantity of pulpwood and a demonstration of their reasonable commercial endeavours to do so if FT claim an inability to supply the quantity previously made available.
 - If the change in floor stumpage for either native forest or plantation pulpwood is demonstrated by Gunns or FT to be significantly different to the change in the reasonable cost of managing native forests then the parties will agree on a different adjustment of the floor stumpage and if there is no agreement within 3 months then they will refer the matter to an independent expert for determination. Guidelines for the independent expert will be:

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- * is the change in the floor price stumpage significantly different to the change in the reasonable cost of managing native forests; and
- * if it is, then what should the floor stumpage be to bring the two into line.

The parties agree to adopt the new floor price (if any) recommended by the independent expert.

- a review of the stumpage arrangements applying under the agreement which will take into account:
 - * the relative profitability of the hardwood market pulp business; and
 - * the relative profitability of managing forested lands for wood production; and
 - * the relative stumpage charged for comparative Timber in Australia and overseas; and
 - * the relative costs incurred by Gunns in obtaining pulpwood from FT.

If the Parties cannot agree by the end of the period specified, then either Party may refer the matter to dispute resolution as provided for in Clause [B11 of Attach 2].

11. Other operational and administrative matters – clauses required will cover the matters listed in Attachment 2 and any other matter agreed by the parties.

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ATTACHMENT 1 Pricing Issues

1. Products by stumpage group
 - 1.1. native forest pulpwood
 - 1.2. hardwood plantation pulpwood
 - 1.3. Plantation pulpwood will be sold and priced on a Bone Dry Tonne (BDT) basis, with annual adjustments for pulp yield. A sampling process to determine dry matter fraction to convert GMT to BDT will be agreed with continuous (weekly) sharing of results.
 - 1.4. Native forest pulpwood will be sold and priced on a Green Metric Tonne (GMT) basis with no adjustment for variations in pulp yield. NB: this clause is dependent on conclusion of discussions regarding the practicality of sale and sampling protocols related to NF wood pulp yield
2. Base stumpage
 - 2.1. \$15.75 per GMT for native forest pulpwood.
 - 2.2. \$32.00 per GMT [to be converted to an equivalent price per BDMT in the final agreement] for hardwood plantation pulpwood.
3. Base pulp prices index and other factors (if applicable) to which Base stumpage applies
 - 3.1. The base pulp price cif North Europe is agreed to be AUD800 per ADT.
 - 3.2. hardwood pulp price index

The pulp price information to be used is the “PIX INDEX VALUES” for BHKP cif North Europe published by FOEX Indexes Limited <http://www.foex.fi/> in Euros. The weekly PIX INDEX VALUES will be averaged for each relevant 6-month period and converted from Euros to AUD using the average exchange rate for the same period as published by the Reserve Bank of Australia.
4. Setting actual stumpage levels, adjustment mechanism
 - 4.1. Base stumpages will be reviewed each 6 months as per Clause 4.2 on the basis of a percentage of the proportional movement in the hardwood pulp price index. [. For movements below the base pulp price (\$800), the percentage is 75%; for movements above the base pulp price (\$800-\$900) the percentage is 175%; and for movements above \$900, the percentage is 250% of the further increase above \$900]
 - 4.2. Subject to clauses 5 and 6, stumpages will be set on 1 January and 1 July in each year calculated separately for native forests and plantation using the formula:

$$\text{NewS} = \text{BaseS} * (1 + \text{EF2} * \text{DPPI} / \text{BasePPI}) * (1 + \text{EF3} * (\text{NewPPI} - \text{BasePPI} - 100) / (\text{BasePPI} + 100))$$

where:

NewS is the new stumpage to apply from the designated date

BaseS is the base stumpage agreed by the parties in clause 2 of this Attachment

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NewPPI is the average PIX INDEX VALUES for BHKP cif North Europe converted to AUD (using the average foreign exchange rate for the same period) for the immediately preceding 6 month period prior to the designated date.

BasePPI is the base pulp price cif North Europe converted to AUD specified in Clause 3 of this Attachment.

DPPI is a factor determined as follows:

if NewPPI is greater than BasePPI by more than AUD100 then DPPI=100;
or

if NewPPI is not greater than BasePPI by more than AUD100 then
DPPI=NewPPI-BasePPI

EF2 is a factor determined as follows:

if NewPPI is less than BasePPI then EF2 = 0.75; or

if NewPPI is equal to or greater than BasePPI then EF2=1.75,

EF3 is a factor determined as follows:

if NewPPI is greater than BasePPI by more than AUD100 then EF3=2.5; or

if NewPPI is not greater than BasePPI by more than AUD100 then EF3=0.

5. Quality adjustment for plantation pulpwood

- 5.1. The parties will agree on a sampling program for pulp yield of plantation pulpwood with continuous sharing of results. Pulp yield will be expressed in percentage form to one decimal place.
- 5.2. The first full year of pulp mill operation and that part of the second year up to 31 March of plantation supply to the pulp mill will be used to establish an average pulp yield for that period referred to as the benchmark pulp yield (or "BPY").
- 5.3. After the BPY is established the sampling program will be used to establish an average pulp yield ("APYn") for each year ending 31 March.
- 5.4. Annual variations in pulp yield from the benchmark pulp yield will form the basis of stumpage variation according to an agreed formula.

6. Floor stumpage and its adjustment

- 6.1. If the calculations in clause 4 and 5 for a period result in new stumpage levels that are lower than floor stumpages, then floor stumpages will apply for the relevant period.
- 6.2. native forest pulpwood
 - 6.2.1. An initial floor stumpage for native forest of \$12.50/GMT which will be increased by 12% at year 5, by 25% at year 10 and by 40% at year 15, from the initial floor.

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6.3. hardwood plantation floor stumpage

6.3.1. An initial floor stumpage for plantation pulpwood of \$27 per GMT [to be converted to an equivalent price per BDMT in the final agreement] which will be increased by 12% at year 5, by 25% at year 10 and by 40% at year 15, from the initial floor.

7. Periodic review of stumpage

7.1. Stumpages will be reviewed at 5 yearly intervals in accordance with clause 11 of the heads of agreement.

8. Stumpage until the pulp mill starts

8.1. Until the deemed commencement date of the pulp mill the stumpage paid for pulpwood will be based on sale for woodchip export in accordance with this clause 8.

8.2. Stumpages for native forest pulpwood will be set on 1 January and 1 July in each year based on the following formula:

$$S = SF * FOB6$$

where:

S is the stumpage to apply from the relevant date

SF is an agreed factor equal to 0.175

FOB6 is the average weighted average FOB export price (converted to AUD and GMT) achieved by Gunns in the market for native forest woodchips for the 6 months immediately before the relevant date.

8.3. Unless otherwise agreed in advance, a notional floor FOB price of \$115 will apply, where sales lower than this floor are treated for the purposes of the calculation as at the floor.

8.4. For the purposes of this clause Gunns will provide a certificate from their external auditor stating and verifying the accuracy of the required woodchip price and conversion factors to AUD and GMT within 15 days of the end of each 6-month period.

8.5. The stumpage price for plantation pulpwood for the period until the deemed commencement of the pulp mill will be \$26.50 per GMT.

8.6. The provisions of clause 9 will apply for mill door deliveries by FT.

9. Mill door pricing from forest and merchandising yard

9.1. Mill door pricing will be based on a "built up" price of stumpage, road tolls, harvesting, carting, supervision and administrative costs in accordance with procedures to be agreed.

9.2. Pricing for timber from merchandising yards will be on a competitive basis in accordance with the principles in this Clause 9.2.

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9.2.1. North West Mill Door Zone (Murchison West Supply Zone): The price paid for such material will be based on the average delivered price for pulpwood supplied from the North West Mill Door Zone (Murchison West) to the designated market to which such material is to be supplied, with an appropriate allowance if material is supplied in chip form.

9.2.2. South East Mill Door Zone: The price paid for such material will be based on the assumption that 75% of the material was sourced from the Huon District and 25% from the Derwent West Supply Zone. The delivered price for such material would then be based on the average delivered price for pulpwood from those two areas to the designated market, and the assumed percentage of material coming from each area, with an appropriate allowance if material is supplied in chip form.

10. Road Tolls

- Current arrangements to apply with provision for a review of road tolls by the parties during 2008 for implementation by 1 January, 2009. That review will include consideration of whether it is appropriate to create a separate road toll for timber from hardwood plantations.

11. Take or Pay

- Take or pay for the stumpage component will apply if Gunns takes less than 85% of contracted quantity (“the TP Minimum”).
- In addition if FT has reasonably incurred additional harvest or transportation costs as a result of the Company taking less than the TP Minimum then Gunns will reimburse FT for these costs. For the avoidance of doubt any such additional costs incurred by FT can not relate to quantities which FT may have anticipated harvesting or transporting above the TP Minimum.

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ATTACHMENT 2 – List of Other Operational and Administrative Matters to be included in the final version of the agreement

- A. Operational matters [based upon existing provisions]
1. segregation
 2. harvesting
 3. specifications
 4. point of sale including delivery to rail heads
 5. wood measurement – [GMT for native forest pulpwood, BDT for hardwood plantation pulpwood]
 6. forward operational planning
 7. planning protocol previously agreed with NFP
 8. fire management
 9. clear guidelines for field staff on specifications and utilisation standards
 10. roading
 11. procedures during the commissioning period
 12. plantation issues
 13. defect and overload penalties
- B. Other administrative matters [based upon existing provisions]
1. change clause
 2. confidentiality/public document
 3. assignment
 4. invoicing and payment
 5. indemnity
 6. variation
 7. insurance
 8. default
 9. termination
 10. consequences of termination
 11. dispute resolution
 12. force majeure
 13. severability
 14. laws of the State
 15. entire agreement
 16. waiver
 17. notices

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