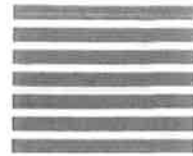


13 September 2011



Wise Lord & Ferguson



advice to advantage
Chartered Accountants

Mr T Ferrall
Deputy Secretary
Department of Treasury and Finance
21 Murray Street
Hobart TAS 7000

Dear Sir

I refer to your emails of 12 September 2011 in which you updated me regarding the most recent events in relation to the Government's offer to Gunns Limited and you instructed me to conduct a further probity review.

I have reviewed the following documents:

- Letter to Gunns Ltd from the Premier dated 26 August 2011 making an offer to settle.
- Letter to Forestry Tasmania from the Premier dated 26 August 2011 making an offer to settle.
- Meeting notes dated 30 August 2011 reflecting a meeting of representatives of the State with representatives of Gunns Ltd to discuss the State's offer.
- Letter from the Assistant Crown Solicitor dated 1 September 2011 to yourself commenting on requests from Forestry Tasmania to amend the settlement deed.
- Letter dated 2 September 2011 from Gunns Limited rejecting the State's offer.
- File note dated 6 September 2011 made by Mr G Swain of a telephone conversation between Mr G L'Estrange of Gunns Ltd and Mr M Sayer of the Premier's office.
- Letter from Tony Burke faxed from the office of the PM on 5 September 2011 indicating support for the process.
- Letter dated 7 September 2011 from Gunns Ltd returning marked up copies of the draft deed and stating that they would accept an offer of \$23M.
- Letter to yourself dated 8 September 2011 from the Assistant Crown Solicitor advising regarding the marked up deed provided by Gunns Ltd.
- Undated letter from the Premier to Tony Burke, the Federal Minister for Sustainability, Environment, Water, Population and Communities advising the current status of the negotiations and requesting his agreement.
- Letter dated 9 September 2011 from Tony Burke confirming the agreement of the Commonwealth to the proposals of the Premier in her letter.
- Undated letter to Forestry Tasmania advising that the offer of the State to Forestry Tasmania was conditional on Gunns Ltd accepting the offer made to them.
- Undated letter from the Premier to Gunns Ltd making a further offer.
- Various copies of the three Deeds of Settlement.



1st Floor 180 Collins Street Hobart TAS 7000 GPO Box 1083 Hobart TAS 7001
Tel: (03) 6223 6155 Fax: (03) 6223 8993 Email: email@wlf.com.au Internet: www.wlf.com.au

Partners: Peter Beven, Harvey Gibson, Danny McCarthy, Douglas Thomson,
Joanne Doyle, Stuart Clutterbuck, Ian Wheeler, Dean Johnson, Marg Marshall
Managers: Alicia Lais, Melanie Richardson, Nick Carter, Paul Lyons,
Simon Jones, Shaun Evans, Trent Queen

It is our view that the process reflected in the documents reviewed is a continuation of the process considered in my previous report. We therefore conclude that it is consistent with the:

- Heads of Agreement,
- Intergovernmental Agreement; and
- Legal advice provided by the Crown Solicitor and the Solicitor-General.

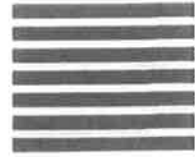
I would be pleased to discuss any of the above with you.

Yours Faithfully

A handwritten signature in black ink, appearing to read 'D.J. McCarthy', written over a circular stamp or seal.

D J MCCARTHY
PARTNER
WISE LORD & FERGUSON
CHARTERED ACCOUNTANTS

19 September 2011



Wise Lord & Ferguson



advice to advantage
Chartered Accountants

**Mr T Ferrall
Deputy Secretary
Department of Treasury and Finance
21 Murray Street
HOBART TAS 7000**

Dear Sir

Further to your email of 15 September 2011 in which you confirmed that Gunns Limited and Forestry Tasmania had accepted the offer made by the State in respect of the negotiated settlement I advise as follows.

I have reviewed the following signed documents:

- Deed between The Crown in Right of Tasmania and Gunns Limited.
- Deed between The Crown in Right of Tasmania and Forestry Tasmania. And
- Deed between Forestry Tasmania and Gunns Limited.

These documents are essentially the same as draft documents previously provided to me and accurately reflect the outcomes referred to in my letter of 13 September 2011.

I would be pleased to discuss any of the above with you.

Yours faithfully

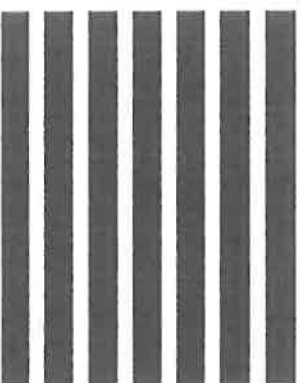
**D J MCCARTHY
PARTNER
WISE LORD & FERGUSON
CHARTERED ACCOUNTANTS**



1st Floor 160 Collins Street Hobart TAS 7000 GPO Box 1083 Hobart TAS 7001
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Review of the process for determining the recommended position of the State and Settlements to be made to Gunns Limited and Forestry Tasmania Under the Tasmanian Forests Intergovernmental Agreement.



Wise Lord & Ferguson

advice to advantage



Chartered Accountants

Introduction

We have been appointed by way of letter dated 17 August 2011 to conduct a review of the process for determining the recommended position of the State and settlements to be put to Gunns Limited and Forestry Tasmania under the Tasmanian Forests Intergovernmental Agreement.



Introduction (Cont'd)

Terms of Reference - Background

The Commonwealth and Tasmanian Governments signed the Tasmanian Forests Intergovernmental Agreement on 7 August 2011. The Agreement is designed to support the State's forest industry to transition to a more sustainable and diversified setting and to build regional economic diversification.

Clauses 22 and 34 of the Intergovernmental Agreement refer to the actions necessary and compensation payable in order to achieve key objectives as set out in clauses 19, 20 and 29 of the Agreement. These clauses make clear the requirement to extinguish wood supply contracts to the extent required to create reserved areas as referred to in clause 29.

Clause 22 of the agreement states that:

'...the State will enter a process with Gunns Ltd to ensure that a sufficient volume of native forest sawlog supply is retired to achieve the objects of clauses 17 and 29.'



Introduction (Cont'd)

Terms of Reference – Background (Cont'd)

Clause 34 states that:

“The Commonwealth will provide \$43 million to the Tasmanian Government to assist the State to facilitate the implementation of this Agreement. At least \$15 million of this funding will be used by the State to support voluntary compensable exits by saw-millers wishing to exit the industry (as set out in clause 23), and \$5 million is to be used in accordance with purposes and conditions to be agreed with the Commonwealth to support provision of information and consultation with affected parties”.

Given these prescribed allocations, there is a maximum of \$23 million available from the \$43 million to facilitate the Agreement through the extinguishment of specific wood supply contracts. The Government has agreed to give effect to the Intergovernmental Agreement by resolving the uncertainty surrounding the contract issues in relation to wood supply contracts WS917 and WS918 between Gunns Limited and Forestry Tasmania.



Introduction (Cont'd)

Terms of Reference – Background (Cont'd)

To support this process the Government has agreed to appoint a suitably qualified and registered Probity Auditor to provide advice on the process undertaken in determining a preferred State position and the appropriateness of that position in relation to resolving the complex commercial settlement of outstanding matters between Gunns Limited and Forestry Tasmania.



Introduction (Cont'd)

Terms of Reference – Scope

1. The requirements to give effect to the Intergovernmental Agreement, particularly clauses 22, 29 and 34.
2. The advice provided by the Department of Treasury and Finance on options resolving these issues.
3. The legal advice provided by the Crown Solicitor and the Solicitor-General in relation to these matters.
4. The appropriateness of the Government's proposed offer to both Gunns Limited and Forestry Tasmania.
5. In the event that an offer is subsequently made to both parties and following any negotiation, accepted by Gunns Limited and Forestry Tasmania, the appropriateness of the final executed agreement(s). Any agreement between the State and either party against the other, in relation to the relevant wood supply contracts.



Background

Through an eight month process independent of Government but funded by the Commonwealth Government, Bill Kelty facilitated a statement of principles signed by the stakeholders in Tasmanian Forestry invited to participate in the process who elected to do so. Significantly the two key operational stakeholders in forestry in Tasmania being Gunns Limited and Forestry Tasmania were not involved in that process.

The report from that process was submitted to Government in early July 2011.

On 24 July 2011 a Tasmanian Forest Agreement Heads of Agreement was signed by the Prime Minister and the Minister for the Environment on behalf of the Commonwealth of Australia and by the Premier and Deputy Premier on behalf of the State of Tasmania.

Subsequently on the 7 August 2011 the Tasmanian Forests Intergovernmental Agreement between the Commonwealth of Australia and the State of Tasmania was signed .



Background (Cont'd)

The following paragraphs of that Agreement are germane to this report.

Paragraph 8 of the Intergovernmental Agreement states:

“To give effect to this common policy intent, the Governments agree to the following three Streams of activity all of which will commence now:

- i. Stream One: Support for Workers Contractors and Communities;*
- ii. Stream Two: Protecting High Conservation Forests and Ensuring Sustainable Wood Supply; and*
- iii. Stream Three: Economic Diversification.”*



Background (Cont'd)

Paragraph 22 of the Intergovernmental Agreement states:

“Pursuant to outcome (iii) to clause 6, the State will enter into a process with Gunns Ltd to ensure that a sufficient volume of native forest sawlog supply is retired to achieve the objectives of clauses 17 and 29.”

Paragraph 29 of the Intergovernmental Agreement states:

“The State will ensure legislative protection of the areas of reserve (from the ENGO-nominated 572,000 hectares) determined by the independent verification process referred to in clause 20 above as compatible with the guaranteed timber supply.

This protection will be achieved through appropriate forms of land tenure, informed by the Independent Verification Group and compatible with other economic development opportunities, including National Parks and other Formal Reserves in the National reserve System, and possible nomination of appropriate areas for inclusion in the Tasmanian Wilderness World Heritage Area.”

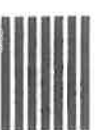


Background (Cont'd)

Paragraph 34 of the Intergovernmental Agreement states

“The Commonwealth will provide \$43 million to the Tasmanian Government to assist the State to facilitate the implementation of this agreement.

At least \$15 million of this funding will be used by the State to support voluntary compensable exits by saw-millers wishing to exit the industry (as set out in clause 23), and \$5 million is to be used in accordance with purposes and conditions to be agreed with the Commonwealth to support provision of information and consultation with affected communities.”



The Review Process

Documents Reviewed

Correspondence

- Gunns to Forestry Tasmania 1 December 2010
- Forestry Tasmania to Gunns 9 February 2011
- Gunns to Forestry Tasmania 18 April 2011
- Forestry Tasmania To Gunns 4 May 2011
- Gunns to Treasury 23 June 2011
- Forestry to Bill Kelty 29 June 2011
- Memorandum Lipman Karam to Gunns re Contracts 917 and 918 dated 28 June 2011.
- Gunns to Forestry Tasmania 30 June 2011
- Briefing note Forestry Tasmania to Minister for Energy and Resources 30 June 2011
- Gunns to the Premier of Tasmania 12 July 2011
- Briefing note Forestry Tasmania to the Treasurer and the Minister for Energy and Resources 29 July 2011

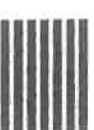


The Review Process (Cont'd)

Documents Reviewed

Correspondence

- Letter of request for advice from the Crown Solicitor to the Solicitor-General of 29 July 2011 regarding the status of Wood Supply Agreements between Gunns and Forestry Tasmania
- Advice from the Solicitor-General dated 5 August 2011 regarding the Wood Supply Contracts
- Advice from the Solicitor-General to DIER of 5 August 2011 regarding specific questions concerning the relationship of Forestry Tasmania to the Portfolio Ministers
- Email of 8 August 2011 from the Solicitor General to Mark Sayer
- Gunns to ASX of 8 August 2011 re suspension of trading
- Email from the Solicitor-General to the Crown solicitor re legal advice dated 8 August 2011

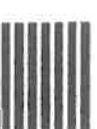


The Review Process (cont'd)

Documents Reviewed

Correspondence

- Email to Forestry Tasmania from the Crown solicitor dated 11 August 2011
- Email from the Crown Solicitor to Secretary of the Treasury of 11 August 2011
- File note from Forestry Tasmania re the draft agreement dated 12 August 2011



The Review Process (Cont'd)

Advice and Agreements

- Tasmanian Forest Agreement – Heads of Agreement 24 July 2011.
- Tasmanian Forests Intergovernmental Agreement 7 August 2011.
- Minute to the Treasurer of recommendations with respect to the Intergovernmental Agreement Payments under clause 34 of 11 August 2011.

Draft Agreements

Draft deed between the Crown and Forestry Tasmania.

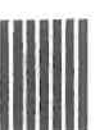
Draft deed between the Crown and Gunns.



The Review Process (Cont'd)

Parties Interviewed

- Mr Martin Wallace, Secretary of the Department of Treasury and Finance
- Mr Tony Ferrall, Deputy Secretary of the Department of Treasury and Finance
- Mr Leigh Sealy, Solicitor General
- Mr Grant Kench, Acting Crown Solicitor
- Mr Greg Johannes, Deputy Secretary of the Department of Premier and Cabinet
- Mr Rhys Edwards, Secretary of the Department of Premier and Cabinet



The Review Process (cont'd)

Process

In completing this review I have taken the following steps.

1. Read all of the documents provided so as to understand the transaction and also the process by which the transaction was conducted.
2. Interviewed each of the parties above regarding the transaction and in particular regarding the process by which the transaction was completed.
3. In the context of 1 and 2 above I have considered in particular the issues detailed at 1 to 4 of the Scope.
i.e.
 - The requirements to give effect to the Intergovernmental Agreement , particularly clauses 22, 29 and 34.
 - The advice provided by the Department of Treasury and Finance on options resolving these issues.
 - The legal advice provided by the Crown solicitor and the Solicitor-General in relation to these matters.
 - The appropriateness of the Government's proposed offer to both Gunns Limited and Forestry Tasmania.



Chronology of the Transaction

The Cogent Facts of the Transaction

1. Heads of Agreement.

The Heads of Agreement is the foundation stone of the restructure process providing the necessary support for the transaction.

2. Legal Opinions.

The legal opinions define that there is a real legal dispute and its scope. The essence of the advice is that if a negotiated settlement is not arrived at through the current process, but left to Gunns and Forestry Tasmania to resolve, there will be protracted and expensive legal action which will be resolved long after this opportunity for restructure has passed. Without resolution of the legal dispute streams one, two and three of paragraph 8 of the Intergovernmental Agreement cannot proceed.



Chronology of the Transaction

The Cogent Facts of the Transaction

3. Intergovernmental Agreement.

This confirms the agreement between the State and the Commonwealth as to what is to be achieved and how it is to be funded. The pathway provided by clauses 6 (iii), 22, 29 and 34 provides the mechanism for removal of the legacy issues between Gunns and Forestry Tasmania.

4. Implementation of the Intergovernmental Agreement.

The advice of Treasury to the Treasurer of 11 August 2011 is a succinct summary of the possible ways to implement the agreement.



Treasury Options Paper

I will not attempt to summarise the Treasury options paper here. I will deal with it in the context of the four issues included in the scope.

1. The requirements to give effect to the Intergovernmental Agreement , particularly clauses 22,29 and 34.

The Treasury advice concludes that to give effect to the Intergovernmental Agreement the existing contractual arrangements between Gunns and Forestry Tasmania needs to be extinguished before the Agreement can proceed.

2. The advice provided by the Department of Treasury and Finance on options resolving these issues.

The Treasury advice provides four options available. They recommend option 2 as the only option which would see an immediate extinguishment of the existing contractual arrangements between Gunns and Forestry Tasmania.



Treasury Options Paper (cont'd)

3. The legal advice provided by the Crown Solicitor and the Solicitor-General in relation to these matters.

The legal advice confirms that there are disputed contractual arrangements between Gunns and Forestry Tasmania and these need to be extinguished if the Agreement is to proceed in a timely manner. Paragraph 8 requires streams one, two and three to commence now. This cannot happen if the legal dispute between Gunns and Forestry Tasmania has not been extinguished.

4. The appropriateness of the Government's proposed offer to both Gunns Limited and Forestry Tasmania.

The Treasury advice concludes that there is no right answer with respect to what is required to extinguish the existing contractual arrangements. They have recommended to split the available money equally between the parties.



Conclusion

It is our view that the process through which the Secretaries of the Departments of Treasury and Finance and Premier and Cabinet reviewed and concluded on the transaction is guided by and is consistent with the:

- Heds of Agreement,
- Intergovernmental Agreement ;and
- Legal advice provided by the Crown Solicitor and the Solicitor-General.

The recommendation in the minute to the Treasurer is the only one which will give finality to the matter and enable Government to proceed with its other objectives and the timeframe set out in paragraph 8.

