



February 20, 2013

DELIVERED BY HAND

WITHOUT PREJUDICE

To: The State Commission to inspect and review Kumtor compliance with standards and requirements on rational use of natural resources, environmental & operational safety, and community social protection (the “State Commission”)
Attention: Mr. T. Sariev, Chairman of the State Commission

To: His Excellency, Jantoro Satybaldiyev, Prime Minister of the Kyrgyz Republic

Re: State Commission Report – Social and Economic Analysis of the Kumtor Project

Dear Sirs and Mesdames:

On behalf of Centerra Gold Inc. (“Centerra”) and Kumtor Gold Company CJSC (“KGC”), I acknowledge receipt of the final report of the Kyrgyz Republic State Commission on Kumtor – Social and Economic Working Group (the “Report”) received on January 18, 2013. We have set out below our responses to allegations raised by the working group in the Report, organized with reference to the Summary and Recommendation sections of the Report. In addition to this written response, we look forward to meeting with the working group to expand on the points made in the letter.

Preliminary Matters

Release Agreement

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 (the “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, which is not applicable in the present circumstances). 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 allegations that relate to matters prior to June 6, 2009 which are raised in the Report and have provided the general responses noted below. However, we note that, 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.

Actions of Prior 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.

Responses to Report

Conclusion Section

Preamble to Conclusion – Allegations against Centerra and Kumtor management

The Report alleges that the Kumtor Project has been mismanaged. We disagree. We believe that the project has been managed in accordance with good international mining practices. Operational decisions are made with a view to maximizing Kumtor's production over the life of the mine while ensuring the health and safety of our employees, and minimizing impacts on affected communities and the environment. We would welcome the opportunity to discuss this matter further with members of the State Commission working group on social and technical matters.

Summary Point #1 – Allegations relating to the 1992 Master Agreement

The Report makes allegations regarding the original master agreement between the Government and Kyrgyzaltyn (of the first part) and Cameco (of the second part) 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 one-sided and against the interest of the Kyrgyz Republic ("KR"). In particular, the Report refers to problems associated with the management system of the Kumtor Project, the manner of project funding, and the over-run of project development costs of approximately US\$175.6 million.

At the outset, we point out that the Master Agreement and the arrangements contained therein on these matters were reviewed and approved by the KR Government. With respect to the management of the Kumtor Project, the Master Agreement set out the authority of the management committee and the board of directors, including the composition of each body. In addition, the Master Agreement contemplated that the development of the Kumtor Project would be by loans from international financial institutions (ultimately, loans were obtained from such international financial institutes as the International Finance Corporation and European Bank for Reconstruction and Development), and would include security being granted by each shareholder. The Master Agreement also expressly contemplated Cameco providing a subordinated interest-bearing loan on commercially reasonable terms. Given that these matters were all expressly provided in the Master Agreement, which was approved by the Government, we do not understand the basis of the working group's allegation.

Next, we note that 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. Construction costs for the development did overrun initial projections by approximately

US\$176 million, but the cost over-runs were previously audited and resolved by another Government Commission in 1997/1998. Furthermore, cost over-runs in the mining industry, both historically and currently, are not unusual. In any event, the decision to accept cost over-runs was made by KGC (at that time owned by Kzn and Cameco) and any concerns relating thereto have been released pursuant to the Release Agreement.

Summary Point #2 – Allegations relating to the 2003-2004 Restructuring Agreement

The Report refers to the 2003-2004 restructuring as being unfair to the interests of the KR. We note that the restructuring of the Kumtor Project which was finalized in 2004, and the initial public offering (“IPO”) of Centerra common shares, were negotiated at arm’s length among the parties, with the assistance of experts on all sides, including Standard Bank of London and Blake, Cassel and Graydon LLP (a Canadian law firm) for the Government and Kzn. In particular, the value of the assets being contributed to Centerra, the conversion of corporate loans from Cameco into Centerra shares, and the issuance of Centerra shares to other parties, including in relation to the outstanding subordinated loans from International Finance Corporation and the European Bank of Reconstruction and Development were all the subject of extensive negotiations among all parties and their respective experts. Allegations that certain assets, including the Kumtor Project, the REN Project and shares in AGR Limited, were undervalued or overvalued are unfounded. The Kyrgyz Republic Government and Kyrgyzaltyn had access to all technical data, exploration results and other engineering, operating and other financial information relating to the properties in the control of Cameco and Centerra. The Report contains no evidence that assets being contributed to Centerra were undervalued or overvalued, or that there was any impropriety with respect to the provision of data, results and other information by Cameco and Centerra. As noted above, each party was represented by independent experts to assist, among other things, in the assessment of the valuation. The restructuring agreements were reviewed and approved by the Government, and supported by legal opinions from the Kyrgyz Republic Ministry of Justice. In any event, any allegations of economic loss and improper valuation were discussed and resolved by the Government, Centerra, KGC, KOC and Cameco in 2009 with the Restated Project Agreements, which fully and finally resolved all issues in relation to the Kumtor Project, and are covered by the Release Agreement.

The Report also discusses the involvement of a company, Eckerd, and its role in the Kumtor Project restructuring. The Report implies an indirect connection between Eckerd and Cameco and a corrupt element in their activities. There is no evidence provided of any improper activity and no specific allegation made. Centerra has no knowledge of any impropriety. Centerra takes all allegations of this type very seriously. Centerra has adopted procedures and policies throughout its organization to combat against corruption and other improper activity, and to create an environment that is transparent and compliant with applicable legislation and principles against corruption. We ask that the State Commission provide Centerra with all information which may relate to improper activity relating to Centerra or the Kumtor Project, in order for us to fully investigate the matter.

With respect to the transactions for US\$4 million and US\$11 million, these are described in

Centerra's prospectus dated June 22, 2004 for the IPO (see page 98 for the discussion on the restructuring). Centerra had no concurrent knowledge of communications between or contracts entered into between Eckerd and the KR Government and Kzn. These are all questions to be asked of Kzn. None of Centerra, KOC or KGC had any agreements with Eckerd.

We understand that Cameco loaned US\$4 million to the Ministry of Finance of the KR Government in September 2002 as an advance of taxes. As the Report notes, this US\$4 million debt was not repaid to Cameco by Eckerd. Instead, the loan was assigned to Kzn as contemplated in the Restructuring Agreement dated December 31, 2003. In addition, the Restructuring Agreement also contemplated a cash transfer of US\$11 million by Centerra to Kzn. The assignment of the US\$4 million loan payable by the Ministry of Finance and the transfer US\$11 million, in both cases to Kzn, was to compensate Kzn for its share of insurance claim proceeds relating to a July 2002 pit wall collapse, which claim was submitted to the insurance company but not yet paid at the time of the Restructuring Agreement.

At the closing of the Restructuring Agreement transaction, the US\$11 million was transferred by Centerra to Kzn's bank account with Standard Bank pursuant to a written direction signed by Kzn. Centerra is not aware of the use of such funds by Kzn. Allegations in the Report that Centerra was involved in the transfer of such funds to Eckerd, directly or indirectly, are unsupported by any evidence provided in the Report.

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 initial public offering of Centerra, Kzn was able to monetize a portion of its 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 indirect equity ownership in 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.

Summary Point #3 – Allegations relating to the 2009 Project Agreements

In this allegation, the Report references the concessions received by the KR Government and Kzn as part of the Restated Project Agreements, but questions whether they were sufficient given that Kumtor received an expanded concession area and an increase in gold reserves for 40.43tons.

First, we point out that as part of the Restated Project Agreements, the KR Government and Kzn received significant benefits including (i) the transfer to Kzn of 25,300,000 common shares in Centerra; (ii) the issuance from treasury to Kzn of 18,232,615 additional shares,

which together with the 25,300,000 shares transferred, increased Kzn's shareholding interest from 15.7% to 33.1%; (iii) a cash payment to the KR budget of US\$1,750,000; (iv) the adoption of a new tax regime, which was at the request of the KR Government, effective January 1, 2008 (ie: made retroactive), (v) a catch up tax payment of US\$20,692,921 representing the difference between applying the then-current stabilized tax regime to Kumtor and the newly-agreed to tax regime for Kumtor for the 2008 calendar year; (vi) forgiveness of US\$4,400,000 million debt owed by the Government to KGC; and (vii) an additional nominee (for a total of 2 nominees) to the Centerra board of directors, so long as Kzn's ownership interest in Centerra was at least 10% (the right decreases to one nominee if Kzn holds less than 10% interest but more than 5%).

We note that the 2009 Project Agreements were negotiated at arm's length, reviewed and approved by the Government and Parliament, and supported by a decision of the Constitutional Courts and a legal opinion by the Kyrgyz Republic Department of Justice.

Furthermore, the Report also incorrectly states that as part of the Restated Project Agreements, Kumtor was given a land parcel of 240 hectares of the Sary-Ertash Nature Reserve. On the contrary, at the time of completion of the Restated Project Agreements, Centerra, KOC and KGC received written confirmation from the Government (signed by Prime Minister I.V. Chuddinov) that no part of the expanded concession area was part of the Sarychat-Ertash National Park.

Recommendations Section

Recommendation #1 – Change of the Kumtor Project management at Centerra, KGC and KOC levels

The Report argues that having only two Kyrgyz directors on the board of directors of Centerra unduly restricts KR's interests with regard to the representation in Centerra's board of directors and management, and requests additional representation in various committees of the board of directors. The Report also makes recommendations regarding reforms at Kzn, which we will not comment upon.

Kzn's right to representation on Centerra's board of directors is expressly provided in the restated shareholders agreement between Centerra and Kzn dated as of June 6, 2009 (the "Restated Shareholders Agreement"). The agreement provides that so long as Kzn holds 10% or more of Centerra's common shares, Centerra would include in its proposed slate of directors nominated for election at each annual meeting or special meeting at which directors are to be elected two board nominees designated by Kzn, at least one of whom must be independent of the Government, and if Kzn owns less than 10% but more than 5% of Centerra's outstanding shares, Centerra would include in its proposed slate of directors one nominee of Kzn, who is not required to be independent from the Government. This agreement is a valid and legally binding obligation of the KR Government and Centerra. We do not see a reason to change the agreement. The agreement was negotiated at arm's length

and was reviewed and approved by the KR Government and Parliament, and supported by a decision of the Constitutional Courts and a legal opinion by the KR Ministry of Justice.

The Report also discusses KGC and KOC, noting that the two should be merged into one company and that Kyrgyz representatives should be placed into management roles, including at the level of Vice Presidents and the President. The issue of merging KGC and KOC has been reviewed in the past, including by the board of directors of Centerra which, at such time, included three representatives from the Kyrgyz Republic. Following such review, it was determined that the operations of the Kumtor project would be transitioned from KOC to KGC, such that over time KOC would cease to have a role to play and could be wound up or dissolved at such time. The process is being carried out in a manner that does not unduly interfere with the operations of the Kumtor Project, and preserves the interests of the Kumtor mine and the integrity of the contracts, permits, approvals and other obligations. This transition process is currently underway, and we would be happy to discuss this matter further with members of the working group.

With respect to the request for Kyrgyz nationals in the management of KGC and KOC, we note that the project currently employs dozens of Kyrgyz nationals in positions of management responsibilities. Positions at Kumtor are filled based on experience, education and other qualifications, not based on nationality. The KR Law on Investments expressly gives investors the freedom to appoint managers as it determines, which is also reflected in section 2.2 of the Restated Investment Agreement which provides that KOC and KGC have the right to enter in such arrangements for management and operation of the Kumtor Project as it sees fit, and section 7.1 which refers to the Investment Law and its rights to non-interference and operational independence.

Recommendation #2 – Regarding the Reclamation Trust and Environmental Payments

The Report makes the following recommendations: (i) the amount of the contributions made to the Kumtor reclamation trust be increased, and (ii) the amount of environmental payment being paid by Kumtor (as expressly set out in the Restated Investment Agreement) should be increased from its current amount of US\$310,000 per year. We will address each recommendation in turn.

With respect to the reclamation trust, Kumtor contributes funds to the reclamation trust fund in the manner set out in the Restated Investment Agreement and the Reclamation Trust Deed dated as of January 25, 1996 among KGC, Rothschild Trust Corporation Limited (as Trustee) and the Government. In particular, KGC annually deposits into the reclamation trust an amount equal to the amount of the total reclamation cost required to be amortized in such year calculated in accordance with Canadian generally accepted accounting principles. Such principles require that reclamation costs be amortized over the life of the mine, pro rata with the number of ounces of gold sales. This has been, and continues to be KGC's practice. We note that KGC is in the process of transferring the trust funds to a bank in the Kyrgyz Republic.

With respect to the amount of reclamation funds needed for the Kumtor Project, we note that

KGC reviews its reclamation obligations every three years to ensure that it is complying with international practice. There will be a review in 2013 and we would be pleased to involve KR authorities in that process to respond to any concerns.

With respect to the annual environmental payment of US\$310,000, we note that this is expressly provided for in section 5.3(d) of the Restated Investment Agreement. This amount of US\$310,000 was negotiated at arm's length between Kumtor and Centerra, on one hand, and the Government on the other.

We note that implicit in the Report's recommendation that Kumtor be subject to additional environmental payments, is the assertion that Kumtor is causing material environmental damage. We expressly deny this. Kumtor's operations have been subject to numerous reviews by local and independent environmental experts, including most recently, the study carried out by ERM, an internationally recognized expert in the area, which was done at the request of Centerra's Safety, Health and Environment committee of the board of directors which acts independently of Centerra and Kumtor's management. The ERM report (a copy of which has been provided to the State Commission and is available at Kumtor's website in Russian and Kyrgyz) confirms that there are no material environmental deficiencies at the project.

Recommendation #3 – Regarding issues relating to protection of KR interests and arbitration

The working group recommends the opening of the Restated Project Agreements, with the objective of providing Kzn with more influence over Centerra, in light of the fact that Kumtor contributes significantly to Centerra's cash flow.

On the first issue of Centerra relying heavily on Kumtor for cash flow, we agree that the Kumtor Project is a material project for Centerra and is a significant contributor to its financial performance. However, we point out the development of the Kumtor Project required significant capital, which has historically affected cash flow. In those years, the continued operations at the Kumtor Project relied on cash flow from Centerra's other projects. As discussed earlier, from 2006-2008, the Boroo mine was significantly more profitable than the Kumtor Project due to Kumtor's high costs. During these years, cash from the Boroo project helped to fund the Kumtor operations, at one point providing funding of approximately US\$115 million.

Furthermore, Centerra is actively involved in exploring and developing other properties in Mongolia, Turkey, Russia and China. Exploration work has also historically been performed in the KR but has now stopped due to the expiry of the Karasay and Koendy licenses, and the inaction of the Licensing Commission of the Agency for Subsoil and Natural Resources in renewing such licenses. In addition, Centerra's management and directors (including two nominees from Kzn) regularly review and discuss potential acquisitions of properties of interest to Centerra, with the purchase price to be paid through the use of cash and/or Centerra common shares. To date, none have been approved by Centerra's board. Lastly, we note that Centerra has previously expressed an interest in participating in the development of the Jerooy

project in the KR.

With respect to concerns raised regarding the restructuring of the Kumtor Project in 2003, the valuation process and possible transactions involving Centerra and Eckerd, we refer you the responses provided above.

Recommendation #4 – Change of tax system for the Kumtor Project

The Report recommends a change to the Kumtor Project such that the current KR Tax Code would apply. We disagree with this. The Restated Investment Agreement sets out a comprehensive regime of all payments to the Government, and expressly states that unless otherwise provided therein, KOC and KGC are exempt from all other taxes, duties, rates, royalties, withholding obligations, deductions, or other governmental charges whatsoever, however characterized, and whether accessed by the KR or by any national, regional, municipal, local or administrative instrumentality of the KR (“Taxes”). We do not understand the legal basis for changing the current tax regime, particularly as Section 5.9 of the Restated Investment Agreement provides for stabilization of Taxes and states that KGC and KOC will not be subject to any future change in legislation which would be more burdensome to the company. The tax regime was fully negotiated and approved, and was an integral part of the 2009 agreements. It was one of the bases for Kzn receiving substantial economic benefit at that time, including the issuance or transfer of approximately 43 million common shares of Centerra.

We would welcome the opportunity to further discuss any of these matters with members of the working group.

Sincerely,

Jeffrey Parr
Vice President and Chief Financial Officer
Centerra Gold Inc.

Copy Almambet Shykmamatov, Kyrgyz Republic, Minister of Justice
Ian Atkinson, President and Chief Executive Officer, Centerra Gold Inc.
Michael Fischer, President, Kumtor Operating Company CJSC