



December 24, 2012

VIA PERSONAL DELIVERY

Mr. T. Sariiev
Chairman of the State Commission
The State Commission
195 Abdumomunov Street
Bishkek, Kyrgyz Republic
720040

Dear Mr. Sariiev,

On behalf of Centerra Gold Inc. (“Centerra”) and Kumtor Gold Company CJSC (“KGC”), I acknowledge receipt of the draft report of the Kyrgyz Republic State Commission on Kumtor – Legal Working Group (the “Report”) received in mid-November 2012. Centerra and KGC would like to respond to the conclusions and recommendations raised in the Report.

Please find below our responses to the Report. For convenience, we have referred generally to the allegation and the applicable page number in the English translation of the Report, which page number may be slightly different than in the original Russian version of the Report. Please further note that, as more fully described below, we will not be responding on any allegations or conclusions that relate to matters that occurred prior to June 6, 2009.

A. The Pre-2009 Claims in the Report Have Been Irrevocably Released by the Kyrgyz Republic Pursuant to the Termination of Arbitration Proceedings and Cannot Be Revived Now

As a preliminary matter, we note that all the allegations raised in the Report that relate to matters prior to June 6, 2009 have been previously raised and have been discussed and debated at length. Indeed, Centerra previously commenced international arbitration proceedings against the Kyrgyz Republic Government (the “Government”) on March 8, 2006 to resolve these issues. Over the next three years, the parties engaged in arbitration proceedings and held a series of discussions and negotiations in an attempt to resolve their disputes. Under the auspices of the international arbitration proceedings (Permanent Court of Arbitration Case N° AA278) the parties finally reached a settlement on April 24, 2009, when the parties entered into the Agreement on New Terms (“ANT”), a framework agreement for the resolution of all then-existing disputes concerning Kumtor. Shortly thereafter, the parties entered additional agreements fulfilling the terms of the ANT and finalizing the settlement, including a release agreement executed on June 6, 2009 (“Release Agreement”), as well as a

Settlement Agreement signed the same day pursuant to which the parties agreed to terminate the arbitration proceedings. On June 29, 2009, in view of the agreements between the parties releasing and settling all claims, the arbitrator issued a termination order bringing the arbitration to a close.

Pursuant to the terms of the Release Agreement – which was entered into between and among Centerra, KGC, Kumtor Operating Company CJSC (“KOC”), Cameco Corporation (“Cameco”), Cameco Gold Inc. (“Cameco Gold”), Kumtor Mountain Corporation (“KMC”), the Government and Kyrgyzaltyn JSC (“Kzn”) – the parties agreed to release each other from any claims, including any legal, tax and fiscal matters, in respect of any matter arising or existing prior to June 6, 2009, whether such matters were known or unknown as of June 6, 2009 (except for unknown environmental damages). The parties also agreed never to arbitrate or litigate, directly or indirectly, on any of the matters so released. All of these claims thus cannot be pursued, and Centerra respectfully submits that an arbitrator will summarily dismiss them. (We note as well that the UNCITRAL Arbitration Rules, which will apply in any arbitration of these claims, provide that the costs of arbitration, including legal fees, are to be borne in principle by the losing party.)

In the spirit of cooperation, however, Centerra, KOC and KGC have nonetheless reviewed the various pre-2009 allegations raised in the Report and have provided the general responses below but expressly note that at all times, Centerra, KOC and KGC are relying on the provisions of the Release Agreement, which as noted above was executed in connection with a duly convened and conducted international arbitration proceeding settled as contemplated by the rules of the arbitration.

- Allegations regarding the original master agreement between the Government and Kyrgyzaltyn (of the first part) and Cameco made as of the 4th day of December 1992, as restated and amended (as the case may be) on January 16, 1993, September 3, 1993, and May 31, 1994 (collectively, the “Master Agreement”) being improper and in violation of Kyrgyz Republic (KR) law are unfounded. The Master Agreement and the amendments thereto (and the operating agreement between KGC and KOC) were reviewed and approved by the Government.
- The development of the Kumtor mine was carried out in reliance upon the Kumtor Feasibility Study and Government Decree #895 of December 28, 1994. The development was subject to all required expertise and endorsements, and was in compliance with the Concession Agreement and applicable legislation in effect at such time.
- The restructuring of the Kumtor Project which was finalized in 2004, and the initial public offering (“IPO”) of Centerra common shares was negotiated at arm’s length among the parties, with the assistance of experts on all sides, including Standard Bank of London and Blakes, Cassel and Graydon for the Government and Kzn. The resulting restructuring agreements were all reviewed by the Government and were supported by legal opinions from the Kyrgyz Republic Ministry of Justice.
- The restructuring of the Kumtor Project also provided the Government and Kzn with

significant benefits, including liquidity of their equity interest in the Kumtor Project. By virtue of the restructuring of the Kumtor Project into Centerra (along with other gold assets held by Cameco), and the subsequent IPO, Kzn was able to monetize on a portion of their equity interest in Kumtor; Kzn participated in the IPO and sold 7,500,000 common shares for gross proceeds of C \$116,250,000 (approximately US \$87,000,000 using the exchange rate as of June 30, 2004).

- Lastly, we note that the restructuring of the Kumtor Project provided Kzn with the benefits of Centerra's other gold producing mine, namely the Boroo mine located in Mongolia. In particular, we note that from 2006-2008, the Boroo mine was significantly more profitable than the Kumtor mine due to Kumtor's high costs. During these years, cash from the Boroo operations helped to fund the Kumtor operations, at one point providing funding of approximately US\$115 million.

B. The Post-2009 Claims in the Report Are Based on Allegations that are Factually Inaccurate and Contrary to International Law

- (i) The 2009 Restructuring Was Substantively Fair, Legally Valid and Duly Authorized in Accordance with the Laws and Constitution of the Kyrgyz Republic

Contrary to the implication of the Report, the 2009 Restructuring was eminently fair to the Kyrgyz Republic. Indeed, as a result of the ANT and related agreements undertaken to implement the restructuring of Kumtor, the Kyrgyz Republic (including Kzn, a company controlled by the Government) received very substantial economic and non-economic benefits. These include:

- (a) a new tax regime that was requested by the Government and which heavily favoured the Kyrgyz Republic, including a catch up tax payment of US \$20,692,921 to reflect the application of the new tax regime for calendar year 2008;
- (b) an additional cash payment of US \$1,750,000;
- (c) debt forgiveness of US \$4,400,000 in debt owed by the Government to KGC,
- (d) the issuance and transfer of additional Centerra shares to Kzn; and
- (e) other economic and non-economic benefits, including greater ability to review and approve mining plans, an additional seat for a nominee from Kzn on the Centerra board of directors and, of course, termination of the arbitration proceedings.

Moreover, the process of bringing the ANT into law consisted of several steps specifically designed to ensure the full participation of the Government and Kyrgyz Republic Parliament (the "Parliament" or "Jogorku Kenesh"), including the following:

- (1) On April 24, 2009, the Kyrgyz Republic Prime Minister signed the ANT, and the Kyrgyz Parliament ratified the ANT and draft legislation authorizing its implementation by Law No. 142 of the Kyrgyz Republic, "On Ratification of the Agreement on New Terms for the Kumtor Project" (the "ANT Law");

- (2) In connection with the ratification of the ANT, the Kyrgyz Parliament also adopted two related laws, Law No. 143 of April 24, 2009 of the Kyrgyz Republic, “On Modification and Amendment of the Tax Code of the Kyrgyz Republic” (the “Tax Code Law”) and Law No. 175 of April 30, 2009 of the Kyrgyz Republic, “On Modification and Amendment of Certain Legislative Acts of the Kyrgyz Republic” (the “Amendment Law”) (the ANT Law, Tax Code Law and Amendment Law are referred to collectively herein as the “Kumtor Laws”);
 - (3) the Kyrgyz Government engaged in a comprehensive expertization process, which involved analysis by and consultation with various state agencies, including the Kyrgyz Republic State Agency for Geology and Mineral Resources, and advice regarding the proposed transactions from the prominent London-based international law firm Allen & Overy as well as the Canadian law firm of Blakes, Cassels and Graydon LLP;
 - (4) On June 2, 2009, the Constitutional Court of the Kyrgyz Republic issued a decision dismissing a challenge to the Kumtor Laws, and upholding their validity; and
 - (5) On June 9, 2009, pursuant to a requirement of the ANT, the Ministry of Justice, after reviewing, among other things, the ANT, the Kumtor Laws and the decision of the Constitutional Court, issued an opinion that also confirmed the validity and binding effect of the ANT and related agreements.
- (ii) Under Public International Law, Agreements of Prior Governments Are Binding on Successive Governments

Many of the allegations in the Report appear to rely on the premise that the current government of the Kyrgyz Republic should not be responsible for obligations undertaken by prior governments. Under public international law, however, it is well established that “the legal rights and responsibility of states are not affected by changes in the head of state or the internal form of government.” Ian Brownlie, *Principles of Public International Law* 80 (5th ed. 1998). Arbitral tribunals have reached the same conclusion, even in cases in which the argument was made that a prior government was corrupt. E.g., *Sistem Muhendislik Sanayi Ve Ticaret A.S. v. Kyrgyz Republic*, ICSID Case No. ARB(AF)/06/1, Award of 30 September 2009 (noting that it would be problematic for a state to rely on the corruption of its own officials to preclude the admissibility of an investor’s claim) (summary at <http://cisarbitration.com/2012/07/23/icsid-tribunal-kyrgyzstans-judiciary-decisions-amounted-to-expropriation/>). Accordingly, a national government presently in power must recognize the obligations and agreements undertaken by prior governments that acted as authorized representatives of that state. Kyrgyzstan has been a member state of the United Nations since February 3, 1992, and the Government of Kyrgyzstan that was in power in 2009 – when Centerra entered into the ANT and related agreements with the Government – was the duly authorized representative of the Kyrgyz Republic, recognized not only by the United Nations but also by all 192 member states then admitted to the United Nations. Thus, it is clear that the Kyrgyz Government in 2009 had the full authority to bind – and did bind – itself and successive governments of the Kyrgyz Republic by the acts and contracts it entered into, including the ANT and related agreements, and those obligations remain applicable to this

day notwithstanding any change in the head of state or allegations of malfeasance, criminal activity or negligence on the part of previous governments.

The specific responses to matters related to after June 2009 are as follows:

Allegation #1 (pages 15) regarding the violation of the Kyrgyz Republic (“KR”) Tax Code due to the introduction of the new tax regime for the Kumtor Project .

This allegation is not against Centerra or Kumtor.

In any case, the Tax Code of the Kyrgyz Republic was amended by the Jogorku Kenesh on January 1, 2009 to provide that if an agreement is executed by the Government and ratified by the Jogorku Kenesh, as was the case here with the ANT, then the tax provisions in that agreement apply notwithstanding other tax legislation of the KR.

This was entirely proper because, as the Constitutional Court noted in rejecting a similar argument that the new tax regime was invalid, “Amending or modifying respective laws, including the Tax Code, is the prerogative of” the Kyrgyz Parliament (the Jogorku Kenesh).

Allegation # 2 (page 15) regarding the Government exceeding its authority to amend the Tax Code, and that the Jogorku Kenesh does not have having the authority to ratify the ANT and the project agreements (because they are not “international agreements”).

This allegation is not against Centerra or Kumtor.

In any case, the ANT and amendments to the tax law were approved by the Government and ratified by the Parliament, and the Constitutional Court denied a challenge on precisely these grounds. The Ministry of Justice confirmed that that decision was a valid and binding decision issued pursuant to the Constitution and other legislation of the KR. In a system based on laws, investors and others must be able to rely on such decisions.

Specifically, the Government presented the ANT and draft legislation authorizing its implementation to the Kyrgyz Parliament for ratification, and on April 30, 2009, the Kyrgyz Parliament ratified the ANT by Law No. 142 of the Kyrgyz Republic, “On Ratification of the Agreement on New Terms for the Kumtor Project” (the “ANT Law”).

The Constitutional Court subsequently denied a challenge to the validity of the ANT based on the argument that the ANT was not properly approved by the Kyrgyz Government, holding that the Jogorku Kenesh “expressed its approval by adopting the Law on ratification of this Agreement.” Similarly, the Court rejected the argument that the new tax regime was invalid, stating that “Amending or modifying respective laws, including the Tax Code, is the prerogative of” the Kyrgyz Parliament.

This was confirmed by an opinion from the Ministry of Justice concluding that “Each of the ANT Law, the Amendment Law and the Tax Code Law has been duly adopted by the

[Kyrgyz Parliament] of the Kyrgyz Republic pursuant to the procedures established by the Legislation” and, to the extent there was any conflict between the rules set forth in the ANT or the Restated Project Agreements and the rules of legislation promulgated by the Kyrgyz Republic, “then the rules provided for by the Restated Project Agreements shall apply in relation to the matters governed thereby.”

Allegation #3 (page 15) regarding the new tax regime for Kumtor violating the Constitution because it was dictated by the interest of one private company despite the KR Constitution providing that the State and its bodies serve all society.

See our response to Allegation 1 and 2.

Allegation #4 (page 15) regarding the constitutional court.

The allegation is hard to understand, but it is not against Centerra or Kumtor.

In any case, as noted above, the Ministry of Justice confirmed the validity of the opinion of the Constitutional Court, stating “The Constitutional Court Decision has been duly issued by the Constitutional Court of the Kyrgyz Republic in accordance with the Legislation and is a valid and binding decision of the Constitutional Court of the Kyrgyz Republic pursuant to the Constitution of the Kyrgyz Republic and the other Legislation”

Allegation #5 (page 16) regarding the ability of the Government to write off bad debt.

See response to Allegation #4 above. Specifically, the Constitutional Court found that “[a]mending or modifying respective laws, including the Tax Code, is the prerogative of” the Kyrgyz Parliament.

Allegation #6 (page 17) regarding the Restated Investment Agreement and that it contravenes the KR Constitution because it: (A) restricts the ability of the Government to act on certain matters, including expropriating assets; and (B) requires the Government to make all efforts to cancel, annul or in some other manner stop any action of a state official that contradicts the Restated Investment Agreement (which therefore restricts the authority of other Government bodies and agencies).

This allegation is not against Centerra or Kumtor.

First, we note that The Law of the KR “On Investments in the KR” (the “KR Investment Law”) specifically contemplated the KR Government entering into international agreements such as the Restated Investment Agreement. We do not see any allegation that the KR Investment Law itself (on which many investors in the Kyrgyz Republic have relied) is unconstitutional.

We note that the Restated Investment Agreement was reviewed and approved by the Government, as was the ANT, which specifically contemplated the Restated Investment Agreement and the provisions recited therein. And, as noted above, the Constitutional Court

upheld the constitutionality of the ANT in a decision which was confirmed by an Opinion of the Ministry of Justice.

With respect to the particular allegations raised regarding expropriation, we note that the language in the Restated Investment Agreement reflects the language in Article 6 of the KR Investment Law. Specifically, Article 6 states that investments will not be subject to expropriation (nationalization, requisition, or other equivalent measures, including actions or omissions by the government bodies of the Kyrgyz Republic which have the effect of forcing the withdraw of investor's funds or in depriving them of an opportunity to gain on the investments' results). It goes on to provide that if expropriation does occur, the investor is entitled to reparation equivalent to the fair market value of the expropriated investment, including lost profit and that the fair market value does not reflect any changes in the value of the investments caused by the expropriation itself. These same concepts are stated in the Restated Investment Agreement.

Next, with respect to the argument that the Restated Investment Agreement requires the Government to make all efforts to cancel, annul or in some other manner stop any action of a state official that contradicts the Restated Investment Agreement, we note that the argument appears to be based on a mischaracterization of the Government's obligation. Section 8.2 of the Restated Investment Agreement states:

“If any Public Official shall take any action that conflicts with this Agreement or the Restated Concession Agreement, or has the effect of denying Investor, KGC or KOC of an investment benefit to which it is entitled hereunder or thereunder, the Government shall use its best efforts to reverse, annul or otherwise terminate or remedy such action.”

Nothing in the “best efforts” clause purports to give the Government power to take action that it is not otherwise authorized to take. To the contrary, the clause clearly states that the Government should use its “best efforts,” which by its very definition means that the Government can only act within its powers.

Allegation #7 (page 21) regarding the Restated Concession Agreement being granted in violation of KR legislation.

We disagree with this argument. As discussed previously, the ANT and the project agreements, including the Restated Concession Agreement, were approved by the Government and Parliament, and subject to a decision of the Constitutional Courts and an opinion of the KR Ministry of Justice.

Allegation #8 (page 19) regarding the cancellation of the previously issued temporary land use rights, and the conclusion that Kumtor currently has no land now for exploration and development.

The Restated Investment Agreement guarantees Kumtor all necessary permits and approvals (see Section 7.1(a)) as well as access to the project site, including surface lands, as is

necessary for the operation of the project (see Section 7.1(c)).

During a visit to the project on July 6, 2012, Prime Minister Babanov confirmed that the purported cancellation of a prior decree granting surface rights would have no impact on or limit in any way the activities or operations of the Kumtor project.

On October 11, 2012, Centerra and Kumtor wrote a letter to the Government, the State Geology Agency under the Government and the Jeti-Oguz district department of land planning and registration, taking note of the Government decrees purporting to cancel previously issued land rights for a land plot of 26,400 .8 ha. In the letter, Centerra and Kumtor drew attention to the various obligations of the Government under the Restated Investment Agreement, including the duty to ensure access to land plots to enable the project delivery and to not take actions which would lead to the termination of rights or to stoppage of production, and the duty to do its best to discontinue any actions taken by government officials that would prevent Centerra and Kumtor from its rights under the Restated Investment Agreement. To this end, Centerra and Kumtor requested that the Government and the Jeti-Oguz Land Office rectify that matter.

Please contact me if you have any questions regarding our responses to the Report.

Sincerely,

Frank Herbert
General Counsel
Centerra Gold Inc.

Copy His Excellency, Jantoro Satybaldiyev, Prime Minister of the Kyrgyz Republic
Almambet Shykmamatov, Kyrgyz Republic, Minister of Justice
Ian Atkinson, President and CEO, Centerra Gold Inc.
Michael Fischer, President, Kumtor Operating Company CJSC