
**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549**

FORM 10-Q

(Mark One)
 QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2006

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

COMMISSION FILE NUMBER 1-6780

RAYONIER INC.

**Incorporated in the State of North Carolina
I.R.S. Employer Identification Number 13-2607329**

**50 North Laura Street, Jacksonville, FL 32202
(Principal Executive Office)**

Telephone Number: (904) 357-9100

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months and (2) has been subject to such filing requirements for the past 90 days. YES NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, or a non-accelerated filer. See definition of "accelerated filer" and "large accelerated filer" in Rule 12b-2 of the Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). YES NO

As of July 21, 2006, there were outstanding 76,570,449 Common Shares of the Registrant.

TABLE OF CONTENTS

	<u>PAGE</u>
PART I. FINANCIAL INFORMATION	
Item 1. Condensed Consolidated Financial Statements (Unaudited)	
Condensed Consolidated Statements of Income and Comprehensive Income for the Three and Six Months Ended June 30, 2006 and 2005	1
Condensed Consolidated Balance Sheets as of June 30, 2006 and December 31, 2005	2
Condensed Consolidated Statements of Cash Flows for the Six Months Ended June 30, 2006 and 2005	3
Notes to Condensed Consolidated Financial Statements	4
Item 2. Management’s Discussion and Analysis of Financial Condition and Results of Operations	23
Item 3. Quantitative and Qualitative Disclosures about Market Risk	35
Item 4. Controls and Procedures	35
PART II. OTHER INFORMATION	
Item 1. Legal Proceedings	36
Item 1A. Risk Factors	36
Item 2. Unregistered Sales of Equity Securities and Use of Proceeds	36
Item 3. Defaults Upon Senior Securities	36
Item 4. Submission of Matters to a Vote of Security Holders	36
Item 5. Other Information	36
Item 6. Exhibits	37
Signature	38

RAYONIER INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED STATEMENTS OF INCOME
AND COMPREHENSIVE INCOME
(Unaudited)
(Dollars in thousands, except per share data)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
SALES	<u>\$312,122</u>	<u>\$290,287</u>	<u>\$589,274</u>	<u>\$565,259</u>
Costs and Expenses				
Cost of sales	247,429	227,040	471,580	444,366
Selling and general expenses	14,436	15,260	30,620	29,800
Other operating income, net	(818)	(915)	(2,050)	(5,116)
	<u>261,047</u>	<u>241,385</u>	<u>500,150</u>	<u>469,050</u>
Equity in loss of New Zealand joint venture	(99)	—	(848)	—
OPERATING INCOME	<u>50,976</u>	<u>48,902</u>	<u>88,276</u>	<u>96,209</u>
Gain on sale of portion of New Zealand joint venture	7,769	—	7,769	—
INCOME FROM CONTINUING OPERATIONS, INCLUDING GAIN ON SALE OF PORTION OF NEW ZEALAND JOINT VENTURE	<u>58,745</u>	<u>48,902</u>	<u>96,045</u>	<u>96,209</u>
Interest expense	(11,874)	(12,827)	(24,063)	(25,140)
Interest and miscellaneous income, net	1,781	1,042	3,979	1,531
INCOME FROM CONTINUING OPERATIONS BEFORE INCOME TAXES	<u>48,652</u>	<u>37,117</u>	<u>75,961</u>	<u>72,600</u>
Income tax (expense) benefit	(5,874)	4,458	(9,879)	3,815
INCOME FROM CONTINUING OPERATIONS	<u>42,778</u>	<u>41,575</u>	<u>66,082</u>	<u>76,415</u>
DISCONTINUED OPERATIONS, NET				
Loss on discontinued operations, net of income tax benefit of \$9,863 and \$10,329	—	(24,699)	—	(25,080)
NET INCOME	<u>42,778</u>	<u>16,876</u>	<u>66,082</u>	<u>51,335</u>
OTHER COMPREHENSIVE INCOME (LOSS)				
Unrealized loss on hedged transactions, net of income tax benefit of \$358 and \$262	—	(229)	—	(410)
Foreign currency translation adjustment	(1,035)	(4,345)	(8,704)	(656)
COMPREHENSIVE INCOME	<u>\$ 41,743</u>	<u>\$ 12,302</u>	<u>\$ 57,378</u>	<u>\$ 50,269</u>
EARNINGS (LOSS) PER COMMON SHARE				
BASIC EARNINGS (LOSS) PER SHARE				
Continuing Operations	\$ 0.56	\$ 0.55	\$ 0.87	\$ 1.01
Discontinued Operations	—	(0.33)	—	(0.33)
Net Income	<u>\$ 0.56</u>	<u>\$ 0.22</u>	<u>\$ 0.87</u>	<u>\$ 0.68</u>
DILUTED EARNINGS (LOSS) PER SHARE				
Continuing Operations	\$ 0.55	\$ 0.54	\$ 0.85	\$ 0.99
Discontinued Operations	—	(0.32)	—	(0.32)
Net Income	<u>\$ 0.55</u>	<u>\$ 0.22</u>	<u>\$ 0.85</u>	<u>\$ 0.67</u>

See Notes to Condensed Consolidated Financial Statements.

RAYONIER INC. AND SUBSIDIARIES
CONDENSED CONSOLIDATED BALANCE SHEETS
(Unaudited)
(Dollars in thousands unless otherwise noted)

	<u>June 30,</u> <u>2006</u>	<u>December 31,</u> <u>2005</u>
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents	\$ 165,020	\$ 146,227
Accounts receivable, less allowance for doubtful accounts of \$1,108 and \$1,158	105,605	88,378
Inventory		
Finished goods	56,192	65,214
Work in process	8,481	8,666
Raw materials	8,051	10,013
Manufacturing and maintenance supplies	1,775	1,652
Total inventory	74,499	85,545
Other current assets	58,212	33,948
Total current assets	403,336	354,098
TIMBER, TIMBERLANDS AND LOGGING ROADS, NET OF DEPLETION AND AMORTIZATION	917,253	927,019
PROPERTY, PLANT AND EQUIPMENT		
Land	21,386	20,862
Buildings	115,325	114,678
Machinery and equipment	1,250,795	1,216,864
Total property, plant and equipment	1,387,506	1,352,404
Less - accumulated depreciation	(1,018,725)	(991,094)
	368,781	361,310
INVESTMENT IN JOINT VENTURE	55,917	81,648
OTHER ASSETS	114,347	114,989
	<u>\$ 1,859,634</u>	<u>\$1,839,064</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Accounts payable	\$ 80,034	\$ 66,362
Bank loans and current maturities	1,765	3,310
Accrued taxes	36,776	19,634
Accrued payroll and benefits	14,582	23,380
Accrued interest	2,970	1,924
Accrued customer incentives	6,976	9,087
Other current liabilities	36,842	33,951
Current reserves for dispositions and discontinued operations	11,844	12,422
Total current liabilities	191,789	170,070
DEFERRED INCOME TAXES	34,778	32,236
LONG-TERM DEBT	554,691	555,213
NON-CURRENT RESERVES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS	124,068	127,960
OTHER NON-CURRENT LIABILITIES	69,275	68,733
COMMITMENTS AND CONTINGENCIES (Notes 11 and 12)		
SHAREHOLDERS' EQUITY		
Common Shares, 120,000,000 shares authorized, 76,570,449 and 76,092,566 shares issued and outstanding	437,087	422,364
Retained earnings	449,046	454,884
Accumulated other comprehensive (loss) income	(1,100)	7,604
	885,033	884,852
	<u>\$ 1,859,634</u>	<u>\$1,839,064</u>

See Notes to Condensed Consolidated Financial Statements.

RAYONIER INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(Unaudited)
(Dollars in thousands, unless otherwise noted)

	Six Months Ended June 30,	
	2006	2005
OPERATING ACTIVITIES		
Income from continuing operations	\$ 66,082	\$ 76,415
Non-cash items included in income:		
Depreciation, depletion and amortization	66,611	71,998
Non-cash cost of real estate sales	4,504	6,003
Gain on sale of portion of New Zealand joint venture (Note 8)	(7,769)	—
Deferred income tax benefit	(3,571)	(12,584)
Non-cash stock-based incentive compensation expense	5,799	—
Other	1,530	—
Increase in accounts receivable	(17,507)	(614)
Decrease (increase) in inventory	6,815	(2,712)
Increase (decrease) in accounts payable	15,349	(6,565)
Increase in other current assets	(16,053)	(12,811)
Increase in accrued liabilities	2,927	2,044
Increase in other non-current liabilities	1,654	3,790
Decrease in other assets	11,849	2,770
Expenditures for dispositions and discontinued operations	(5,108)	(4,804)
CASH PROVIDED BY OPERATING ACTIVITIES FROM CONTINUING OPERATIONS	133,112	122,930
CASH PROVIDED BY OPERATING ACTIVITIES FROM DISCONTINUED OPERATIONS	—	965
INVESTING ACTIVITIES		
Capital expenditures	(61,616)	(43,645)
Purchase of timberlands	(4,324)	—
Proceeds from sale of portion of New Zealand joint venture	21,770	—
Proceeds from matured energy forward contracts	674	—
Increase in restricted cash	(4,240)	(1,998)
CASH USED FOR INVESTING ACTIVITIES FROM CONTINUING OPERATIONS	(47,736)	(45,643)
CASH USED FOR INVESTING ACTIVITIES FROM DISCONTINUED OPERATIONS	—	(274)
FINANCING ACTIVITIES		
Issuance of debt	66,000	75,000
Repayment of debt	(67,545)	(46,545)
Dividends paid	(71,841)	(62,245)
Issuance of common shares	5,345	7,967
Repurchase of common shares	(472)	—
Excess tax benefits from stock-based compensation (Note 3)	2,211	—
CASH USED FOR FINANCING ACTIVITIES FROM CONTINUING OPERATIONS	(66,302)	(25,823)
EFFECT OF EXCHANGE RATE CHANGES ON CASH	(281)	43
CASH AND CASH EQUIVALENTS		
Increase in cash and cash equivalents	18,793	52,198
Balance, beginning of year	146,227	84,117
Balance, end of period	<u>\$ 165,020</u>	<u>\$ 136,315</u>
SUPPLEMENTAL DISCLOSURES OF CASH FLOW INFORMATION		
Cash paid during the period:		
Interest	<u>\$ 22,735</u>	<u>\$ 23,867</u>
Income taxes	<u>\$ 9,983</u>	<u>\$ 5,898</u>
Non-cash investing activity:		
Capital assets purchased on account	<u>\$ (1,672)</u>	<u>\$ —</u>

See Notes to Condensed Consolidated Financial Statements.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

1. BASIS OF PRESENTATION

The unaudited condensed consolidated financial statements of Rayonier Inc. and its subsidiaries (Rayonier or the Company), reflect all adjustments (which include normal recurring adjustments) necessary for the fair presentation of the results of operations, the financial position and the cash flows for the periods presented. The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires the use of certain estimates by management in determining the amount of assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting periods. There are risks inherent in estimating, and therefore, actual results could differ from those estimates. For a full description of the Company's significant accounting policies, please refer to the Notes to Consolidated Financial Statements in the 2005 Annual Report on Form 10-K.

New Accounting Standards

In July 2006, the FASB issued FIN 48, *Accounting for Uncertainty in Income Taxes - an interpretation of FASB Statement No. 109*. This Interpretation clarifies the accounting for uncertain tax positions recognized in an enterprise's financial statements in accordance with SFAS No. 109, *Accounting for Income Taxes*. It prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. In addition, it provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. FIN 48 is effective for fiscal years beginning after December 15, 2006. The Company is in the process of determining the potential impact this Interpretation will have on its financial position, cash flows and results of operations.

2. INCOME PER COMMON SHARE

All 2005 share amounts presented in the following table and hereafter have been restated to reflect the Company's October 17, 2005 three-for-two stock split. The following table provides details of the calculation of basic and diluted earnings per common share:

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Income from continuing operations	\$ 42,778	\$ 41,575	\$ 66,082	\$ 76,415
Loss from discontinued operations	—	(24,699)	—	(25,080)
Net income	<u>\$ 42,778</u>	<u>\$ 16,876</u>	<u>\$ 66,082</u>	<u>\$ 51,335</u>
Shares used for determining basic earnings per common share	76,465,269	75,326,922	76,377,976	75,253,811
Dilutive effect of:				
Stock options	1,177,197	1,432,695	1,299,922	1,374,752
Performance and restricted shares	326,666	652,493	311,900	650,033
Shares used for determining diluted earnings per common share	<u>77,969,132</u>	<u>77,412,110</u>	<u>77,989,798</u>	<u>77,278,596</u>
Basic earnings (loss) per common share:				
Continuing operations	\$ 0.56	\$ 0.55	\$ 0.87	\$ 1.01
Discontinued operations	—	(0.33)	—	(0.33)
Net income	<u>\$ 0.56</u>	<u>\$ 0.22</u>	<u>\$ 0.87</u>	<u>\$ 0.68</u>
Diluted earnings (loss) per common share:				
Continuing operations	\$ 0.55	\$ 0.54	\$ 0.85	\$ 0.99
Discontinued operations	—	(0.32)	—	(0.32)
Net income	<u>\$ 0.55</u>	<u>\$ 0.22</u>	<u>\$ 0.85</u>	<u>\$ 0.67</u>

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

3. INCENTIVE STOCK PLANS

Accounting Prior to Adoption of SFAS No. 123(R)

Prior to January 1, 2006, the Company accounted for stock-based compensation using the intrinsic value based method under Accounting Principles Board Opinion No. 25 (APB No. 25), *Accounting for Stock Issued to Employees* and related Accounting Interpretations thereof, as permitted by FASB Statement No. 123, *Accounting for Stock-Based Compensation*. No compensation expense was recognized in the Condensed Consolidated Statements of Income and Comprehensive Income for the three and six months ended June 30, 2005 for stock options under APB No. 25. The Company adopted SFAS No. 123(R), *Share-Based Payment*, on January 1, 2006 using the modified prospective basis, which requires stock-based compensation to be accounted for under the fair value method.

At June 30, 2006, the Company had two stock-based employee compensation plans. The 1994 Rayonier Incentive Stock Plan (the 1994 Plan) provided for the grant of incentive stock options, non-qualified stock options, stock appreciation rights, performance shares and restricted stock, subject to certain limitations. Effective January 1, 2004, the Company adopted the 2004 Rayonier Incentive Stock and Management Bonus Plan (the 2004 Plan), after shareholder approval was obtained. The 2004 Plan provides for 4.5 million shares to be granted for incentive stock options, non-qualified stock options, stock appreciation rights, performance shares and restricted stock, subject to certain limitations. The Company has issued non-qualified stock options, performance shares and restricted stock under both of the plans. The Company issues new shares of stock upon the exercise of stock options, the granting of restricted stock, and the vesting of performance shares.

Summary of Impact of SFAS No. 123(R)

Total compensation cost recorded in "Selling and general expenses" for stock-based compensation was \$2.2 million and \$2.7 million for the three months ended June 30, 2006 and 2005, respectively and \$5.8 million and \$3.9 million for the six months ended June 30, 2006 and 2005, respectively. Included in the compensation cost for the three and six months ended June 30, 2006 was \$0.2 million and \$0.4 million related to stock option awards for retirement eligible employees that were granted prior to the adoption of SFAS No. 123(R), which is being recognized over the three-year vesting period. All stock option awards to retirement eligible employees subsequent to the adoption of SFAS No. 123(R) are expensed immediately. The \$5.8 million stock-based compensation expense recorded in the first six months of 2006 includes \$2.8 million for stock options of which \$1.4 million was for stock options granted to retirement-eligible employees and expensed immediately in January 2006. The SFAS No. 123(R) compensation expense is expected to be approximately \$2.3 million for each of the remaining two quarters of 2006.

As a result of adopting SFAS No. 123(R), the Company's pre-tax income for the three and six months ended June 30, 2006 is \$2.3 million and \$2.2 million below what would have been reported under APB No. 25, respectively. Net income for the three months and six months ended June 30, 2006 is \$1.8 million and \$1.7 million lower than what would have been reported under APB No. 25, respectively. Basic and diluted earnings per share for the three and six months ended June 30, 2006 would have each been \$0.58 and \$0.57 per share and \$0.89 and \$0.87 per share, respectively, if the Company had not adopted SFAS No. 123(R). This compares to actual basic and diluted earnings per share of \$0.56 and \$0.55 per share and \$0.87 and \$0.85 per share, respectively. Tax benefits recognized related to stock-based compensation for the three months ended June 30, 2006 and 2005 were \$0.6 million and \$0.7 million, respectively, and \$0.9 million and \$1.1 million, for the six months ended, respectively.

Prior to the adoption of SFAS No. 123(R), the Company presented all tax benefits of deductions resulting from the exercise of stock options as operating cash flows in the Consolidated Statement of Cash Flows. SFAS No. 123(R) requires the \$2.2 million of cash flows resulting from tax benefits in excess of the compensation cost recognized (excess tax benefits) to be classified as financing cash flows.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

Pro Forma Disclosures for the Three and Six Months Ended June 30, 2005

Pursuant to the requirements of SFAS No. 148, *Accounting for Stock-Based Compensation-Transition and Disclosure*, the Company continues to provide the following disclosure for income statement periods presented prior to the adoption of SFAS No. 123(R). The following table provides a reconciliation for the three and six months ended June 30, 2005 that adds back to reported net income the recorded expense under APB No. 25, net of related income tax effects, deducts the total fair value expense under SFAS No. 123, net of related income tax effects, and shows the reported and pro forma earnings per share amounts:

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005
Net income, as reported	\$ 16,876	\$ 51,335
Total stock-based employee compensation cost included in the determination of net income, net of related tax effects	2,080	3,052
Total stock-based employee compensation cost determined under fair value method for all awards, net of related tax effects	(1,742)	(3,454)
Pro forma net income	<u>\$ 17,214</u>	<u>\$ 50,933</u>
Earnings per share:		
Basic, as reported	\$ 0.22	\$ 0.68
Basic, pro forma	\$ 0.23	\$ 0.68
Diluted, as reported	\$ 0.22	\$ 0.67
Diluted, pro forma	\$ 0.22	\$ 0.66

Fair Value Calculations by Award

Restricted Stock

Restricted stock granted under the 1994 and 2004 Plans generally vests upon completion of a three-year period. The fair value of each share granted is equal to the share price of the Company's stock on the date of grant. As of June 30, 2006, there was \$1.4 million of unrecognized compensation cost related to the Company's outstanding restricted stock. This cost is expected to be recognized over a weighted average period of 1.2 years. The total intrinsic value of restricted stock outstanding at June 30, 2006 and 2005 was \$2.9 million and \$3.0 million, respectively. During the six months ended June 30, 2006, the Company canceled 8,217 common shares to pay the minimum withholding tax requirements on the participants' behalf.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

A summary of the Company's restricted stock plans as of and for the six months ended June 30, 2006 is presented below:

	<u>2006</u>	<u>Weighted Average Grant Date Fair Value</u>
	<u>Number of Shares</u>	
Nonvested Restricted Shares at January 1	117,731	\$ 25.77
Granted	14,500	\$ 39.64
Vested	(42,731)	\$ 16.57
Nonvested Restricted Shares at June 30	<u>89,500</u>	<u>\$ 32.41</u>

Performance Shares

The Company's performance shares generally vest upon completion of a three-year period. The number of shares, if any, that are ultimately awarded is contingent upon total shareholder return versus peer groups. Under APB No. 25, the Company's performance shares are expensed using the closing market price of the Company's common stock at each reporting date, adjusted for an estimate of the ultimate number of shares to be issued. Upon adoption of SFAS No. 123(R), all performance share awards granted after January 1, 2006 are valued by an independent third party using a Monte Carlo simulation model. The fair value of awards granted prior to 2006 is equal to the share price of the Company's stock on the date of grant. Compensation cost is based on the number of shares expected to be awarded upon vesting. The Company allows for the cash settlement of performance share awards to pay the minimum required withholding tax. During the six months ended June 30, 2006 and 2005, \$3.9 million and \$2.2 million in cash was used to pay the minimum withholding tax requirements in lieu of receiving common shares, respectively. As of June 30, 2006, there was \$7.4 million of unrecognized compensation cost related to the Company's performance share awards. This cost is expected to be recognized over a weighted average period of 2.0 years. The total intrinsic value of non-vested outstanding performance shares at June 30, 2006 and 2005 was \$17.9 million and \$18.5 million, respectively.

Expected volatility, dividend yield and beta were estimated using daily returns on the Company's common stock for the three-year period ending on the grant date. The following chart provides a tabular overview of the assumptions used by an independent third party in calculating the fair value of the awards granted in the six months ended June 30, 2006:

	<u>2006</u>
Dividend yield	4.4%
Expected volatility	21.2%
Risk-free rate	4.4%
Expected market risk-premium	8.5%
Beta	0.92

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

A summary of the status of the Company's performance share plans as of and for the six months ended June 30, 2006 is presented below:

	2006	
	Number of Shares	Weighted Average Grant Date Fair Value
Nonvested Performance Shares at January 1	614,795	\$ 24.05
Granted	148,000	\$ 36.25
Vested	(272,420)	\$ 17.22
Nonvested Performance Shares at June 30	<u>490,375</u>	<u>\$ 31.52</u>

Non-Qualified Employee Stock Options

The exercise price of each non-qualified stock option granted under both the 1994 and 2004 plans is equal to the market price of the Company's stock on the date of grant. Under the 1994 plan, the maximum term is 10 years and two days from the date of grant while under the 2004 Plan, the maximum term is 10 years from the grant date. Awards vest ratably over three years. Under APB No. 25, no compensation expense was recorded for stock options. Under SFAS No. 123(R), the fair value of each option grant is estimated on the date of grant using the Black-Scholes option-pricing model. The Company uses historical volatility, while the expected term is based on prior exercise behavior. The historical volatility for each grant is based on the change in daily market price of the Company's common stock over the expected life of the award. The Company has elected to value each grant in total and recognize the expense for stock options on a straight-line basis. The following chart provides a tabular overview of the weighted average assumptions and related fair value calculations of options granted for the six months ended June 30:

	2006	2005
Dividend yield	4.6%	5.1%
Expected volatility	30.2%	31.1%
Risk-free rate	4.3%	3.9%
Expected life (in years)	6.3	6.7
Fair value per share of options granted	<u>\$9.03</u>	<u>\$6.54</u>

A summary of the status of the Company's stock option plans as of and for the six months ended June 30, 2006 is presented below:

	Number of Shares	Weighted Average Exercise Price (per common share)	Weighted Average Remaining Contractual Term (in years)	Aggregate Intrinsic Value (in thousands)
Options outstanding at January 1	3,687,958	\$ 20.50		
Granted	396,150	\$ 41.34		
Exercised	(302,052)	\$ 17.70		
Canceled	(5,800)	\$ 34.05		
Options outstanding at June 30	<u>3,776,256</u>	<u>\$ 22.89</u>	<u>5.0</u>	<u>\$ 53,616</u>
Options vested and expected to vest as of June 30	<u>3,733,845</u>	<u>\$ 22.75</u>	<u>5.0</u>	<u>\$ 53,467</u>
Options exercisable at June 30	<u>2,910,613</u>	<u>\$ 19.05</u>	<u>4.8</u>	<u>\$ 51,020</u>

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

The total intrinsic value of options exercised during the six months ended June 30, 2006 and 2005 was \$7.7 million and \$9.2 million, respectively. The total fair value of options that vested during the six months ended June 30, 2006 and 2005 was \$2.5 million and \$2.9 million, respectively. As of June 30, 2006, there was \$3.8 million of unrecognized compensation cost related to the Company's stock options. This cost is expected to be recognized over a weighted average period of 1.8 years.

4. INCOME TAXES

The Company is a real estate investment trust (REIT).

General REIT Requirements

As a REIT, if applicable Internal Revenue Code (IRC) requirements are met, only the Company's taxable REIT subsidiaries are subject to corporate income taxes. However, the Company is subject to corporate income tax on built-in gains (the excess of fair market value over tax basis on property held by the Company upon REIT conversion at January 1, 2004) on taxable sales of such property during the first ten years following the election to be taxed as a REIT. In accordance with SFAS No. 109, *Accounting for Income Taxes*, the Company estimated the amount of timberland and other assets that will be sold within the ten-year built-in gain period and retained deferred tax liabilities for such built-in gains. All deferred tax liabilities and assets related to the taxable REIT subsidiaries were retained.

Under current law, the built-in gains tax from the sale of timberlands can be deferred if sales proceeds from relinquished properties are reinvested in similar property consistent with the requirements of IRC Section 1031 regarding like-kind exchanges (LKE), and eliminated if the replacement property is owned at least until expiration of the ten-year built-in gain period on December 31, 2013. The Company's ability to harvest timber on a pay-as-cut basis from such replacement property is not restricted during the ten-year built-in gain period.

As a REIT, the Company can be subject to a 100 percent tax on the gain from entering into "prohibited transactions." The Company believes it did not engage in any prohibited transactions during the six months ended June 30, 2006 or 2005.

Undistributed Foreign Earnings

Prior to March 31, 2004, the Company did not provide for U.S. taxes on all undistributed foreign earnings as it intended to permanently reinvest its undistributed foreign earnings overseas. Following the Company's conversion to a REIT, this strategy was reevaluated with a greater likelihood of most future investments being made in U.S. timberlands. Accordingly, during 2004, the Company recognized tax expense on approximately \$123 million of undistributed foreign earnings that it expected to ultimately repatriate. During the first six months of 2005, the Company recognized \$1.4 million of tax benefits related to exchange rate fluctuations on these undistributed foreign earnings. During the fourth quarter of 2005, the Company repatriated these previously undistributed foreign earnings.

The Company has undistributed foreign earnings it intends to permanently reinvest overseas, including all future foreign earnings. Therefore, no U.S. taxes have been provided on undistributed foreign earnings.

Tax Audits

Prior to filing its first quarter 2005 Form 10-Q, the Company executed a settlement agreement with the Internal Revenue Service (IRS) regarding a disputed issue for its 1996 and 1997 taxable years. The Company reversed the final \$9.5 million of federal tax reserves previously established for this issue in the first quarter of 2005.

In June 2005, the Company reached an agreement with the IRS regarding disputed issues for its 1998 and 1999 taxable years, resulting in the reversal in the second quarter of 2005 of a \$7.2 million reserve previously established for these issues. In the first quarter of 2006, the Company reversed \$0.5 million of state tax reserves, as a result of the favorable IRS settlements related to 1998 and 1999.

In the third quarter of 2005, the IRS completed its field examination of tax years 2000, 2001 and 2002. The Company reached an agreement with the IRS regarding certain issues for those years. The Company has appealed the IRS' findings for "unagreed" issues and cannot predict the ultimate outcome and resolution of the disputed items at this time. The Company is in a net overpayment position of approximately \$9.0 million before consideration of the disputed items.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

The Company has other matters under review by various taxing authorities, including the items noted above. The Company believes its positions on these matters as well as others, including the unagreed issues, are technically sound and its tax reserves at June 30, 2006 adequately reflect the probable resolution of these items. Nevertheless, it is reasonably possible that the final resolution of these matters could result in additional tax liability of up to \$8.5 million above established reserves.

Provision for Income Taxes from Continuing Operations

The effective tax rate before discrete items was 14.0 percent in the second quarter of 2006 compared to 14.1 percent in the second quarter of 2005. Compared to the first quarter, the effective rate decreased 2.4 percent primarily due to foreign earnings taxed at a rate lower than the U.S. statutory rate. Through June 30, the effective tax rate before discrete items was 14.9 percent compared to 15.7 percent for the comparable period in 2005 primarily due to U.S. taxes recorded on undistributed foreign earnings in 2005.

The Company's effective tax rate is below the 35 percent U.S. statutory tax rate primarily due to tax benefits associated with being a REIT and the effect of LKE transactions. Partially offsetting these benefits is the loss of tax deductibility on interest expense (\$4.9 million in the quarter) and corporate overhead expenses associated with REIT activities (\$2.9 million in the quarter). The net tax benefit from REIT activities was \$8.7 million compared to \$7.3 million in the second quarter of 2005. The Company's net tax benefit from REIT activities for the six months ended June 30, 2006 and 2005 was \$13.5 million and \$13.0 million, respectively.

In determining its effective tax rate, the Company estimates it will complete LKE transactions for \$23.6 million of its real estate sales which will result in tax benefits of \$6.7 million, \$2.6 million of which has been recognized to date. During the six months ended June 30, 2005, the Company completed LKE transactions for \$6.7 million of its real estate sales and realized tax benefits of \$0.9 million.

The following tables reconcile the Company's income tax provision at the U.S. statutory tax rate to the reported provision and effective tax rate for the three and six months ended June 30 (millions of dollars):

	<u>Three months ended June 30,</u>			
	<u>2006</u>	<u>%</u>	<u>2005</u>	<u>%</u>
Income tax (provision) benefit from continuing operations at U.S. statutory rate	\$(17.0)	(35.0)	\$(13.0)	(35.0)
State and local income taxes, net of federal benefit	(0.4)	(0.8)	(0.1)	(0.3)
REIT income not subject to federal tax	8.7	17.9	7.3	19.7
Foreign operations*	1.7	3.5	0.4	1.1
Tax benefit on U.S. export sales	0.5	1.0	0.5	1.3
Permanent differences	—	—	0.1	0.2
Tax credits and other, net	(0.3)	(0.6)	(0.4)	(1.1)
Income tax (provision) benefit from continuing operations before discrete items	\$ (6.8)	(14.0)	\$ (5.2)	(14.1)
Return to accrual adjustments	0.9	1.9	—	—
Favorable IRS audit settlements	—	—	7.2	19.4
Foreign exchange rate change on U.S. tax from undistributed foreign earnings	—	—	2.5	6.7
Income tax (provision) benefit from continuing operations as reported	<u>\$ (5.9)</u>	<u>(12.1)</u>	<u>\$ 4.5</u>	<u>12.0</u>

* Primarily from foreign exchange and rate differentials.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

	Six months ended June 30,			
	2006	%	2005	%
Income tax (provision) benefit from continuing operations at U.S. statutory rate	\$(26.6)	(35.0)	\$(25.4)	(35.0)
State and local income taxes, net of federal benefit	(0.6)	(0.7)	(0.5)	(0.7)
REIT income not subject to federal tax	13.5	17.7	13.0	18.0
Foreign operations*	1.7	2.2	0.5	0.7
Tax benefit on U.S. export sales	0.8	1.0	1.1	1.5
Permanent differences	0.2	0.3	0.3	0.3
Tax credits and other, net	(0.3)	(0.4)	(0.4)	(0.5)
Income tax (provision) benefit from continuing operations before discrete items	\$(11.3)	(14.9)	\$(11.4)	(15.7)
Return to accrual adjustments	0.9	1.2	—	—
Favorable IRS audit settlements	0.5	0.7	16.7	23.1
Unrealizable New Zealand tax credits for U.S. withholding tax paid	—	—	(2.9)	(4.0)
Foreign exchange rate change on U.S. tax from undistributed foreign earnings	—	—	1.4	1.9
Income tax (provision) benefit from continuing operations as reported	<u>\$ (9.9)</u>	<u>(13.0)</u>	<u>\$ 3.8</u>	<u>5.3</u>

* Primarily from foreign exchange and rate differentials.

Provision for Income Taxes from Discontinued Operations

On June 28, 2005, the Board of Directors approved a plan to sell the Medium-Density Fiberboard (MDF) business located in New Zealand and on August 28, 2005, the Company completed the sale. During the three and six months ended June 30, 2005, the Company had a pre-tax loss from its MDF business of \$34.6 million and \$35.4 million, respectively. See Note 7 - *Sale of Medium-Density Fiberboard Business*, for additional information.

A reconciliation of the income tax benefit from discontinued operations at the U. S. statutory rate to the reported benefit follows:

	Three months ended		Six months ended	
	June 30,		June 30,	
	2005	%	2005	%
Income tax benefit from discontinued operations at U. S. statutory rate	\$ 12.1	35.0	\$ 12.4	35.0
State and local income taxes	0.4	1.2	0.4	1.2
Permanent differences related to foreign exchange rate changes	(2.6)	(7.7)	(2.5)	(7.0)
Income tax benefit from discontinued operations as reported	<u>\$ 9.9</u>	<u>28.5</u>	<u>\$ 10.3</u>	<u>29.2</u>

5. LIKE-KIND EXCHANGES AND RESTRICTED CASH

In order to qualify for LKE treatment, proceeds from real estate sales must be deposited with a third party intermediary and accounted for as restricted cash until qualifying replacement property is acquired. In the event that LKE purchases are not completed, the proceeds are returned to the Company and reclassified as available cash after 180 days. As of June 30, 2006 and December 31, 2005, the Company had \$6.7 million and \$2.5 million, respectively, of proceeds from real estate sales classified as restricted cash in "Other assets", which were on deposit with an LKE intermediary.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

6. SHAREHOLDERS' EQUITY

An analysis of shareholders' equity for the six months ended June 30, 2006 and the year ended December 31, 2005 is shown below:

(Share and per share amounts not in thousands)	Common Shares		Retained Earnings	Accumulated Other Comprehensive Income/(Loss)	Shareholders' Equity
	Shares	Amount			
Balance, January 1, 2005	74,966,330	\$ 393,513	\$ 401,479	\$ 1,396	\$ 796,388
Net income	—	—	182,839	—	182,839
Dividends (\$1.71 per share)	—	—	(129,434)	—	(129,434)
Issuance of shares under incentive stock plans	1,132,390	23,029	—	—	23,029
Cash in lieu of fractional shares	(6,154)	(356)	—	—	(356)
Unrealized loss on hedged transactions	—	—	—	(410)	(410)
Minimum pension liability adjustments	—	—	—	16,323	16,323
Tax benefit on exercise of stock options	—	6,178	—	—	6,178
Foreign currency translation adjustment	—	—	—	(9,705)	(9,705)
Balance, December 31, 2005	76,092,566	\$ 422,364	\$ 454,884	\$ 7,604	\$ 884,852
Net income	—	—	66,082	—	66,082
Dividends (\$0.94 per share)	—	—	(71,920)	—	(71,920)
Issuance of shares under incentive stock plans	489,883	12,984	—	—	12,984
Repurchase of common shares	(12,000)	(472)	—	—	(472)
Tax benefit on stock-based compensation	—	2,211	—	—	2,211
Foreign currency translation adjustment	—	—	—	(8,704)	(8,704)
Balance, June 30, 2006	76,570,449	\$ 437,087	\$ 449,046	\$ (1,100)	\$ 885,033

7. SALE OF MEDIUM-DENSITY FIBERBOARD BUSINESS (MDF)

On August 28, 2005, the Company completed the sale of its MDF business to Dongwha Hong Kong International Limited for approximately \$40 million. The sale resulted in an insignificant gain in the third quarter of 2005. Prior to the sale, in the second quarter of 2005, an after-tax loss of \$24.1 million was recorded to adjust the MDF assets to fair market value. The operations of MDF qualified as discontinued operations in accordance with SFAS No. 144, *Accounting for the Impairment or Disposal of Long-Lived Assets*. The operating results of MDF were segregated from continuing operations in the Condensed Consolidated Statements of Income and Comprehensive Income for the three and six months ended June 30, 2005.

Operating results of the discontinued operation are summarized below:

	Three Months Ended June 30, 2005	Six Months Ended June 30, 2005
Sales	\$ 11,461	\$ 22,851
Operating loss	\$ (34,563)	\$ (35,409)
Net loss from discontinued operations	\$ (24,699)	\$ (25,080)

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

8. JOINT VENTURE INVESTMENT

On October 3, 2005, the Company entered into a joint venture (JV) arrangement with RREEF Infrastructure, the global infrastructure investing arm of Deutsche Asset Management (RREEF), under which the JV purchased approximately 354,000 acres of New Zealand timberlands. The JV used investor capital of approximately \$245 million and secured bank debt of approximately \$260 million to purchase Rayonier New Zealand Limited's (RNZ, a wholly-owned subsidiary of Rayonier Inc.) forests consisting of 118,000 acres for approximately \$187 million and 236,000 acres of New Zealand forests from Carter Holt Harvey (CHH), an Australasian forest products company, for approximately \$301 million. The Company's initial investment represented a 49.7 percent equity interest in the JV. In addition to the Company having an equity investment, RNZ serves as the manager of the JV forests.

The sale of RNZ's forests in 2005 resulted in \$65 million in cash proceeds, net of the Company's investment in the JV, and a \$73 million gain, of which \$37 million was recognized (based on the proportion of non-Rayonier (outside) interests in the JV on the date of sale) and the remaining \$36 million was deferred.

On June 30, 2006, the Company reduced its investment in the JV from 49.7 percent to 40 percent. AMP Capital Investors Limited, a subsidiary of the Australian Corporation AMP Limited, purchased a total interest in the JV of 35 percent, of which 9.7 percent was from RNZ and the remainder from RREEF. The Company received approximately \$21.8 million in cash proceeds and recorded an after-tax gain of \$6.5 million or \$0.08 per common share. The total after-tax gain includes approximately \$4.9 million of previously deferred gain from RNZ's October 3, 2005 timberland sale to the JV.

Rayonier's investment in the JV is accounted for using the equity method of accounting. Income from the JV is reported in the Timber segment as operating income since the Company manages the forests and its JV interest is an extension of RNZ's operations. The JV is subject to New Zealand income taxes, however its timber harvest operations are REIT-qualifying and therefore, the Company generally is not required to pay U.S. federal income taxes on its equity investment income.

In the three and six months ended June 30, 2006, the Company recorded losses of \$0.1 million and \$0.8 million, respectively, on its JV investment as sales were negatively impacted by limited export shipping capacity and higher freight rates due to fuel cost increases. Rayonier's equity method investment at June 30, 2006 was \$55.9 million, while its proportionate share of the JV's net assets at June 30, 2006 was \$81 million. The difference primarily represents the Company's unrecognized gain from the sale of timberland which will be recognized as timber and timberland is sold.

A rollforward of the Company's investment in the JV for the six months ended June 30, 2006 and from inception on October 3, 2005 through December 31, 2005 follows (in millions):

	<u>June 30, 2006</u>	<u>December 31, 2005</u>
Balance at beginning of period	\$ 81.7	\$ 85.3
Equity in loss of JV	(0.8)	(1.4)
Foreign exchange translation loss/other	(11.1)	(2.2)
Partial sale of investment	(13.9)	—
Balance at end of period	<u>\$ 55.9</u>	<u>\$ 81.7</u>

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

Summarized financial information for the JV as of June 30, 2006 and December 31, 2005 and for the three and six months ended June 30, 2006 is as follows (in millions):

	Three months ended June 30, 2006	Six months ended June 30, 2006
Sales	\$ 31.8	\$ 52.6
Operating income/(loss)	\$ 1.3	\$ 1.3
Pretax loss from operations	\$ (6.6)	\$ (14.3)
Net loss*	\$ (4.4)	\$ (9.6)
	June 30, 2006 **	December 31, 2005 **
Current assets	\$ 25.0	\$ 19.8
Timber and timberlands	468.1	528.6
Total assets	<u>\$ 493.1</u>	<u>\$ 548.4</u>
Current liabilities	\$ 25.3	\$ 14.9
Noncurrent liabilities	265.2	298.3
Partners' debt and capital	202.6	235.2
Total liabilities and equity	<u>\$ 493.1</u>	<u>\$ 548.4</u>

* The Company's equity interest in the JV's net losses of \$4.4 million and \$9.6 million, respectively, excludes interest of \$3.4 million and \$6.8 million, respectively, on debt owed to partners and includes \$0.6 million and \$0.9 million of deferred gain amortization, respectively.

** The final purchase price allocation has not been completed for the JV.

9. SEGMENT INFORMATION

Rayonier operates in four reportable business segments as defined by SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*: Timber, Real Estate, Performance Fibers, and Wood Products. Timber sales include all activities that relate to the harvesting of timber. The Real Estate segment includes the sale of all properties, including those designated for higher and better use (HBU). In the future, the Real Estate segment may include revenue generated from land with entitlements and infrastructure improvements, some of which may be through joint ventures. The assets of the Real Estate segment include HBU property held by TerraPointe LLC (TerraPointe), a wholly-owned real estate subsidiary of the Company, and timberlands under contract previously reported in the Timber segment. Allocations of depletion expense and the non-cash cost basis of real estate sold are recorded when the Real Estate segment reports the sale of an asset from the Timber segment. The Performance Fibers segment includes two major product lines, Cellulose Specialties and Absorbent Materials. The Wood Products segment is comprised of the Company's lumber operations. The Company's remaining operations include purchasing, harvesting and selling timber acquired from third parties (log trading) and trading wood products. As permitted by SFAS No. 131, these operations are combined and reported in an "Other" category. Sales between operating segments are made based on fair market value and intercompany profit or loss is eliminated in consolidation. The Company evaluates financial performance based on the operating income of the segments.

In August 2005, the Company sold its MDF business and the operations are shown as discontinued operations (see Note 7 - *Sale of Medium-Density Fiberboard Business*). These operations were previously included in the Wood Products segment. The Wood Products segment amounts shown below have been restated to exclude the MDF business.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

Total assets, sales, operating income (loss) and depreciation, depletion and amortization by segment including corporate and dispositions were as follows:

	June 30, 2006	December 31, 2005
ASSETS		
Timber	\$1,033,880	\$1,032,833*
Real Estate	22,649	29,594
Performance Fibers	483,503	459,962
Wood Products	38,495	39,781
Other Operations	33,761	34,998
Corporate	242,180	236,733*
Dispositions	5,166	5,163
TOTAL	<u>\$1,859,634</u>	<u>\$1,839,064</u>

* The Company revised the December 31, 2005 Timber assets amount (previously reported as \$959 million) and Corporate assets amount (previously reported as \$310 million) to correct the classification of the investment in the JV.

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
SALES				
Timber	\$ 61,038	\$ 54,597	\$115,512	\$106,459
Real Estate	17,822	14,626	30,889	38,277
Performance Fibers	165,859	153,283	311,841	296,227
Wood Products	32,243	36,348	63,803	66,896
Other Operations	35,248	31,504	67,358	57,790
Corporate and other	(88)	(71)	(129)	(390)
TOTAL	<u>\$312,122</u>	<u>\$290,287</u>	<u>\$589,274</u>	<u>\$565,259</u>

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
OPERATING INCOME (LOSS)				
Timber	\$ 29,705	\$ 23,158	\$ 53,576	\$ 46,821
Real Estate **	10,969	10,634	21,145	25,991
Performance Fibers	15,760	18,505	26,017	30,886
Wood Products	1,990	5,781	4,554	9,031
Other Operations	362	(382)	(35)	(196)
Corporate and other	(7,810)	(8,794)	(16,981)	(16,324)
TOTAL	<u>\$ 50,976</u>	<u>\$ 48,902</u>	<u>\$ 88,276</u>	<u>\$ 96,209</u>

** Includes non-cash cost basis of real estate sold during the three and six months ended June 30, 2006 and 2005 of \$4 million and \$5 million, and \$2 million and \$6 million, respectively.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
DEPRECIATION, DEPLETION AND AMORTIZATION				
Timber	\$13,528	\$15,264	\$28,507	\$29,881
Real Estate	913	235	1,360	3,419
Performance Fibers	17,338	18,653	32,444	34,634
Wood Products	1,805	1,837	3,589	3,584
Other Operations	147	156	297	306
Corporate and other	171	87	414	174
TOTAL	<u>\$33,902</u>	<u>\$36,232</u>	<u>\$66,611</u>	<u>\$71,998</u>

Operating income (loss), as stated in the preceding tables and as presented in the Condensed Consolidated Statements of Income and Comprehensive Income, is equal to Segment income (loss). The income (loss) items below "Operating income" in the Condensed Consolidated Statements of Income and Comprehensive Income are not allocated to segments. These items, which include interest (expense) income, miscellaneous income (expense), income tax (expense) benefit and the gain on sale of a portion of the New Zealand JV, are not considered by Company management to be part of segment operations.

10. FINANCIAL INSTRUMENTS

Interest Rate Swap Agreements

Rayonier Forest Resources, L.P. (RFR), a wholly owned subsidiary of Rayonier, entered into an interest rate swap on \$40 million of 8.288 percent fixed rate notes payable which matures on December 31, 2007. The swap converts interest payments from the fixed rate to six month LIBOR plus 4.99 percent and qualifies as a fair value hedge under SFAS No. 133, *Accounting for Derivative Instruments and Hedging Activities*. As such, the net effect from the interest rate swap is recorded as interest expense. The swap agreement settles every June 30 and December 31, until maturity. During the three and six months ended June 30, 2006, this swap agreement increased interest expense by \$0.2 million and \$0.3 million, respectively. During the three and six months ended June 30, 2005, this swap agreement reduced the Company's interest expense by \$0.1 million. Based upon current interest rates for similar transactions, the fair value of the interest rate swap agreement at June 30, 2006 and December 31, 2005 resulted in a liability of approximately \$1.4 million and \$1.2 million, respectively with corresponding decreases in debt.

In addition, RFR entered into an interest rate swap on \$50 million of 8.288 percent fixed rate notes payable which also matures on December 31, 2007. The swap converts interest payments from the fixed rate to a six month LIBOR plus 4.7825 percent rate and qualifies as a fair value hedge under SFAS No. 133. As such, the net effect of the interest rate swap is recorded in interest expense. The swap agreement settles every June 30 and December 31, until maturity. During the three and six months ended June 30, 2006, this swap agreement increased the Company's interest expense by \$0.1 million and \$0.3 million, respectively. During the three and six months ended June 30, 2005, the swap agreement reduced interest expense by \$0.1 million and \$0.2 million, respectively. Based upon current interest rates for similar transactions, the fair value of the interest rate swap agreement at June 30, 2006 and December 31, 2005 resulted in a liability of approximately \$1.6 million and \$1.3 million, respectively, with corresponding decreases in debt.

Commodity Swap Agreements

The Company enters into commodity forward contracts to fix some of its fuel oil and natural gas costs at its Performance Fibers mills. The Company's commodity forward contracts do not qualify for hedge accounting under SFAS No. 133 and instead are required to be marked-to-market.

During the three and six months ended June 30, 2006, the Company realized gains on matured fuel oil forward contracts of \$0.5 and \$1.1 million, respectively. The realized gain recorded on fuel oil forward contracts maturing during the three and six months ended June 30, 2005 was \$0.9 million and \$1.0 million, respectively. The mark-to-market valuation of outstanding fuel oil forward contracts at June 30, 2006 and December 31, 2005 resulted in an asset of \$0.7 million and \$0.8 million, respectively. The mark-to-market adjustments are recorded in "Other Operating Income/Expense."

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

During the three and six months ended June 30, 2006, the Company realized losses on matured natural gas forward contracts of \$0.1 and \$0.4 million, respectively. During the three and six months ended June 30, 2005, the Company realized a \$22 thousand gain and a \$0.1 million loss on natural gas forward contracts that matured, respectively. The mark-to-market valuation of outstanding natural gas forward contracts at June 30, 2006 and December 31, 2005 resulted in a liability of \$0.2 million and an asset of \$0.3 million, respectively. The mark-to-market adjustments are recorded in "Other Operating Income/Expense."

11. GUARANTEES

The Company provides financial guarantees as required by creditors, insurance programs and foreign governmental agencies. As of June 30, 2006, the following financial guarantees were outstanding:

	Maximum Potential Payment	Carrying Amount of Liability
Standby letters of credit (1)	\$ 79,136	\$ 61,509
Guarantees (2) and (3)	8,045	96
Surety bonds (4)	7,239	1,701
Total	<u>\$ 94,420</u>	<u>\$ 63,306</u>

(1) Approximately \$62 million of the standby letters of credit serve as credit support for industrial revenue bonds. The remaining letters of credit support obligations under various insurance related agreements, primarily workers' compensation and pollution liability policy requirements. These letters of credit expire at various dates during 2006 and 2007 and are typically renewed as required.

(2) In conjunction with the sale of RNZ's timberlands to the JV in October 2005, the Company guaranteed five years of Crown Forest license obligations. The JV is the primary obligor and has posted a bank performance bond with the New Zealand government. If the JV fails to pay the obligation, the New Zealand government will demand payment from the bank that posted the bond. The Company would have to perform if the bank defaulted on the bond. A \$54 thousand liability, representing Rayonier's obligation to perform, was recorded in accordance with FASB Interpretation No. 45, *Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others*. As of June 30, 2006, four annual payments of \$1.0 million each remain. This guarantee expires in 2010.

In conjunction with the sale of its New Zealand East Coast timber operations in 2002, the Company guaranteed five years of Crown Forest license obligations. In late 2003, the buyer defaulted on its loan payments to its creditors and went into receivership with the 2004 obligation paid by the receiver. The property was then re-sold. The new owner is the primary obligor and has posted a bank performance bond with the New Zealand government. If the new owner fails to pay the obligations, the New Zealand government will demand payment from the owner's bank pursuant to the bond. The Company would have to perform under the guarantee and seek legal redress from the owner if the owner's bank defaulted on the bond. The Company expects the owner's bond to be sufficient to cover the license obligations. As of June 30, 2006, one annual payment, estimated at \$1.3 million, remains. This guarantee expires in 2007.

In conjunction with a timberland sale and note monetization in the first quarter of 2004, the Company issued a make-whole agreement pursuant to which it guaranteed \$2.5 million of obligations of a qualified special purpose entity that was established to complete the monetization. At June 30, 2006 and December 31, 2005, the Company had a liability of \$43 thousand to reflect the fair market value of its obligation to perform under the make-whole agreement.

(3) In conjunction with the Company's \$250 million revolving credit facility, Rayonier guarantees the borrowings of RFR and Rayonier TRS Holdings Inc. (TRS). Additionally, TRS guarantees the borrowings of Rayonier Inc. At June 30, 2006 and December 31, 2005, there were no outstanding borrowings covered by these guarantees.

(4) Rayonier has issued surety bonds primarily to secure timber harvesting obligations in the State of Washington and to provide collateral for the Company's workers' compensation self-insurance program in that state. These surety bonds expire at various dates during 2006 and 2007 and are renewed as required.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

12. CONTINGENCIES

From time to time, Rayonier may become liable with respect to pending and threatened litigation and environmental and other matters. The following updates or repeats commentary included in the 2005 Annual Report on Form 10-K.

Legal Proceedings

The Company is involved in various legal actions, including those involving environmental matters that are discussed more fully in Note 13 - *Reserves for Dispositions and Discontinued Operations*. While the ultimate results of these legal actions and related claims cannot be determined, the Company does not expect that they will have a material adverse effect on its consolidated financial position or results of operations.

Between 1985 and 1995, Southern Wood Piedmont Company (SWP, a wholly-owned subsidiary of the Company) sent contaminated soil excavated in connection with the cleanup of various closed wood processing sites to a third-party processor in Louisiana for recycling. The processing facility, referred to as the Marine Shale Processors (MSP) facility, closed in 1995 and has been the subject of a variety of environmental related charges and a lawsuit brought by the U.S. Department of Justice (DOJ), the U.S. Environmental Protection Agency (EPA) and the State of Louisiana, through its Department of Environmental Quality (LDEQ), in United States District Court for the Western District of Louisiana (the Court) against the owner of the processing facility. Also in dispute is disposal liability for approximately 150,000 tons of recycled material from sites operated by SWP that were placed at another site, referred to as the RPI site, which is owned by an affiliate of the owner of the MSP facility. SWP, DOJ, EPA and LDEQ have been engaged in discussions regarding a settlement of this matter. A trial had been scheduled for June of 2006, in which DOJ, EPA and LDEQ were primarily asserting claims for cost recovery under the U.S. Comprehensive Environmental Response, Compensation and Liability Act of 1980 (CERCLA) in respect of the investigation and remediation of the MSP facility and the RPI site. In advance of the scheduled June 2006 trial date, the Company reached a settlement with DOJ, EPA and LDEQ under which SWP will oversee and pay for certain remedial activities to be performed at the RPI site, and pay DOJ and LDEQ \$0.2 million. In exchange for these commitments, the Company will receive, among other things, a "covenant not to sue" from DOJ, EPA and LDEQ for any claims relating to the MSP facility and the RPI site, and contribution protection under the applicable provisions of CERCLA against suits by third parties relating thereto. This settlement, which was reflected in a consent decree lodged with the Court on June 6, 2006, is expected to receive final approval of the Court shortly after closure of the public comment period on July 31, 2006. The Company believes that its reserves at June 30, 2006 adequately reflect the probable costs to be incurred through the ultimate completion of the Company's obligations under the consent decree.

In 1998, EPA and the New Jersey Department of Environmental Protection (DEP) filed separate lawsuits against Rayonier Inc., and approximately 30 other defendants, in the U.S. District Court, District of New Jersey, seeking recovery of current and future response costs and natural resource damages under applicable federal and state law relating to a contaminated landfill in Chester Township, New Jersey, referred to as Combe Fill South (Combe). It is alleged that the Company's former Eastern Research Division (ERD) in Whippany, New Jersey sent small quantities of dumpster waste, via a contract hauler, to Combe in the 1960s and early 1970s. The Company is working with other defendants in a joint defense group, which subsequently filed third-party actions against over 200 parties seeking contribution. A court-ordered, nonbinding alternative dispute resolution process is ongoing and in March of 2006 a court-appointed neutral issued a report and recommendations, which are currently being reviewed by all parties. Settlement discussions have not substantially progressed to date, but may commence now that the neutral's report has been issued. The Company believes that its reserves at June 30, 2006 adequately reflect the probable costs to be incurred upon the ultimate resolution of these matters.

The Company received an April 22, 2005 letter from the Environmental Protection Division of the Georgia Department of Natural Resources (EPD), which identified it as a responsible party under the Georgia Hazardous Site Response Act for potential polychlorinated biphenyl (PCB) contamination allegedly originating from a third-party owned site in Jesup, Georgia. Approximately 60 other parties received similar letters. It is unclear at this time as to the nature, extent or scope of any potential contamination at the site. The Company is currently unable to estimate the amount and probability of any potential exposure.

In the third quarter of 2005, the Company advised EPD of the results of certain testing undertaken by the Company at its Jesup, Georgia mill. This testing related to potential non-capture of certain methanol emissions during a particular stage of the mill's pulp manufacturing process. The potential non-capture at issue appears to have taken place during portions of three years between 2001 and 2004. While the Company's position is that no applicable law or regulation has been violated, EPD was voluntarily notified by the Company. To date, no notices of violation or citations have been issued by EPD. Discussions with EPD over this matter are ongoing, and there can be no assurances as to the outcome. The Company believes that its reserves at June 30, 2006 adequately reflect the probable costs to be incurred upon the ultimate resolution of this matter.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

The Company and the Board of Assessors of Wayne County, Georgia (the County) executed an agreement which, among other things, provided that the parties would resolve a property tax dispute relating to the Jesup mill property for the tax years 2002 to 2004 through binding arbitration. On December 22, 2004, the arbitration agreement was approved by the Georgia Superior Court (the Court). On September 10, 2005, after completion of six-day arbitration, the Company received a favorable arbitration ruling. The arbitrators' decision resulted in the County owing the Company a refund of approximately \$5.1 million for excess taxes paid. Additionally, the decision would allow the Company to reverse its \$2.8 million accrued property tax balance. In December 2005, the County filed motions with the Court claiming that it did not have the power and authority to enter into the arbitration agreement with Rayonier, and that the arbitrators' decision should be vacated. On March 24, 2006, the Court upheld the validity of the arbitration agreement (with the exception of one provision governing the calculation of certain future years' taxes, which does not affect the amount of the refund for 2002 to 2004 tax years), and confirmed the decision rendered by the panel of arbitrators. The County filed an appeal of the Court's decision. In July, the Company and the County reached an agreement in principle to resolve this dispute, subject to mutual agreement on final documentation. The tentative agreement, among other things, establishes a fair market value assessment for the mill and research and development facility for each of the years 2002 through 2006, and a framework for computing the fair market value of these properties for years 2007 through 2011. The tentative agreement would also resolve several other ancillary issues related to this matter. The proposed settlement will require approvals of the Wayne County Commission and Board of Assessors. Based on this tentative agreement, and in compliance with SFAS No. 5, *Accounting for Contingencies*, no adjustment for taxes previously accrued has been recorded in the Company's financial statements as of June 30, 2006.

Environmental Matters

Rayonier is subject to stringent environmental laws and regulations concerning air emissions, water discharges and waste handling and disposal. Such environmental laws and regulations include the Federal Clean Air Act, the Clean Water Act, the Resource Conservation and Recovery Act, CERCLA and similar state laws and regulations. Management closely monitors its environmental responsibilities, and believes that the Company is in substantial compliance with current environmental requirements. In addition to ongoing compliance with laws and regulations, the Company's facilities operate in accordance with various permits, which are issued by state and federal environmental agencies. Many of these permits impose operating conditions on the Company which require significant expenditures to ensure compliance. In addition, upon renewal and renegotiation of these permits, the issuing agencies often seek to impose new or additional conditions in response to new environmental laws and regulations, or more stringent interpretations of existing laws and regulations. It is the opinion of management that substantial expenditures over the next ten years will be required in the area of environmental compliance. During 2006 and 2007, Rayonier expects spending on environmental capital projects, exclusive of discontinued operations described in Note 13 - *Reserves for Dispositions and Discontinued Operations*, to be approximately \$4 million and \$2 million, respectively.

The EPA finalized its Cluster Rules governing air emissions in 1998 but, due to the specialty nature of Rayonier's Performance Fibers products and operations, the agency postponed finalizing water discharge rules and certain air emissions rules governing the Company's two Performance Fibers dissolving pulp mills and two other similar mills. (The EPA uses the term "Cluster Rules" to identify parallel rule-making for water and air technology-based discharge limits for pulp and paper mills.) In late 2003, the EPA informed Rayonier that it was delegating its Cluster Rule rulemaking authority for these four mills to the environmental agencies of the respective states. Rayonier will continue to work with the EPA and the applicable state environmental authorities to establish such rules for its mills, but the timing and costs associated with such rulemaking are uncertain. In the opinion of management, capital costs to be incurred over the next five years (2006—2010) associated with Cluster Rule compliance and other environmental regulations are not expected to exceed \$21 million. Such capital expenditures are not expected to cause total capital expenditures of the Company to exceed an annual average of \$90 million to \$100 million.

Federal, state and local laws and regulations intended to protect threatened and endangered species, as well as wetlands and waterways, limit and may in certain cases prevent timber harvesting, road construction and other activities on private lands, including a portion of the Company's timberlands. Over the past several years, the harvest of timber from the Company's timberlands in the State of Washington has been restricted as a result of the listing of the northern spotted owl, the marbled murrelet and several species of salmon and trout as threatened species under the Endangered Species Act. In 1999, the timber industry and federal, state, local and tribal governments, entered into an agreement, known as the Forests and Fish Report, which led the Washington Forest Practices Board to adopt rules further restricting timber harvesting within buffers along streams with fish habitat. All of these restrictions have caused Rayonier over time to restructure and reschedule its harvest plans and have reduced the total volume of timber available for future harvest.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

13. RESERVES FOR DISPOSITIONS AND DISCONTINUED OPERATIONS

The Company's dispositions and discontinued operations include Rayonier's Port Angeles, WA mill, which was closed in 1997; SWP, which ceased operations in 1989 except for remedial activities; ERD, which ceased operations in 1981; and other miscellaneous assets held for disposition. SWP has been designated a potentially responsible party (PRP), or has had other claims made against it, under CERCLA and/or comparable state statutes relating to ten former wood processing sites which are no longer operating.

An analysis of activity in the reserves for dispositions and discontinued operations for the six months ended June 30, 2006 and the year ended December 31, 2005, is as follows:

	<u>June 30, 2006</u>	<u>December 31, 2005</u>
Balance, January 1,	\$ 140,382	\$ 146,054
Expenditures charged to reserves	(5,108)	(8,697)
Additions to reserves	638	3,025
Balance, end of period	135,912	140,382
Less: Current portion	(11,844)	(12,422)
Non-current portion	<u>\$124,068</u>	<u>\$ 127,960</u>

Rayonier has identified specific reserves for three SWP sites (Augusta, GA, Spartanburg, SC, and East Point, GA) and Port Angeles, WA as material and requiring separate disclosure which was presented in the Company's 2005 Annual Report on Form 10-K. There have not been any significant changes in these sites' reserve requirements for the six months ended June 30, 2006, and therefore separate disclosure is not presented herein; however, in the second quarter, we recorded a charge of \$0.6 million relating to additional investigation to be performed in connection with the Port Angeles, WA site. For an analysis of the reserve activity for the three years ended December 31, 2005 and a brief description of these individually material sites, see the Company's 2005 Annual Report on Form 10-K, Note 15 to Consolidated Financial Statements.

Rayonier currently estimates that expenditures for environmental remediation, monitoring and other costs for all dispositions and discontinued operations in 2006 and 2007 will approximate \$12 million each year. Such costs will be charged against reserves for dispositions and discontinued operations, which include environmental investigation, remediation and monitoring costs. The Company believes established reserves are sufficient for costs expected to be incurred over the next 20 years with respect to its dispositions and discontinued operations. Remedial actions for these sites vary, but can include, among other remedies, removal of contaminated soils, groundwater recovery and treatment systems, and source remediation and/or control.

In addition, the Company is exposed to the risk of reasonably possible additional losses in excess of the established reserves. As of June 30, 2006, this amount could range up to \$29 million and arises from uncertainty over the effectiveness of remedial measures, changes in remediation technology, additional contamination that may be discovered, changes in applicable law and the exercise of discretion in interpretation of applicable law and regulations by governmental agencies.

The reliability and precision of cost estimates for these sites and the amount of actual future environmental costs can be impacted by various factors, including but not limited to significant changes in discharge volumes, requirements to perform additional or different remediation, changes in environmental remediation technology, the extent of groundwater contamination migration, additional findings of contaminated soil or sediment off-site, remedy selection, and the outcome of negotiations with federal and state agencies. Additionally, a site's potential for Brownfields (environmentally impacted site considered for re-development), or other similar projects, could accelerate expenditures as well as impact the amount and/or type of remediation required, as could new laws, regulations and the exercise of discretion in interpretation of applicable law and regulations by governmental agencies. For example, regulatory agencies in Washington and Florida are currently proposing new rules that, if fully implemented, would tighten the remedial standards for certain contaminants present in on- and off-site soils. Based on information currently available, the Company does not believe that any future changes in estimates, if necessary, would materially affect its consolidated financial position or results of operations.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

14. EMPLOYEE BENEFIT PLANS

The Company has four qualified non-contributory defined benefit pension plans covering substantially all of its employees and an unfunded plan that provides benefits in excess of amounts allowable under current tax law in the qualified plans. Certain plans are subject to union negotiation. Employee benefit plan liabilities are calculated using actuarial estimates and management assumptions. These estimates are based on historical information, along with certain assumptions about future events. Changes in assumptions, as well as changes in actual experience, could cause the estimates to change.

The Company has closed enrollment in its pension and postretirement medical plans to new salaried employees hired after December 31, 2005. New salaried employees will automatically be enrolled in the Company's 401(k) plan and receive an enhanced contribution.

The net periodic benefit cost for the Company's pension and postretirement plans for the three and six months ended June 30, 2006 and 2005 are shown in the following tables:

Components of Net Periodic Benefit Cost

	<u>Pension</u>		<u>Postretirement</u>	
	<u>Three Months Ended</u>		<u>Three Months Ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Service cost	\$ 2,046	\$ 1,825	\$ 206	\$ 152
Interest cost	3,631	3,250	680	540
Expected return on plan assets	(4,295)	(3,550)	—	—
Amortization of prior service cost	396	350	315	71
Amortization of losses	1,350	1,125	270	264
Net periodic benefit cost	<u>\$ 3,128</u>	<u>\$ 3,000</u>	<u>\$ 1,471</u>	<u>\$ 1,027</u>

	<u>Pension</u>		<u>Postretirement</u>	
	<u>Six Months Ended</u>		<u>Six Months Ended</u>	
	<u>June 30,</u>		<u>June 30,</u>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
Service cost	\$ 3,981	\$ 3,650	\$ 385	\$ 303
Interest cost	7,064	6,500	1,266	1,077
Expected return on plan assets	(8,357)	(7,100)	—	—
Amortization of prior service cost	770	700	386	141
Amortization of losses	2,627	2,250	611	526
Net periodic benefit cost	<u>\$ 6,085</u>	<u>\$ 6,000</u>	<u>\$ 2,648</u>	<u>\$ 2,047</u>

The Company does not have any required pension plan contributions for 2006; however, the Company anticipates making discretionary pension contributions ranging from \$11 million to \$15 million in 2006.

RAYONIER INC. AND SUBSIDIARIES
NOTES TO CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
(Unaudited)
(Dollars in thousands unless otherwise stated)

15. ACCUMULATED OTHER COMPREHENSIVE INCOME (LOSS)

Accumulated Other Comprehensive Income (Loss) was comprised of the following as of June 30, 2006 and December 31, 2005:

	<u>June 30, 2006</u>	<u>December 31, 2005</u>
Foreign currency translation adjustments	\$ 15,361	\$ 24,065
Minimum pension liability adjustments, net of tax	(16,461)	(16,461)
Total	<u>\$ (1,100)</u>	<u>\$ 7,604</u>

During the six months ended June 30, 2006, the decrease in net foreign currency translation adjustments was primarily due to the change in the New Zealand to U.S. dollar exchange rate.

16. SUBSEQUENT EVENT

On July 21, 2006, the Company's Board of Directors declared a third quarter cash dividend of 47 cents per common share, payable September 29, 2006, to shareholders of record on September 8, 2006.

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations

Safe Harbor

Except for historical information, the statements made in this Form 10-Q are "forward-looking statements" made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995 and other federal securities laws. These forward-looking statements, which include statements regarding anticipated markets and market growth, earnings, cash flow, revenues, contracts, volumes, demand, pricing, costs, cost structure and other statements relating to Rayonier's financial and operational performance, in some cases are identified by the use of words such as "may," "will," "should," "expect," "estimate," "believe," "anticipate," and other similar language. The following important factors, among others, could cause actual results to differ materially from those expressed in the forward-looking statements contained in this release: changes in global market trends and world events; interest rate and currency movements; fluctuations in demand for, or supply of, cellulose specialty products, absorbent materials, timber, wood products or real estate and entry of new competitors into these markets; adverse weather conditions affecting production, timber availability and sales, or distribution; changes in production costs for wood products or performance fibers, particularly for raw materials such as wood, energy and chemicals; unexpected delays in the entry into or closing of real estate sale transactions; changes in law or policy that might condition, limit or restrict the development of real estate; the ability of the Company to identify and complete timberland and higher-value real estate acquisitions; the Company's ability to continue to qualify as a REIT; the ability of the Company to complete tax-efficient exchanges of real estate; and implementation or revision of governmental policies and regulations affecting the environment, endangered species, import and export controls or taxes, including changes in tax laws that could reduce the benefits associated with REIT status. For additional factors that could impact future results, please see the Company's most recent Form 10-K on file with the Securities and Exchange Commission. Rayonier assumes no obligation to update these statements except as may be required by law.

Critical Accounting Policies and Use of Estimates

The preparation of our consolidated financial statements requires us to make estimates, assumptions and judgments that affect our assets, liabilities, revenues and expenses and disclosure of contingent assets and liabilities. We base these estimates and assumptions on historical data and trends, current fact patterns, expectations and other sources of information we believe are reasonable. Actual results may differ from these estimates under different conditions. For a full description of our critical accounting policies, see Item 7 – *Management's Discussion and Analysis of Financial Condition and Results of Operations* in the 2005 Annual Report on Form 10-K.

Segment Information

We operate in four reportable business segments as defined by SFAS No. 131, *Disclosures about Segments of an Enterprise and Related Information*: Timber, Real Estate, Performance Fibers, and Wood Products. Timber sales include all activities that relate to the harvesting of timber. Real Estate sales include the sale of all properties, including those designated for higher and better use (HBU). In the future, the Real Estate segment may include revenue generated from properties with entitlements and infrastructure improvements, some of which may be through joint ventures. The assets of the Real Estate segment include HBU property held by TerraPointe, the Company's real estate subsidiary, and timberlands under contract previously reported in the Timber segment. Allocations of depletion expense and non-cash costs of real estate sold are recorded when the Real Estate segment sells an asset from the Timber segment. The Performance Fibers segment includes two major product lines, Cellulose Specialties and Absorbent Materials. The Wood Products segment is comprised of the lumber operations. Our remaining operations include purchasing, harvesting and selling timber acquired from third parties (log trading) and trading wood products. As permitted by SFAS No. 131, these operations are combined and reported in an "Other" category. Sales between operating segments are made based on fair market value and intercompany profit or loss is eliminated in consolidation. We evaluate financial performance based on the operating income of the segments.

Operating income/(loss), as stated in the following table and presented in the Consolidated Statements of Income and Comprehensive Income, is equal to segment income/(loss). The income/(loss) items below "Operating income" in the Consolidated Statements of Income and Comprehensive Income are not allocated to segments. These items, which include interest, miscellaneous income/(expense), income tax (expense)/benefit and the gain on sale of a portion of the New Zealand joint venture (JV), are not considered by management to be part of segment operations.

[Table of Contents](#)

In 2005, we entered into a JV with RREEF Infrastructure, the global infrastructure investing arm of Deutsche Asset Management, under which the JV purchased approximately 354,000 acres of New Zealand timberlands, including 118,000 acres from Rayonier. Our investment at June 30, 2006 of \$55.9 million represents a 40 percent equity interest, which was reduced from 49.7 percent due to a sale in the second quarter. In addition to having an equity investment, we manage the JV's 354,000 acres of timberlands for a fee. The JV is included in the Timber segment. See Note 8 – *Joint Venture Investment* for additional information on the JV.

In August 2005, we sold our MDF business and the operations are now shown as discontinued operations (see Note 7 – *Sale of Medium-Density Fiberboard Business (MDF)*). These operations were previously included in the Wood Products segment, which has been restated to exclude the operations and assets of MDF for all periods presented.

[Table of Contents](#)
Results of Operations, Three and Six Months Ended June 30, 2006 Compared to Three and Six Months Ended June 30, 2005.

Financial Information (in millions)	Three Months Ended June 30,		Six Months Ended June 30,	
	2006	2005	2006	2005
Sales				
Timber	\$ 61.1	\$ 54.5	\$ 115.5	\$ 106.4
Real Estate				
Development	0.1	5.2	6.5	11.3
Rural	17.7	8.9	24.4	26.4
Other	—	0.6	—	0.6
Total Real Estate	17.8	14.7	30.9	38.3
Performance Fibers				
Cellulose Specialties	126.4	108.0	233.1	209.1
Absorbent Materials	39.4	45.2	78.7	87.1
Total Performance Fibers	165.8	153.2	311.8	296.2
Wood Products	32.2	36.4	63.8	66.9
Other operations	35.3	31.5	67.4	57.8
Intersegment Eliminations	(0.1)	—	(0.1)	(0.3)
Total Sales	\$ 312.1	\$ 290.3	\$ 589.3	\$ 565.3
Operating Income (Loss)				
Timber	\$ 29.8	\$ 23.1	\$ 53.6	\$ 46.8
Real Estate	10.9	10.7	21.1	26.0
Performance Fibers	15.7	18.5	26.0	30.9
Wood Products	2.0	5.8	4.6	9.0
Other operations	0.4	(0.4)	—	(0.2)
Corporate and other expenses / eliminations	(7.8)	(8.8)	(17.0)	(16.3)
Total Operating Income	51.0	48.9	88.3	96.2
Gain on sale of portion of New Zealand JV	7.8	—	7.8	—
Interest Expense	(11.9)	(12.8)	(24.1)	(25.1)
Interest / Other income	1.8	1.0	4.0	1.5
Income tax (expense) benefit	(5.9)	4.5	(9.9)	3.8
Income from Continuing Operations	42.8	41.6	66.1	76.4
Loss from Discontinued Operations	—	(24.7)	—	(25.1)
Net Income	\$ 42.8	\$ 16.9	\$ 66.1	\$ 51.3
Diluted Earnings Per Share	\$ 0.55	\$ 0.22	\$ 0.85	\$ 0.67

Timber

Sales for the three and six months ended June 30, 2006 increased from the prior year periods by approximately \$7 million and \$9 million, respectively, as higher sales in the Southeast and Northwest regions more than offset the change in New Zealand operations. Beginning in the fourth quarter of 2005, the New Zealand timber operations consist of a JV which we currently hold a 40 percent investment and management of the timberlands. Our investment is accounted for under the equity method and our equity in the earnings/loss of the JV is included in timber operating income.

In the Southeast, sawlog demand was strong earlier in 2006, but significantly softened in the second quarter. As a result, our harvested volumes increased 2 percent for the six month period, but were down 4 percent for the quarter. The decline in demand had minimal impact on sales price as 90 percent of the timber was under contract. Average prices for the three and six months ended June 30, 2006 were 10 percent and 13 percent above prior year periods.

The Northwest's prices and volume increased 4 percent and 29 percent, respectively, for the second quarter and 6 percent and 13 percent, respectively, for the six month period. Market prices rose as spring flooding limited log supply and a weaker US dollar reduced Canadian imports.

Sales (in millions)	2005	Changes Attributable to:			2006
		Price	Volume/Mix	Other*	
Three months ended June 30,					
Total Sales	<u>\$ 54.5</u>	<u>\$3.3</u>	<u>\$ 7.2</u>	<u>\$ (3.9)</u>	<u>\$ 61.1</u>
Six months ended June 30,					
Total Sales	<u>\$106.4</u>	<u>\$7.9</u>	<u>\$ 7.2</u>	<u>\$ (6.0)</u>	<u>\$115.5</u>

* Includes the impact of RNZ's 2005 sales.

Operating income was above prior year periods due to price and volume improvements in our Southeast and Northwest regions.

Operating Income (in millions)	2005	Changes Attributable to:			2006
		Price	Volume/Mix	Cost/Other	
Three months ended June 30,					
Total Operating Income	<u>\$23.1</u>	<u>\$3.3</u>	<u>\$ 4.6</u>	<u>\$ (1.2)</u>	<u>\$29.8</u>
Six months ended June 30,					
Total Operating Income	<u>\$46.8</u>	<u>\$7.9</u>	<u>\$ 4.2</u>	<u>\$ (5.3)</u>	<u>\$53.6</u>

Real Estate

Our real estate holdings in the Southeast have been segregated into two groups; development properties and rural properties. Development properties are predominantly located in the eleven coastal counties between Savannah, GA and Daytona Beach, FL, while the rural properties essentially include the balance of our ownership in the Southeast. Our Northwest real estate sales comprise the Other category.

During the second quarter of 2006, sales increased by approximately \$3 million and operating income improved slightly over the prior year period as significantly higher rural sales offset reduced development sales. For the six months ended June 30, 2006, sales and operating income declined approximately \$7 million and \$5 million, respectively, over the prior year. The nature of real estate sales is such that year over year fluctuations may be material due to the uncertain timing of entry into and closure of transactions.

[Table of Contents](#)

Sales (in millions)	2005	Changes Attributable to:		2006
		Price	Volume	
Three months ended June 30,				
Development	\$ 5.2	\$ —	\$ (5.1)	\$ 0.1
Rural	8.9	0.8	8.0	17.7
Other	0.6	—	(0.6)	—
Total Sales	<u>\$14.7</u>	<u>\$ 0.8</u>	<u>\$ 2.3</u>	<u>\$17.8</u>
Six months ended June 30,				
Development	\$11.3	\$ 3.2	\$ (8.0)	\$ 6.5
Rural	26.4	1.5	(3.5)	24.4
Other	0.6	—	(0.6)	—
Total Sales	<u>\$38.3</u>	<u>\$ 4.7</u>	<u>\$ (12.1)</u>	<u>\$30.9</u>
Operating Income (in millions)				
Three months ended June 30,				
Total Operating Income	<u>\$10.7</u>	<u>\$ 0.8</u>	<u>\$ (0.6)</u>	<u>\$10.9</u>
Six months ended June 30,				
Total Operating Income	<u>\$26.0</u>	<u>\$ 4.7</u>	<u>\$ (9.6)</u>	<u>\$21.1</u>

Performance Fibers

In the three and six months ended June 30, 2006, cellulose specialty sales improved by \$18 million and \$24 million, respectively. Market demand for cellulose specialties resulted in average price increases of \$93 per ton and \$87 per ton, or 10 percent and 9 percent, respectively. These price increases included a fuel oil surcharge of \$29 per ton on all acetate volume and other cellulose specialty volume allowable by contract totaling \$5 million for the six month period. Volumes also contributed favorably to sales, increasing from prior year periods primarily due to a timing shift in customers' orders.

Sales of absorbent materials decreased primarily due to the fourth quarter 2005 disposition of our Engineered Absorbent Materials (EAM) facility which contributed \$3.5 million and \$7.2 million in sales for the three and six months ended June 30, 2005. Excluding this impact, absorbent materials sales volume declined in the second quarter and first half of 2006 as we focused on selling greater volumes of cellulose specialties, a higher margin product.

Sales (in millions)	2005	Changes Attributable to:			2006
		Price	Volume/Mix	Other *	
Three months ended June 30,					
Cellulose Specialties	\$108.0	\$11.2	\$ 7.2	\$ —	\$126.4
Absorbent Materials	45.2	0.3	(2.9)	(3.2)	39.4
Total Sales	<u>\$153.2</u>	<u>\$11.5</u>	<u>\$ 4.3</u>	<u>\$ (3.2)</u>	<u>\$165.8</u>
Six months ended June 30,					
Cellulose Specialties	\$209.1	\$19.5	\$ 4.5	\$ —	\$233.1
Absorbent Materials	87.1	1.1	(3.0)	(6.5)	78.7
Total Sales	<u>\$296.2</u>	<u>\$20.6</u>	<u>\$ 1.5</u>	<u>\$ (6.5)</u>	<u>\$311.8</u>

* Includes the impact of EAM's 2005 sales.

[Table of Contents](#)

For the periods presented, operating income in 2006 declined by \$2.8 million and \$4.9 million from the prior year periods due to increases in raw materials, energy and scheduled maintenance costs. Also negatively impacting operating income was an additional \$1 million in costs associated with unexpected equipment repairs.

Operating Income (in millions)

	2005	Changes Attributable to:			2006	
		Price	Volume/Mix	Costs	Other*	
Three months ended June 30,						
Total Operating Income	<u>\$18.5</u>	<u>\$11.5</u>	<u>\$ 1.1</u>	<u>\$(17.0)</u>	<u>\$ 1.6</u>	<u>\$15.7</u>
Six months ended June 30,						
Total Operating Income	<u>\$30.9</u>	<u>\$20.6</u>	<u>\$ 0.5</u>	<u>\$(28.0)</u>	<u>\$ 2.0</u>	<u>\$26.0</u>

* Includes the impact of EAM's 2005 operating income.

Wood Products

Lumber sales decreased compared to the prior year periods primarily due to lower prices. Prices declined by 14 percent and 7 percent, respectively, for the three and six months ended June 30, 2006 as a result of reduced demand in the housing market.

Sales (in millions)

	2005	Changes Attributable to:			2006
		Price	Volume/Mix	Other	
Three months ended June 30,					
Total Sales	<u>\$36.4</u>	<u>\$(5.3)</u>	<u>\$ 0.9</u>	<u>\$ 0.2</u>	<u>\$32.2</u>
Six months ended June 30,					
Total Sales	<u>\$66.9</u>	<u>\$(4.9)</u>	<u>\$ 1.2</u>	<u>\$ 0.6</u>	<u>\$63.8</u>

For the three and six months ended June 30, 2006, operating income decreased from the prior year periods due to lower selling prices.

Operating Income (in millions)

	2005	Changes Attributable to:			2006	
		Price	Volume/Mix	Costs	Other	
Three months ended June 30,						
Total Operating Income	<u>\$5.8</u>	<u>\$(5.3)</u>	<u>\$ 0.2</u>	<u>\$ 0.5</u>	<u>\$ 0.8</u>	<u>\$2.0</u>
Six months ended June 30,						
Total Operating Income	<u>\$9.0</u>	<u>\$(4.9)</u>	<u>\$ 0.2</u>	<u>\$(0.7)</u>	<u>\$ 1.0</u>	<u>\$4.6</u>

Other Operations

Sales of \$35 million and \$67 million for the three and six months ended June 30, 2006, respectively, were \$4 million and \$10 million higher than the prior year periods due to stronger trading activity. We have no immediate plans to exit these non-core businesses.

Corporate and Other Expenses / Eliminations

Corporate and Other Expenses of \$7.8 million declined by \$1 million in the second quarter from the prior year period due to lower expense relating to stock based incentive compensation. Expenses increased \$0.7 million in the six months ended June 30, 2006 compared to the prior year periods primarily due to higher expense relating to stock based incentive compensation in the first quarter of 2006 related to our adoption of SFAS No. 123(R). See Note 3 – *Incentive Stock Plans* for additional information.

[Table of Contents](#)

Gain on Partial Sale of New Zealand JV

In the second quarter of 2006, we sold a portion of our interest in the New Zealand JV, reducing our investment from 49.7 percent to 40 percent. See Note 8 - *Joint Venture Investment* for details of the transaction.

Other Income / Expense

Interest expense declined for the three and six months ended June 30, 2006 compared to the prior year periods as lower average debt levels more than offset higher interest rates.

Interest/Other income of \$1.8 million and \$4.0 million for the three and six months ended June 30, 2006, respectively, improved by approximately \$0.8 million and \$2.5 million due to increased interest income resulting from higher cash levels in 2006.

Provision for Income Taxes from Continuing and Discontinued Operations

See Note 4 - *Income Taxes* of the Notes to the Condensed Consolidated Financial Statements set forth in Part I of this Report, which is hereby incorporated by reference.

Outlook

Third quarter 2006 results are expected to be above the second quarter (excluding special items), due to higher real estate sales partly offset by seasonally lower Northwest timber volume. In addition, earnings are anticipated to be above third quarter 2005 primarily due to increased real estate sales and higher cellulose specialties prices partly offset by lower lumber prices and higher performance fibers manufacturing costs.

Liquidity and Capital Resources

Cash Flow

Cash provided by operating activities of \$133 million for the six months ended June 30, 2006 was \$10 million above the prior year period, primarily due to reduced working capital requirements partly offset by lower operating income. Cash used for investing activities of \$48 million for the first six months of 2006 was \$2 million above 2005's comparable period. Capital expenditures and timberland purchases totaled \$66 million, an increase of \$22 million over the prior year period while restricted cash deposits increased by \$4 million in 2006, compared to a \$2 million increase in 2005. In addition, cash used for investing activities for the six months ended June 30, 2006 was reduced by \$22 million of proceeds from the sale of a portion of the New Zealand JV. Cash used for financing activities of \$66 million increased \$40 million during the six months ended June 30, 2006 reflecting the absence of \$28 million of short term debt borrowings, higher quarterly dividend payments which increased \$0.06 per share (adjusted for the October 17, 2005 stock-split), or \$10 million and \$3 million of lower proceeds from the exercise of stock options. This increase was partly offset by the classification of \$2 million of excess tax benefit from stock options in financing cash flows as a result of adopting SFAS No. 123(R). Cash and cash equivalents totaled \$165 million and \$146 million as of June 30, 2006 and December 31, 2005, respectively, and consisted primarily of marketable securities with maturities at date of acquisition of 90 days or less.

At June 30, 2006, debt was \$556 million, slightly below the December 31, 2005 balance of \$559 million. Our debt-to-capital ratio at June 30, 2006 remained at 39 percent.

There were no pension contributions made during the six months ended June 30, 2006 or 2005; however we anticipate making discretionary contributions ranging from \$11 million to \$15 million in the next six months. Income tax payments in the first six months of 2006 totaled \$10 million compared to \$6 million in 2005. We expect full year income tax payments to be \$30 million, approximately \$1 million above the prior year. We also expect 2006 capital expenditures, excluding strategic acquisitions, of approximately \$107 million. Pre-tax spending for environmental costs related to dispositions and discontinued operations during the six months ended was \$5 million; full year expenditures of approximately \$12 million are anticipated.

[Table of Contents](#)

Liquidity Performance Indicators

The discussion below is presented to enhance the reader's understanding of our ability to generate cash, our liquidity and our ability to satisfy rating agency and creditor requirements. This information includes two measures of financial results: Earnings from Continuing Operations before Interest, Taxes, Depreciation, Depletion and Amortization (EBITDA), and Adjusted Cash Available for Distribution (Adjusted CAD). These measures are not defined by Generally Accepted Accounting Principles (GAAP) and the discussion of EBITDA and Adjusted CAD is not intended to conflict with or change any of the GAAP disclosures. We consider these measures to be important to estimate the enterprise and shareholder values of Rayonier as a whole and of its core segments, and for allocating capital resources. In addition, analysts, investors and creditors use these measures when analyzing our financial condition and cash generating ability. EBITDA is defined by the Securities and Exchange Commission (SEC); however, Adjusted CAD as defined may not be comparable to similarly titled measures reported by other companies.

EBITDA and Adjusted CAD for the three and six months ended June 30, 2005 have been restated to exclude the discontinued operations of the MDF business. EBITDA is a non-GAAP measure of our operating cash generating capacity. For the three months ended June 30, 2006, EBITDA was \$92.4 million, \$7.2 million above the prior year period primarily due to favorable operating income in the Timber segment and the gain on sale of a portion of the New Zealand JV, partly offset by lower Performance Fibers and Wood Products operating results. EBITDA for the six months ended June 30, 2006 was \$162.5 million, \$5.9 million below the prior year period due to lower Performance Fibers, Real Estate and Wood Products operating income, partly offset by higher Timber segment earnings. Below is a reconciliation of Cash Provided by Operating Activities of Continuing Operations to EBITDA for the respective periods (in millions of dollars):

	Three Months Ended June 30,	
	2006	2005
Cash Provided by Operating Activities of Continuing Operations	\$ 82.3	\$ 47.4
Gain on sale of portion of New Zealand joint venture	7.8	—
Non-cash cost basis of real estate sold	(3.7)	(2.0)
Income tax expense (benefit)	5.9	(4.5)
Interest expense, net	9.9	11.6
Working capital changes	(1.5)	20.1
Other balance sheet changes	(8.3)	12.6
EBITDA	<u>\$ 92.4</u>	<u>\$ 85.2</u>

	Six Months Ended June 30,	
	2006	2005
Cash Provided by Operating Activities of Continuing Operations	\$ 133.1	\$ 122.9
Gain on sale of portion of New Zealand joint venture	7.8	—
Non-cash cost basis of real estate sold	(4.5)	(6.0)
Income tax expense (benefit)	9.9	(3.8)
Interest expense, net	19.9	23.3
Working capital changes	9.0	20.1
Other balance sheet changes	(12.7)	11.9
EBITDA	<u>\$ 162.5</u>	<u>\$ 168.4</u>

A non-cash expense of our Real Estate business is the non-cash cost basis of real estate sold. EBITDA plus the non-cash cost basis of real estate sold for the three and six months ended June 30, 2006 and 2005 totaled \$96.1 million and \$87.2 million and \$167.0 million and \$174.4 million, respectively.

[Table of Contents](#)

Adjusted CAD is a non-GAAP measure of cash generated during a period that is available for dividend distribution, repurchasing our common shares, debt reduction and for strategic acquisitions net of associated financing (e.g. realizing like-kind exchange benefits). We define Cash Available for Distribution (CAD) as Cash Provided by Operating Activities of Continuing Operations less capital spending, adjusted for equity based compensation amounts, proceeds from matured energy forward contracts, the tax benefits associated with certain strategic acquisitions and the change in committed cash. Prior to the adoption of SFAS No. 123(R) on January 1, 2006, the tax benefits from the exercise of stock options were included in cash provided by operating activities and therefore deducted to arrive at Adjusted CAD. Under SFAS No. 123(R), cash flows provided by excess tax benefits from stock-based compensation are required to be presented in the "Financing Activities" section of the Consolidated Statement of Cash Flows and are therefore no longer a reconciling item. Committed cash represents outstanding checks that have been drawn on our zero balance bank accounts but have not been paid. In compliance with SEC requirements for non-GAAP measures, we also reduce CAD by mandatory debt repayments resulting in the measure entitled "Adjusted CAD."

Adjusted CAD for the six months ended June 30, 2006 was \$80 million, \$14 million below the prior year period. The decrease is primarily due to higher capital spending on energy savings projects, offset by increased cash provided by operating activities. The Adjusted Cash Available for Distribution generated in the current period is not necessarily indicative of amounts that may be generated in future periods. Below is a reconciliation of Cash Provided by Operating Activities of Continuing Operations to Adjusted CAD (in millions of dollars):

	Six Months Ended	
	June 30,	
	2006	2005
Cash provided by Operating Activities of Continuing Operations	\$ 133.1	\$ 122.9
Capital spending	(61.6)	(43.7)
Proceeds from matured energy contracts	0.7	—
Decrease in committed cash	7.9	5.5
Equity-based compensation adjustments	4.2	—
Release of restricted cash	—	12.0
LKE tax benefits	(2.6)	(0.9)
Cash Available for Distribution	81.7	95.8
Mandatory debt repayments*	(1.5)	(1.5)
Adjusted Cash Available for Distribution	<u>\$ 80.2</u>	<u>\$ 94.3</u>

* No discretionary repayments were made during the six months ended June 30, 2006 and 2005.

Liquidity Facilities

In connection with our \$250 million revolving credit facility, certain covenants must be met, including ratios based on the facility's definition of EBITDA (Covenant EBITDA). Covenant EBITDA consists of earnings from continuing operations before the cumulative effect of accounting changes and any provision for dispositions, income taxes, interest expense, depreciation, depletion, amortization and the non-cash cost basis of real estate sold. In addition, there are covenant requirements in effect for RFR setting a minimum ratio of cash flow available for fixed charges to fixed charges. At June 30, 2006 and December 31, 2005 the available borrowing capacity was \$234 million under the revolving credit facility, due to \$16 million of standby letters of credit previously issued. The facility expires in November 2006 and we expect to refinance it with a new facility in the third quarter of 2006.

Covenant Funds from Operations (Covenant FFO), another facility covenant, is defined as Consolidated Net Income excluding gains or losses from debt restructuring and investments in marketable securities plus depletion, depreciation and amortization and the non-cash cost basis of real estate sold. This dividend restriction covenant limits the sum of dividends in any period of four fiscal quarters to 90 percent of Covenant FFO plus the aggregate amount of dividends permitted under Covenant FFO in excess of the amount of dividends paid during the prior four fiscal quarters.

[Table of Contents](#)

The covenants listed below are calculated on a trailing 12-month basis. The most restrictive long-term debt covenants in effect as of June 30, 2006 were as follows:

	<u>Covenant Requirement</u>	<u>Actual ratio at June 30, 2006</u>	<u>Favorable (Unfavorable)</u>
Covenant EBITDA to consolidated interest expense should not be less than	2.50 to 1	8.64	6.14
Total debt to Covenant EBITDA should not exceed	4.00 to 1	1.42	2.58
RFR cash flow available for fixed charges to RFR fixed charges should not be less than	2.50 to 1	4.08	1.58
Dividends paid should not exceed 90 percent of Covenant FFO	90%	42%	48%

We are currently in compliance with all of our financial covenants. In addition to the financial covenants listed above, the credit agreements include customary covenants that limit the incurrence of debt, the disposition of assets, and the making of certain payments between RFR and Rayonier among others. An asset sales covenant in the RFR installment note-related agreements requires us, subject to certain exceptions, to either reinvest cumulative timberland sales proceeds in excess of approximately \$100 million (the "excess proceeds") in timberland-related investments and activities or, once the amount of excess proceeds not reinvested exceeds \$50 million, to make an offer to the note holders to prepay the notes ratably in the amount of the excess proceeds. At June 30, 2006 and December 31, 2005 the amount of excess proceeds was approximately \$31 million.

Contractual Financial Obligations and Off-Balance Sheet Arrangements

No material changes to guarantees or financial instruments such as letters of credit and surety bonds occurred during the first six months of 2006. See Note 11 - *Guarantees*, for details on the letters of credit, surety bonds and total guarantees outstanding as of June 30, 2006.

Segment EBITDA

EBITDA is also used for evaluating segment cash return on investment, allocating resources and for valuation purposes. EBITDA by segment is a critical valuation measure used by the Chief Operating Decision Maker, existing shareholders and potential shareholders to measure how management is performing relative to the assets with which they have been entrusted. EBITDA by segment for the three and six months ended June 30, 2006 and 2005 was as follows (millions of dollars):

	<u>Three Months Ended June 30,</u>		<u>Six Months Ended June 30,</u>	
	<u>2006</u>	<u>2005</u>	<u>2006</u>	<u>2005</u>
EBITDA				
Timber	\$ 51.1	\$ 38.4	\$ 89.9	\$ 76.7
Real Estate	11.8	10.9	22.5	29.4
Performance Fibers	33.1	37.3	58.5	65.7
Wood Products	3.8	7.6	8.1	12.6
Other Operations	0.5	(0.2)	0.3	0.1
Corporate and other	(7.9)	(8.8)	(16.8)	(16.1)
Total	<u>\$ 92.4</u>	<u>\$ 85.2</u>	<u>\$162.5</u>	<u>\$168.4</u>

[Table of Contents](#)

The following tables reconcile Cash Provided by Operating Activities by segment to EBITDA by segment:

	Timber	Real Estate	Performance Fibers	Wood Products	Other Operations	Corporate and Other	Total
Three Months Ended June 30, 2006							
Cash provided by operating activities of continuing operations	\$ 53.1	\$ 18.7	\$ 14.8	\$ 6.3	\$ 7.1	\$ (17.7)	\$ 82.3
Less: Non-cash cost basis of real estate sold	—	(3.7)	—	—	—	—	(3.7)
Add: Gain on sale of portion of New Zealand JV	7.8	—	—	—	—	—	7.8
Income tax expense	—	—	—	—	—	5.9	5.9
Interest, net	—	—	—	—	—	9.9	9.9
Working capital increases (decreases)	(6.8)	(3.1)	18.2	(2.5)	(6.4)	(0.9)	(1.5)
Other balance sheet changes	(3.0)	(0.1)	0.1	—	(0.2)	(5.1)	(8.3)
EBITDA	<u>\$ 51.1</u>	<u>\$ 11.8</u>	<u>\$ 33.1</u>	<u>\$ 3.8</u>	<u>\$ 0.5</u>	<u>\$ (7.9)</u>	<u>\$ 92.4</u>
Three Months Ended June 30, 2005							
Cash provided by operating activities of continuing operations	\$ 37.4	\$ (0.4)	\$ 29.0	\$ 6.9	\$ 2.5	\$ (28.0)	\$ 47.4
Less: Non-cash cost basis of real estate sold	—	(1.7)	—	—	(0.3)	—	(2.0)
Income tax benefit	—	—	—	—	—	(4.5)	(4.5)
Add: Interest, net	—	—	—	—	—	11.6	11.6
Working capital increases (decreases)	(1.4)	10.9	8.3	0.7	(2.0)	3.6	20.1
Other balance sheet changes	2.4	2.1	—	—	(0.4)	8.5	12.6
EBITDA	<u>\$ 38.4</u>	<u>\$ 10.9</u>	<u>\$ 37.3</u>	<u>\$ 7.6</u>	<u>\$ (0.2)</u>	<u>\$ (8.8)</u>	<u>\$ 85.2</u>
Six Months Ended June 30, 2006							
Cash provided by operating activities of continuing operations	\$ 96.9	\$ 26.2	\$ 44.4	\$ 7.0	\$ 7.6	\$ (49.0)	\$ 133.1
Less: Non-cash cost basis of real estate sold	—	(4.5)	—	—	—	—	(4.5)
Add: Gain on sale of portion of New Zealand JV	7.8	—	—	—	—	—	7.8
Income tax expense	—	—	—	—	—	9.9	9.9
Interest, net	—	—	—	—	—	19.9	19.9
Working capital increases (decreases)	(2.3)	0.9	14.0	1.1	(7.3)	2.6	9.0
Other balance sheet changes	(12.5)	(0.1)	0.1	—	—	(0.2)	(12.7)
EBITDA	<u>\$ 89.9</u>	<u>\$ 22.5</u>	<u>\$ 58.5</u>	<u>\$ 8.1</u>	<u>\$ 0.3</u>	<u>\$ (16.8)</u>	<u>\$ 162.5</u>
Six Months Ended June 30, 2005							
Cash provided by operating activities of continuing operations	\$ 83.1	\$ 26.1	\$ 54.7	\$ 8.5	\$ (1.2)	\$ (48.3)	\$ 122.9
Less: Non-cash cost basis of real estate sold	—	(5.7)	—	—	(0.3)	—	(6.0)
Income tax benefit	—	—	—	—	—	(3.8)	(3.8)
Add: Interest, net	—	—	—	—	—	23.3	23.3
Working capital increases (decreases)	(6.2)	7.2	11.0	4.1	0.1	3.9	20.1
Other balance sheet changes	(0.2)	1.8	—	—	1.5	8.8	11.9
EBITDA	<u>\$ 76.7</u>	<u>\$ 29.4</u>	<u>\$ 65.7</u>	<u>\$ 12.6</u>	<u>\$ 0.1</u>	<u>\$ (16.1)</u>	<u>\$ 168.4</u>

[Table of Contents](#)

The following tables provide sales volumes by segment:

	Three Months Ended		Six Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Timber				
Northwest U.S., in millions of board feet	89	69	164	145
Southeast U.S., in thousands of short green tons	1,204	1,206	2,451	2,427
Real Estate				
Acres sold				
Development	7	1,006	751	2,526
Rural	9,613	5,031	12,273	14,179
Northwest U.S.	4	149	4	229
Total	9,624	6,186	13,028	16,934
Performance Fibers				
Sales Volume				
Cellulose specialties, in thousands of metric tons	121	113	225	220
Absorbent materials, in thousands of metric tons	63	69	128	136
Production as a percent of capacity	99.2%	100.1%	99.0%	99.8%
Lumber				
Sales volume, in millions of board feet	92	90	176	173

The following tables provide sales by geographic location:

	Three Months Ended		Six Months Ended	
	June 30, 2006	June 30, 2005	June 30, 2006	June 30, 2005
Geographical Data (Non-U.S.)				
Sales				
New Zealand	\$ 8.2	\$ 14.1	\$ 13.7	\$ 23.0
Other	3.7	2.8	8.2	5.5
Total	\$ 11.9	\$ 16.9	\$ 21.9	\$ 28.5
Operating income (loss)				
New Zealand	\$ (0.3)	\$ 1.0	\$ (1.4)	\$ 1.5
Other	(0.5)	(0.4)	(0.9)	(0.6)
Total	\$ (0.8)	\$ 0.6	\$ (2.3)	\$ 0.9
Timber				
Sales				
Northwest U.S.	\$ 35.2	\$ 26.0	\$ 62.3	\$ 52.3
Southeast U.S.	23.5	21.6	48.5	42.5
New Zealand	2.4	6.9	4.7	11.6
Total	\$ 61.1	\$ 54.5	\$ 115.5	\$ 106.4
Operating income				
Northwest U.S.	\$ 21.4	\$ 16.0	\$ 37.4	\$ 32.4
Southeast U.S.	8.8	5.8	17.7	12.2
New Zealand	(0.4)	1.3	(1.5)	2.2
Total	\$ 29.8	\$ 23.1	\$ 53.6	\$ 46.8

Item 3. Quantitative and Qualitative Disclosures about Market Risk

Market Risk

We are exposed to various market risks, including changes in interest rates, commodity prices and foreign exchange rates. Our objective is to minimize the economic impact of these market risks. We use derivatives in accordance with policies and procedures approved by the Finance Committee of the Board of Directors; derivatives are managed by a senior executive committee whose responsibilities include initiating, managing and monitoring resulting exposures. We do not enter into financial instruments for trading or speculative purposes.

Cyclical pricing of commodity market paper pulp ultimately influences prices of the Absorbent Materials product line in the Performance Fibers business. However, since we are a non-integrated producer of specialized Performance Fibers for non-papermaking end uses, our high-value product mix tends to lag (on both the upturn and downturn) commodity paper pulp prices with peaks and valleys that are less severe.

The fair market value of our long-term fixed interest rate debt is subject to interest rate risk; however, we intend to hold most of our debt until maturity. We periodically enter into interest rate swap agreements to manage exposure to interest rate changes. These swaps involve the exchange of fixed and variable interest rate payments without exchanging principal amounts. At June 30, 2006, we had two interest rate swap agreements, both maturing in 2007, which resulted in a liability with a fair market value of \$3.0 million. Generally, the fair market value of fixed-interest rate debt will increase as interest rates fall and decrease as interest rates rise.

We periodically enter into commodity forward contracts to fix some of our fuel oil and natural gas costs. The forward contracts partially mitigate the risk of a change in Performance Fibers margins resulting from an increase or decrease in these energy costs. A hypothetical 10 percent increase/decrease in the prevailing market price of natural gas and fuel oil would result in a change of \$0.2 million and \$0.4 million, respectively, in our pre-tax income. We do not enter into commodity forwards for trading or speculative purposes. The net amounts paid or received under the contracts are recognized as an adjustment to fuel oil or natural gas expense. Our natural gas and fuel oil contracts do not qualify for hedge accounting and as such mark-to-market adjustments are recorded in "Other operating income, net." See Note 10—*Financial Instruments* for outstanding forward contracts at June 30, 2006 as well as gains and losses recognized from such contracts.

Primarily all of our revenues and expenses are U.S. dollar-denominated. However, the JV is subject to the risks of foreign currency fluctuations (See Note 8 – *Joint Venture Investment* for additional information on the JV). At June 30, 2006, there were no outstanding forward foreign currency contracts to purchase New Zealand dollars.

For a full description of our market risk, please refer to Item 7, *Management Discussion and Analysis of Financial Condition and Results of Operations*, in the 2005 Annual Report on Form 10-K.

Item 4. Controls and Procedures

Rayonier management is responsible for establishing and maintaining adequate disclosure controls and procedures. Disclosure controls and procedures (as defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934 (the "Exchange Act")), are designed with the objective of ensuring that information required to be disclosed by the Company in reports filed under the Exchange Act, such as this quarterly report on Form 10-Q, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's rules and forms.

Because of the inherent limitations in all control systems, no control evaluation can provide absolute assurance that all control exceptions and instances of fraud have been prevented or detected on a timely basis. Even systems determined to be effective can provide only reasonable assurance that their objectives are achieved.

Based on an evaluation as of the end of the period covered by this quarterly report on Form 10-Q, our management, including the Chief Executive Officer and Co-Principal Financial Officers, concluded that the design and operation of the disclosure controls and procedures were effective as of June 30, 2006.

In the quarter ended June 30, 2006, based upon the evaluation required by paragraph (d) of Rules 13a-15 and 15d-15 of the Exchange Act, there were no changes in our internal controls over financial reporting that would materially affect or are reasonably likely to affect our internal control over financial reporting.

PART II. OTHER INFORMATION**Item 1. Legal Proceedings**

See Notes 12 and 13 of the Notes to Condensed Consolidated Financial Statements set forth in Part I of this Report, which are hereby incorporated by reference.

Item 1A. Risk Factors

There were no material changes from the risk factors previously disclosed in our Form 10-K for the year ended December 31, 2005. For a full description of these risk factors, please refer to Item 1A, *Risk Factors*, in the 2005 Annual Report on Form 10-K.

Item 2. Unregistered Sales of Equity Securities and Use of Proceeds

The Company is authorized, through its common share repurchase program, to repurchase 2,446,488 and 2,066,763 shares as of June 30, 2006 and 2005, respectively.

The following chart provides the required disclosures with regard to stock repurchases:

<u>Period</u>	<u>Total Number of Shares Purchased</u>	<u>Average Price Paid per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</u>	<u>Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased Under the Plans or Programs</u>
April 1, 2006 to April 30, 2006	—	\$ —	—	—
May 1, 2006 to May 31, 2006	12,000*	\$ 39.29	—	—
June 1, 2006 to June 30, 2006	—	\$ —	—	—
Total	<u>12,000</u>		<u>—</u>	<u>—</u>

* The Company issued 12,000 shares of restricted stock to its Board of Directors on May 19, 2006.

Item 3. Defaults Upon Senior Securities

Not applicable.

Item 4. Submission of Matters to a Vote of Security Holders

The Annual Meeting of Shareholders of the Company was held on May 18, 2006 (the "Annual Meeting"). At that meeting, three directors were elected as follows:

	<u>Votes For</u>	<u>Votes Withheld</u>
Directors of Class III, Terms Expire in 2009		
Richard D. Kincaid	68,100,753	908,068
W. Lee Nutter	67,835,690	1,179,131
Ronald Townsend	67,800,141	1,208,680

The following directors' terms of office also continued after the Annual Meeting: Ronald M. Gross, James H. Hance, Jr., Paul G. Kirk, Jr., Thomas I. Morgan, Katherine D. Ortega and Carl S. Sloane.

Item 5. Other Information

Not applicable.

[Table of Contents](#)

Item 6. Exhibits

3.2	By-laws	Incorporated by reference to Exhibit 3.2 from the Registrant's May 24, 2006 Form 8-K
10.1	Rayonier 1994 Incentive Stock Plan, as amended	Filed herewith
10.2	Rayonier 2004 Incentive Stock and Management Bonus Plan, as amended	Filed herewith
12	Statement re: computation of ratios	Filed herewith
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
31.2	Certification of the Co-Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
31.3	Certification of the Co-Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act	Filed herewith
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act	Furnished herewith

SIGNATURE

Pursuant to the requirements of Section 13 of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

RAYONIER INC. (Registrant)

BY: /s/ HANS E. VANDEN NOORT

Hans E. Vanden Noort
Senior Vice President and
Chief Accounting Officer

August 2, 2006

INDEX TO EXHIBITS

<u>Exhibit No.</u>	<u>Description</u>
3.2	By-laws: Incorporated by reference to Exhibit 3.2 from the Registrant's May 24, 2006 Form 8-K
10.1	Rayonier 1994 Incentive Stock Plan, as amended
10.2	Rayonier 2004 Incentive Stock and Management Bonus Plan, as amended
12	Statement re: computation of ratios
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act
31.2	Certification of the Co-Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act
31.3	Certification of the Co-Principal Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act
32	Certification pursuant to Section 906 of the Sarbanes-Oxley Act

RAYONIER INC.

4,500,000 Common Shares

RAYONIER 1994 INCENTIVE STOCK PLAN

PLAN INFORMATION

**THIS DOCUMENT CONSTITUTES PART OF A PROSPECTUS COVERING SECURITIES
THAT HAVE BEEN REGISTERED UNDER THE
SECURITIES ACT OF 1933.**

The Prospectus covers such additional securities as may be issuable as a result of anti-dilution provisions contained in the instruments pursuant to which securities covered by the Prospectus are issued.

**THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES
AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS
THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES
COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THE
PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A
CRIMINAL OFFENSE.**

As amended July 21, 2006

Additional information about the Plan and its administration may be obtained by writing the Manager of Stock Option Plan Administration, Rayonier Inc., 50 No. Laura Street, Jacksonville, FL 32202, or telephoning the Manager at (904) 357-9100.

Any statement contained in a document incorporated or deemed to be incorporated by reference in the Prospectus shall be deemed to be modified or superseded for purposes of the Prospectus to the extent that a statement contained in the Prospectus or in any other subsequently filed document which also is or is deemed to be incorporated by reference in the Prospectus modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of the Prospectus. Any such document, as well as Rayonier's most recent annual report to shareholders and any other report or communication distributed to Rayonier shareholders generally, may be obtained without charge by written request to W. Edwin Frazier, III, Corporate Secretary, Rayonier Inc., 50 No. Laura Street, Jacksonville, FL 32202, or by telephoning W. Edwin Frazier, III at (904) 357-9100.

TABLE OF CONTENTS

General Information	3
The Plan	3
Administration	13
Federal Tax Treatment	13

GENERAL INFORMATION

The Rayonier 1994 Incentive Stock Plan (the "Plan") was adopted by the Board of Directors of Rayonier Inc. and approved by its shareholder to be effective March 1, 1994.

The maximum number of common shares of Rayonier Inc. (the "Common Shares") for which incentive stock options may be issued under the Plan is one million (1,000,000); the maximum number of shares available for issuance under the Plan generally is determined annually as a function of a percentage of the total number of outstanding Common Shares plus unused carryover from prior years, pursuant to and subject to additional limitations set forth in, Section 3 of the Plan. The Plan does not contain any limitation on the number of shares for which options may be granted to any one employee, other than due to tax requirements relating to incentive stock options. The total number of shares available under the Plan registered currently on Form S-8 with the Securities & Exchange Commission is four million five hundred thousand (4,500,000).

In addition to non-qualified stock options and incentive stock options, the committee administering the Plan (the "Committee") may grant stock appreciation rights ("SAR's") in connection with options to those employees who are considered directors or executive officers for purposes of Section 16(b) of the Securities Exchange Act of 1934, as amended. The Plan permits the Committee to award performance shares and restricted stock, as well as non-qualified stock options, incentive stock options and SAR's. Reference is made to the text of the Plan herein for a complete description of awards permitted under the Plan and the relevant provisions and conditions applicable thereto.

The prospectus does not cover resales of Common Shares acquired pursuant to the provisions of the Plan. Resales may be subject to restrictions or limitations imposed by the Securities Act of 1933 and the Securities Exchange Act of 1934.

The Plan is not subject to any of the provisions of the Employee Retirement Income Security Act of 1974. Furthermore, Section 401 of the Internal Revenue Code relating to certain qualified pension, profit-sharing and stock bonus plans does not apply to the Plan.

Plan participants receive information with respect to their participation, including the date of grant, the exercise price, the amount exercisable and the expiration date, as well as applicable information concerning whatever performance shares or restricted stock may be relevant to them.

1994 RAYONIER INCENTIVE STOCK PLAN

1. Purpose

The purpose of the 1994 Rayonier Incentive Stock Plan is to motivate and reward superior performance on the part of employees of Rayonier and its subsidiaries and to thereby attract and retain employees of superior ability. In addition, the Plan is intended to further opportunities for stock ownership by such employees in order to increase their proprietary interest in Rayonier and, as a result, their interest in the success of the Company. Awards will be made, in the discretion of the Committee, to Key Employees (including officers and directors who are also employees) whose responsibilities and decisions directly affect the performance of any Participating Company and its subsidiaries. Such incentive awards may consist of stock options, stock appreciation rights payable in stock or cash, performance shares, restricted stock or any combination of the foregoing, as the Committee may determine.

2. Definitions

When used herein, the following terms shall have the following meanings:

“Act” means the Securities Exchange Act of 1934.

“Award” means an award granted to any Key Employee in accordance with the provisions of the Plan in the form of Options, Rights, Performance Shares or Restricted Stock, or any combination of the foregoing.

“Award Agreement” means the written agreement evidencing each Award granted to a Key Employee under the Plan.

“Beneficiary” means the beneficiary or beneficiaries designated pursuant to Section 10 to receive the amount, if any, payable under the Plan upon the death of a Key Employee.

“Board” means the Board of Directors of the Company.

“Change in Control” has the meaning specified in the Retirement Plan.

“Code” means the Internal Revenue Code of 1986, as now in effect or as hereafter amended. (All citations to sections of the Code are to such sections as they may from time to time be amended or renumbered.)

“Committee” means the Compensation and Management Development Committee of the Board or such other committee as may be designated by the Board to administer the Plan.

“Company” means Rayonier Inc. and its successors and assigns.

“Fair Market Value”, unless otherwise indicated in the provisions of this Plan, means, as of any date, the composite closing price for one share of Stock on the New York Stock Exchange or, if no sales of Stock have taken place on such date, the composite closing price on the most recent date on which selling prices were quoted, the determination to be made in the discretion of the Committee.

“Incentive Stock Option” means a stock option qualified under Section 422 of the Code.

“Key Employee” means an employee (including any officer or director who is also an employee) of any Participating Company whose responsibilities and decisions, in the judgment of the Committee, directly affect the performance of the Company and its subsidiaries.

“Limited Stock Appreciation Right” means a stock appreciation right which shall become exercisable automatically upon the occurrence of an Acceleration Event as described in Section 9 of the Plan.

“Option” means an option awarded under Section 5 of the Plan to purchase Stock of the Company, which option may be an Incentive Stock Option or a non-qualified stock option.

“Participating Company” means the Company or any subsidiary or other affiliate of the Company; provided, however, for Incentive Stock Options only, “Participating Company” means the Company or any corporation which at the time such Option is granted qualifies as a “subsidiary” of the Company under Section 425(f) of the Code.

“Performance Share” means a performance share awarded under Section 6 of the Plan.

“Plan” means the 1994 Rayonier Incentive Stock Plan, as the same may be amended, administered or interpreted from time to time.

“Plan Year” means the calendar year.

“Retirement” means eligibility to receive immediate retirement benefits under a Participating Company pension plan.

“Restricted Stock” means Stock awarded under Section 7 of the Plan subject to such restrictions as the Committee deems appropriate or desirable.

“Retirement Plan” means the Retirement Plan for Salaried Employees of Rayonier Inc., as amended effective July 18, 1997, and as the same may be thereafter amended from time to time prior to the occurrence of a Change in Control.

“Right” means a stock appreciation right awarded in connection with an option under Section 5 of the Plan.

“Stock” means the common shares of the Company.

“Total Disability” means the complete and permanent inability of a Key Employee to perform all of his or her duties under the terms of his or her employment with any Participating Company, as determined by the Committee upon the basis of such evidence, including independent medical reports and data, as the Committee deems appropriate or necessary.

“Voting Securities” means any securities of the Company that vote generally in the election of directors.

3. Shares Subject to the Plan

The aggregate number of shares of Stock which may be awarded under the Plan in any Plan Year shall be subject to an annual limit. The maximum number of shares of Stock for which Awards may be granted under the Plan in each Plan Year shall be 1.5 percent (1.5%) of the total of the issued and outstanding shares of Stock reported in the Annual Report on Form 10-K of the Company for the fiscal year ending immediately prior to any Plan Year. Any unused portion of the annual limit for any Plan Year shall be carried forward and be made available for awards in succeeding Plan Years.

No more than twenty percent (20%) of such total number of shares on a cumulative basis shall be available for restricted stock and performance shares Awards. In addition to the foregoing, in no event shall more than one million (1,000,000) shares of Stock be cumulatively available for Awards of incentive stock options under the Plan. For any Plan Year, no individual employee may receive an Award of stock options for more than ten percent (10%) of the annual limit on available shares applicable to that Plan Year.

Subject to the above limitations, shares of Stock to be issued under the Plan may be made available from the authorized but unissued shares, or from shares purchased in the open market. For the purpose of computing the total number of shares of Stock available for Awards under the Plan, there shall be counted against the foregoing limitations the number of shares of Stock which equal the value of performance share Awards, in each case determined as at the dates on which such Awards are granted. If any Awards under the Plan are forfeited, terminated, expire unexercised, are settled in cash in lieu of Stock or are exchanged for other Awards, the shares of Stock which were theretofore subject to such Awards shall again be available for Awards under the Plan to the extent of such forfeiture or expiration of such Awards. Further, any shares that are exchanged (either actually or constructively) by optionees as full or partial payment to the Company of the purchase price of shares being acquired through the exercise of a stock option granted under the Plan may be available for subsequent Awards, provided however, that such shares may be awarded only to those participants who are not directors or executive officers (as that term is defined in the rules and regulations under Section 16 of the Exchange Act).

4. Grant of Awards and Award Agreements

(a) Subject to the provisions of the Plan, the Committee shall (i) determine and designate from time to time those Key Employees or groups of Key Employees to whom Awards are to be granted; (ii) determine the form or forms of Award to be granted to any Key Employee; (iii) determine the amount or number of shares of Stock subject to each Award; and (iv) determine the terms and conditions of each Award.

(b) Each Award granted under the Plan shall be evidenced by a written Award Agreement. Such agreement shall be subject to and incorporate the express terms and conditions, if any, required under the Plan or required by the Committee.

5. Stock Options and Rights

(a) With respect to Options and Rights, the Committee shall (i) authorize the granting of Incentive Stock Options, non-qualified stock options, or a combination of Incentive Stock Options and non-qualified stock options; (ii) authorize the granting of Rights which may be granted in connection with all or part of any Option granted under this Plan, either concurrently with the grant of the option or at any time thereafter during the term of the Option; (iii) determine the number of shares of Stock subject to each Option or the number of shares of Stock that shall be used to determine the value of a Right; and (iv) determine the time or times when and the manner in which each Option or Right shall be exercisable and the duration of the exercise period.

(b) Any option issued hereunder which is intended to qualify as an Incentive Stock Option shall be subject to such limitations or requirements as may be necessary for the purposes of Section 422 of the Code or any regulations and rulings thereunder to the extent and in such form as determined by the Committee in its discretion.

(c) Rights may be granted only to Key Employees who may be considered directors or officers of the Company for purposes of Section 16 of the Act.

(d) The exercise period for a non-qualified stock option and any related Right shall not exceed ten years and two days from the date of grant, and the exercise period for an Incentive Stock Option and any related Right shall not exceed ten years from the date of grant.

(e) The Option price per share shall be determined by the Committee at the time any Option is granted and shall be not less than the Fair Market Value of one share of Stock on the date the Option is granted.

(f) No part of any Option or Right may be exercised until the Key Employee who has been granted the Award shall have remained in the employ of a Participating Company for such period after the date of grant as the Committee may specify, if any, and the Committee may further require exercisability in

installments; provided, however, the period during which a Right is exercisable shall commence no earlier than six months following the date the Option or Right is granted.

(g) The purchase price of the shares as to which an Option shall be exercised shall be paid to the Company at the time of exercise either in cash or Stock already owned by the optionee having a total Fair Market Value equal to the purchase price, or a combination of cash and Stock having a total fair market value, as so determined, equal to the purchase price. The Committee shall determine acceptable methods for tendering Stock as payment upon exercise of an Option and may impose such limitations and prohibitions on the use of Stock to exercise an Option as it deems appropriate.

(h) Unless Section 9 shall provide otherwise, Rights granted to a director or officer shall terminate when such person ceases to be considered a director or officer of the Company subject to Section 16 of the Act.

(i) In case of termination of employment, the following provisions shall apply:

(A) If a Key Employee who has been granted an Option shall die before such Option has expired, his or her Option may be exercised in full by the person or persons to whom the Key Employee's rights under the Option pass by will, or if no such person has such right, by his or her executors or administrators, at any time, or from time to time, within five years after the date of the Key Employee's death or within such other period, and subject to such terms and conditions as the Committee may specify, but not later than the expiration date specified in Section 5(d) above.

(B) If the Key Employee's employment by any Participating Company terminates because of his or her Retirement or Total Disability, he or she may exercise his or her Options in full at any time, or from time to time, within five years after the date of the termination of his or her employment or within such other period, and subject to such terms and conditions as the Committee may specify, but not later than the expiration date specified in Section 5(d) above. Any such Options not fully exercisable immediately prior to such optionee's retirement shall become fully exercisable upon such retirement unless the Committee, in its sole discretion, shall otherwise determine.

(C) Except as provided in Section 9, if the Key Employee shall voluntarily resign before eligibility for Retirement or he or she is terminated for cause as determined by the Committee, the Options or Rights shall be cancelled coincident with the effective date of the termination of employment.

(D) If the Key Employee's employment terminates for any other reason, he or she may exercise his or her Options, to the extent that he or she shall have been entitled to do so at the date of the termination of his or her employment, at any time, or from time to time, within three months after the date of the termination of his or her employment or within such other period, and subject to such terms and conditions as the Committee may specify, but not later than the expiration date specified in Section 5(d) above.

(j) No Option or Right granted under the Plan shall be transferable other than by will or by the laws of descent and distribution. During the lifetime of the optionee, an Option or Right shall be exercisable only by the Key Employee to whom the Option or Right is granted.

(k) With respect to an Incentive Stock Option, the Committee shall specify such terms and provisions as the Committee may determine to be necessary or desirable in order to qualify such Option as an "incentive stock option" within the meaning of Section 422 of the Code.

(l) With respect to the exercisability and settlement of Rights:

(i) Upon exercise of a Right, the Key Employee shall be entitled, subject to such terms and conditions the Committee may specify, to receive upon exercise thereof all or a

portion of the excess of (A) the Fair Market Value of a specified number of shares of Stock at the time of exercise, as determined by the Committee, over (B) a specified amount which shall not, subject to Section 5(e), be less than the Fair Market Value of such specified number of shares of Stock at the time the Right is granted. Upon exercise of a Right, payment of such excess shall be made as the Committee shall specify in cash, the issuance or transfer to the Key Employee of whole shares of Stock with a Fair Market Value at such time equal to any excess, or a combination of cash and shares of Stock with a combined Fair Market Value at such time equal to any such excess, all as determined by the Committee. The Company will not issue a fractional share of Stock and, if a fractional share would otherwise be issuable, the Company shall pay cash equal to the Fair Market Value of the fractional share of Stock at such time.

(ii) For the purposes of Subsection (i) of this Section 5(l), in the case of any such Right or portion thereof, other than a Right related to an Incentive Stock Option, exercised for cash during a "window period" specified by Rule 16b-3 under the Act, the Fair Market Value of the Stock at the time of such exercise shall be the highest composite daily closing price of the Stock during such window period.

(iii) In the event of the exercise of such Right, the Company's obligation in respect of any related Option or such portion thereof will be discharged by payment of the Right so exercised.

6. Performance Shares

(a) Subject to the provisions of the Plan, the Committee shall (i) determine and designate from time to time those Key Employees or groups of Key Employees to whom Awards of Performance Shares are to be made, (ii) determine the Performance Period (the "Performance Period") and Performance Objectives (the "Performance Objectives") applicable to such Awards, (iii) determine the form of settlement of a Performance Share and (iv) generally determine the terms and conditions of each such Award. At any date, each Performance Share shall have a value equal to the Fair Market Value of a share of Stock at such date; provided that the Committee may limit the aggregate amount payable upon the settlement of any Award.

(b) The Committee shall determine a Performance Period of not less than two nor more than five years. Performance Periods may overlap and Key Employees may participate simultaneously with respect to Performance Shares for which different Performance Periods are prescribed.

(c) The Committee shall determine the Performance Objectives of Awards of Performance Shares. Performance Objectives may vary from Key Employee to Key Employee and between groups of Key Employees and shall be based upon such performance criteria or combination of factor as the Committee may deem appropriate, including, but not limited to, minimum earnings per share or return on equity. If during the course of a Performance Period there shall occur significant events which the Committee expects to have a substantial effect on the applicable Performance Objectives during such period, the Committee may revise such Performance Objectives.

(d) At the beginning of a Performance Period, the Committee shall determine for each Key Employee or group of Key Employees the number of Performance Shares or the percentage of Performance Shares which shall be paid to the Key Employee or member of the group of Key Employees if Performance Objectives are met in whole or in part.

(e) If a Key Employee terminates service with all Participating Companies during a Performance Period because of death, Total Disability, Retirement, or under other circumstances where the Committee in its sole discretion finds that a waiver would be in the best interests of the Company, that Key Employee may, as determined by the Committee, be entitled to an Award of Performance Shares at the end of the Performance Period based upon the extent to which the Performance Objectives were satisfied at the end of

such period, which Award, in the discretion of the Committee, may be maintained without change or reduced and prorated for the portion of the Performance Period during which the Key Employee was employed by any Participating Company; provided, however, the Committee may provide for an earlier payment in settlement of such Performance Shares in such amount and under such terms and conditions as the Committee deems appropriate or desirable. If a Key Employee terminates service with all Participating Companies during a Performance Period for any other reason, then such Key Employee shall not be entitled to any Award with respect to that Performance Period unless the Committee shall otherwise determine.

(f) Each Award of a Performance Share shall be paid in whole shares of Stock, or cash, or a combination of Stock and cash either as a lump sum payment or in annual installments, all as the Committee shall determine, with payment to commence as soon as practicable after the end of the relevant Performance Period.

7. Restricted Stock

(a) Restricted Stock shall be subject to a restriction period (after which restrictions will lapse) which shall mean a period commencing on the date the Award is granted and ending on such date as the Committee shall determine (the "Restriction Period"). The Committee may provide for the lapse of restrictions in installments where deemed appropriate.

(b) Except when the Committee determines otherwise pursuant to Section 7(d), if a Key Employee terminates employment with all Participating Companies for any reason before the expiration of the Restriction Period, all shares of Restricted Stock still subject to restriction shall be forfeited by the Key Employee and shall be reacquired by the Company.

(c) Except as otherwise provided in this Section 7, no shares of Restricted Stock received by a Key Employee shall be sold, exchanged, transferred, pledged, hypothecated or otherwise disposed of during the Restriction Period.

(d) In cases of death, Total Disability or Retirement or in cases of special circumstances, the Committee may, in its sole discretion when it finds that a waiver would be in the best interests of the Company, elect to waive any or all remaining restrictions with respect to such Key Employee's Restricted Stock.

(e) The Committee may require, under such terms and conditions as it deems appropriate or desirable, that the certificates for Stock delivered under the Plan may be held in custody by a bank or other institution, or that the Company may itself hold such shares in custody until the Restriction Period expires or until restrictions thereon otherwise lapse, and may require, as a condition of any Award of Restricted Stock that the Key Employee shall have delivered a stock power endorsed in blank relating to the Restricted Stock.

(f) Nothing in this Section 7 shall preclude a Key Employee from exchanging any shares of Restricted Stock subject to the restrictions contained herein for any other shares of Stock that are similarly restricted.

(g) Subject to Section 7(e) and Section 8, each Key Employee entitled to receive Restricted Stock under the Plan shall be issued a certificate for the shares of Stock. Such certificate shall be registered in the name of the Key Employee, and shall bear an appropriate legend reciting the terms, conditions and restrictions, if any, applicable to such Award and shall be subject to appropriate stop-transfer orders.

8. Certificates for Awards of Stock

(a) The Company shall not be required to issue or deliver any certificates for shares of Stock prior to (i) the listing of such shares on any stock exchange on which the Stock may then be listed and (ii) the completion of any registration or qualification of such shares under any federal or state law, or any ruling or regulation of any government body which the Company shall, in its sole discretion, determine to be necessary or advisable.

(b) All certificates for shares of Stock delivered under the Plan shall also be subject to such stop-transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations, and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Stock is then listed and any applicable federal or state securities laws, and the Committee may cause a legend or legends to be placed on any such certificates to make appropriate reference to such restrictions. The foregoing provisions of this Section 8(b) shall not be effective if and to the extent that the shares of Stock delivered under the Plan are covered by an effective and current registration statement under the Securities Act of 1933, or if and so long as the Committee determines that application of such provisions is no longer required or desirable. In making such determination, the Committee may rely upon an opinion of counsel for the Company.

(c) Except for the restrictions on Restricted Stock under Section 7, each Key Employee who receives Stock in settlement of an Award of Stock, shall have all of the rights of a shareholder with respect to such shares, including the right to vote the shares and receive dividends and other distributions. No Key Employee awarded an Option, a Right or Performance Share shall have any right as a shareholder with respect to any shares covered by his or her Option, Right or Performance Share prior to the date of issuance to him or her of a certificate or certificates for such shares.

9. Change in Control

Notwithstanding any provisions in this Plan to the contrary:

(a) Each outstanding Option granted under the Plan shall become immediately exercisable in full for the aggregate number of shares covered thereby and all related Rights shall also become exercisable upon the occurrence of a Change in Control and shall continue to be exercisable in full for cash for a period of 60 calendar days beginning on the date that such Change in Control occurs and ending on the 60th calendar day following that date; provided, however, that (A) no Right shall become exercisable earlier than six months following the date the Right is granted, and (B) no Option or Right shall be exercisable beyond the expiration date of its original term.

(b) Options and Rights shall not terminate and shall continue to be fully exercisable for a period of seven months following the occurrence of a Change in Control in the case of an employee who is terminated other than for just cause or who voluntarily terminates his or her employment because he or she in good faith believes that as a result of such Change in Control he or she is unable effectively to discharge his or her present duties or the duties of the position he or she occupied just prior to the occurrence of such Change in Control. For purposes of Section 9 only, termination shall be for "just cause" only if such termination is based on fraud, misappropriation or embezzlement on the part of the employee which results in a final conviction of a felony. Under no circumstances, however, shall any Option or Right be exercised beyond the expiration date of its original term.

(c) Any Right or portion thereof may be exercised for cash within the 60-calendar-day period following the occurrence of a Change in Control with settlement, except in the case of a Right related to an Incentive Stock Option, based on the "Formula Price" which shall be the highest of (A) the highest composite daily closing price of the Stock during the period beginning on the 60th calendar day prior to the date on which the Right is exercised and ending on the date such Right is exercised, (B) the highest gross price paid for the Stock during the same period of time, as reported in a report on Schedule 13D filed with the Securities and Exchange Commission or (C) the highest gross price paid or to be paid for a share of Stock (whether by way of exchange, conversion, distribution upon merger, liquidation or otherwise) in any of the transactions set forth in the definition of "Change in Control" in the Retirement Plan.

(d) Upon the occurrence of a Change in Control, Limited Stock Appreciation Rights shall automatically be granted as to any Option with respect to which Rights are not then outstanding;

provided, however, that Limited Stock Appreciation Rights shall be provided at the time of grant of any Incentive Stock Option subject to exercisability upon the occurrence of a Change in Control. Limited Stock Appreciation Rights shall entitle the holder thereof, upon exercise of such rights and surrender of the related Option or any portion thereof, to receive, without payment to the Company (except for applicable withholding taxes), an amount in cash equal to the excess, if any, of the Formula Price as that term is defined in Section 9 over the option price of the Stock as provided in such Option; provided that in the case of the exercise of any such Limited Stock Appreciation Right or portion thereof related to an Incentive Stock Option, the Fair Market Value of the Stock at the time of such exercise shall be substituted for the Formula Price. Each such Limited Stock Appreciation Right shall be exercisable only during the period beginning on the first business day following the occurrence of such Change in Control and ending on the 60th calendar day following such date and only to the same extent the related Option is exercisable. Upon exercise of a Limited Stock Appreciation Right and surrender of the related Option, or portion thereof, such Option, to the extent surrendered, shall not thereafter be exercisable.

(e) The restrictions applicable to Awards of Restricted Stock issued pursuant to Section 7 shall lapse upon the occurrence of a Change in Control and the Company shall issue stock certificates without a restrictive legend. Key Employees holding Restricted Stock on the date of a Change in Control may tender such Restricted Stock to the Company which shall pay the Formula Price as that term is defined in Section 9; provided, such Restricted Stock must be tendered to the Company within 60 calendar days of the Change in Control.

(f) If a Change in Control occurs during the course of a Performance Period applicable to an Award of Performance Shares pursuant to Section 6, then the Key Employee shall be deemed to have satisfied the Performance Objectives and settlement of such Performance Shares shall be based on the Formula Price, as defined in this Section 9.

10. Beneficiary

(a) Each Key Employee shall file with the Company a written designation of one or more persons as the Beneficiary who shall be entitled to receive the Award, if any, payable under the Plan upon his or her death. A Key Employee may from time-to-time revoke or change his or her Beneficiary designation without the consent of any prior Beneficiary by filing a new designation with the Company. The last such designation received by the Company shall be controlling; provided, however, that no designation, or change or revocation thereof, shall be effective unless received by the Company prior to the Key Employee's death, and in no event shall it be effective as of a date prior to such receipt.

(b) If no such Beneficiary designation is in effect at the time of a Key Employee's death, or if no designated Beneficiary survives the Key Employee or if such designation conflicts with law, the Key Employee's estate shall be entitled to receive the Award, if any, payable under the Plan upon his or her death. If the Committee is in doubt as to the right of any person to receive such Award, the Company may retain such Award, without liability for any interest thereon, until the Committee determines the rights thereto, or the Company may pay such Award into any court of appropriate jurisdiction and such payment shall be a complete discharge of the liability of the Company therefor.

11. Administration of the Plan

(a) Each member of the Committee shall be both a member of the Board and a "non-employee director" within the meaning of Rule 16b-3(b)(3)(i) under the Act or successor rule or regulation. No member of the Committee shall be, or shall have been, eligible to receive an Award under the Plan or any other plan maintained by any Participating Company to acquire stock, stock options, stock appreciation rights, performance shares or restricted stock of a Participating Company at any time within the one year immediately preceding the member's appointment to the Committee.

(b) All decisions, determinations or actions of the Committee made or taken pursuant to grants of authority under the Plan shall be made or taken in the sole discretion of the Committee and shall be final, conclusive and binding on all persons for all purposes.

(c) The Committee shall have full power, discretion and authority to interpret, construe and administer the Plan and any part thereof, and its interpretations and constructions thereof and actions taken thereunder shall be, except as otherwise determined by the Board, final, conclusive and binding on all persons for all purposes.

(d) The Committee's decisions and determinations under the Plan need not be uniform and may be made selectively among Key Employees, whether or not such Key Employees are similarly situated.

(e) The Committee may, in its sole discretion, delegate such of its powers as it deems appropriate.

(f) If a Change in Control has not occurred and if the Committee determines that a Key Employee has taken action inimical to the best interests of any Participating Company, the Committee may, in its sole discretion, terminate in whole or in part such portion of any Option (including any related Right) as has not yet become exercisable at the time of termination, terminate any Performance Share Award for which the Performance Period has not been completed or terminate any Award of Restricted Stock for which the Restriction Period has not lapsed.

12. Amendment, Extension or Termination

The Board may, at any time, amend or terminate the Plan and, specifically, may make such modifications to the Plan as it deems necessary to avoid the application of Section 162(m) of the Code and the Treasury regulations issued thereunder. However, no amendment shall, without approval by a majority of the Company's stockholders, (a) alter the group of persons eligible to participate in the Plan, (b) except as provided in Section 13 increase the maximum number of shares of Stock which are available for Awards under the Plan or (c) extend the period during which awards may be granted beyond December 31, 2003. If a Change in Control has occurred, no amendment or termination shall impair the rights of any person with respect to a prior Award.

13. Adjustments in Event of Change in Common Stock

In the event of any recapitalization, reclassification, split-up or consolidation of shares of Stock or, stock dividend, merger or consolidation of the Company or sale by the Company of all or a portion of its assets, the Committee shall make such adjustments in the Stock subject to Awards, including Stock subject to purchase by an Option, or the terms, conditions or restrictions on Stock or Awards, including the price payable upon the exercise of such Option, as the Committee deems equitable; provided however, that in the event of a stock split, stock dividend or consolidation of shares, the number of shares subject to an outstanding Option and the exercise price thereof, and the number of outstanding Performance Shares, shall be proportionately adjusted to reflect such action. The number of shares available for Awards shall be automatically increased to reflect any additional shares issuable pursuant to the last clause of the preceding sentence. With respect to Awards intended to qualify as "performance-based compensation" under Section 162(m) of the Code, such adjustments shall be made only to the extent that the Committee determines that such adjustments may be made without a loss of deductibility of such Awards under Section 162(m) of the Code.

14. Miscellaneous

(a) Except as provided in Section 9, nothing in this Plan or any Award granted hereunder shall confer upon any employee any right to continue in the employ of any Participating Company or interfere in any way with the right of any Participating Company to terminate his or her employment at any time. No Award payable under the Plan shall be deemed salary or compensation for the purpose of computing benefits under any employee benefit plan or other arrangement of any Participating Company for the benefit of its employees

unless the Company shall determine otherwise. No Key Employee shall have any claim to an Award until it is actually granted under the Plan. To the extent that any person acquires a right to receive payments from the Company under this Plan, such right shall be no greater than the right of an unsecured general creditor of the Company. All payments to be made hereunder shall be paid from the general funds of the Company and no special or separate fund shall be established and no segregation of assets shall be made to assure payment of such amounts except as provided in Section 7(e) with respect to Restricted Stock.

(b) The Committee may cause to be made, as a condition precedent to the payment of any Award, or otherwise, appropriate arrangements with the Key Employee or his or her Beneficiary, for the withholding of any federal, state, local or foreign taxes.

(c) The Plan and the grant of Awards shall be subject to all applicable federal and state laws, rules, and regulations and to such approvals by any government or regulatory agency as may be required.

(d) The terms of the Plan shall be binding upon the Company and its successors and assigns.

(e) Captions preceding the sections hereof are inserted solely as a matter of convenience and in no way define or limit the scope or intent of any provision hereof.

15. Effective Date, Term of Plan and Shareholder Approval

The effective date of the Plan was March 1, 1994 and was approved by the Company's shareholders within twelve months before such date. The Plan was amended and restated effective October 16, 1998. No Award shall be granted under this Plan after the Plan's termination date. The Plan's termination date shall be December 31, 2003. The Plan will continue in effect for existing Awards as long as any such Award is outstanding.

ADMINISTRATION

The Plan is administered by a Committee of the Board of Directors of Rayonier, presently designated as the Compensation and Management Development Committee, the members of which serve during the pleasure of the Board. The Committee is composed of directors none of whom is an officer or employee of Rayonier and none of whom is eligible to receive any award under the Plan.

FEDERAL INCOME TAX TREATMENT

The following is a brief summary of the current Federal income tax rules generally applicable to options, stock appreciation rights, performance shares and restricted stock. Recipients of Awards and Substitute Stock Options should consult their own tax advisors as to the specific Federal, state and local tax consequences applicable to them.

A. Options and Stock Appreciation Rights

Options granted under the Plan may be either non-qualified options or "incentive stock options" qualifying under Section 422 of the Internal Revenue Code. The Substitute Stock Options are non-qualified options.

Non-qualified Options

An optionee is not subject to Federal income tax upon grant of a non-qualified option. At the time of exercise, the optionee will realize compensation income (subject to withholding) to the extent that the then fair market value of the stock exceeds the option price. The amount of such income will constitute an addition to the optionee's tax basis in the optioned stock. Sale of the shares will result in capital gain or loss (long-term or short-term depending on the optionee's holding period). Rayonier is entitled to a Federal tax deduction at the same time and to the same extent that the optionee realizes compensation income.

Incentive Stock Options ("ISOs")

Options under the Plan denominated as ISOs are intended to constitute incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended. An optionee is not subject to Federal income tax upon either the grant or exercise of an ISO. If the optionee holds the shares acquired upon exercise for at least one year after issuance of the optioned shares and until at least two years after grant of the option, then the difference between the amount realized on a subsequent sale or other taxable disposition of the shares and the option price will constitute long-term capital gain or loss. To obtain favorable tax treatment, an ISO must be exercised within three months after termination of employment (other than by retirement, disability, or death) with Rayonier or subsidiary. To obtain favorable tax treatment, an ISO must be exercised within three months of retirement or within one year of cessation of employment for disability (with no limitation in the case of death), notwithstanding any longer exercise period permitted under the terms of the Plan. Rayonier will not be entitled to a Federal tax deduction with respect to the grant or exercise of the ISO.

If the optionee disposes of the shares acquired under an ISO before the requisite holding period, he or she will be deemed to have made a "disqualifying disposition" of the shares and will realize compensation income in the year of disposition equal to the lesser of the fair market value of the shares at exercise or the amount realized on their disposition over the option price of the shares. (However, if the disposition is by gift or by sale to a related party, the compensation income must be measured by the value of the shares at exercise over the option price.) Any gain recognized upon a disqualifying disposition in excess of the ordinary income portion will constitute either short-term or long-term capital gain. In the event of a disqualifying disposition, Rayonier will be entitled to a Federal tax deduction in the amount of the compensation income realized by the optionee.

The option spread on the exercise of an ISO is an adjustment in computing alternative minimum taxable income. No adjustment is required, however, if the optionee made a disqualifying disposition of the shares in the same year as he or she is taxed on the exercise.

Stock Appreciation Rights ("SARs")

SARs may be awarded to officers and directors of Rayonier subject to Section 16(b) of the Securities Exchange Act of 1934 with respect to both incentive stock options and non-qualified options granted under the Plan. An optionee is not taxed upon the grant of SARs. An optionee exercising SARs for cash will realize compensation income (subject to withholding) in the amount of the cash received. Rayonier is entitled to a tax deduction at the same time and to the same extent that the optionee realizes compensation income.

B. Performance Shares

A recipient of performance shares generally will realize compensation income (subject to withholding) when and to the extent that payment is made, whether in the form of cash or shares of Rayonier Common Shares. To the extent that payment is made in the form of stock, income shall be measured by the then fair market value of the shares, which shall constitute an addition to the recipient's tax basis in such shares. Rayonier will be entitled to a Federal tax deduction for the value of payment at the time of payment.

C. Restricted Stock

A recipient of restricted stock generally will realize compensation income (subject to withholding) when and to the extent that the restrictions on the shares lapse, as measured by the value of the shares at the time of lapse. The recipient's holding period for the shares will not commence until the date of lapse, and dividends paid during the restriction period will be treated as compensation. The income realized on lapse of the restrictions will constitute an addition to the recipient's tax basis in the shares.

In lieu of deferred recognition of income, the recipient may file an election with the Internal Revenue Service, within 30 days of award, to realize compensation income at the time of award, as measured by the fair market value of the stock on the date of award determined without regard to the restrictions. The income realized will constitute an addition to the tax basis of the shares. In the case of such election, any appreciation (or depreciation) on the shares during the restriction period will give rise to capital gain (or capital loss). In the event that the recipient terminates employment during the restriction period and forfeits his or her shares, no deduction may be claimed and the taxes paid on award of the shares shall be forfeited.

Rayonier will be entitled to a Federal tax deduction at the same time and to the same extent that the recipient realizes compensation income.

RAYONIER INC.

4,500,000 Common Shares

**2004 RAYONIER INCENTIVE STOCK
AND
MANAGEMENT BONUS PLAN**

PLAN INFORMATION

**THIS DOCUMENT CONSTITUTES PART OF A PROSPECTUS COVERING SECURITIES
THAT HAVE BEEN REGISTERED UNDER THE
SECURITIES ACT OF 1933.**

The Prospectus covers such additional securities as may be issuable as a result of anti-dilution provisions contained in the instruments pursuant to which securities covered by the Prospectus are issued.

**THESE SECURITIES HAVE NOT BEEN APPROVED OR DISAPPROVED BY THE SECURITIES
AND EXCHANGE COMMISSION OR ANY STATE SECURITIES COMMISSION NOR HAS
THE SECURITIES AND EXCHANGE COMMISSION OR ANY STATE SECURITIES
COMMISSION PASSED UPON THE ACCURACY OR ADEQUACY OF THE
PROSPECTUS. ANY REPRESENTATION TO THE CONTRARY IS A
CRIMINAL OFFENSE.**

As amended July 21, 2006

Additional information about the Plan and its administration may be obtained by writing the Manager of Stock Option Plan Administration, Rayonier Inc., 50 No. Laura Street, Jacksonville, FL 32202, or telephoning the Manager at (904) 357-9100.

Any statement contained in a document incorporated or deemed to be incorporated by reference in the Prospectus shall be deemed to be modified or superseded for purposes of the Prospectus to the extent that a statement contained in the Prospectus or in any other subsequently filed document which also is or is deemed to be incorporated by reference in the Prospectus modifies or supersedes such statement. Any such statement so modified or superseded shall not be deemed, except as so modified or superseded, to constitute a part of the Prospectus. Any such document, as well as Rayonier's most recent annual report to shareholders and any other report or communication distributed to Rayonier shareholders generally, may be obtained without charge by written request to W. Edwin Frazier, III, Senior Vice President, Administration and Corporate Secretary, Rayonier Inc., 50 No. Laura Street, Jacksonville, FL 32202, or by telephoning W. Edwin Frazier, III at (904) 357-9100.

TABLE OF CONTENTS

General Information	3
The Plan	4
Administration	15
Federal Tax Treatment	17

GENERAL INFORMATION

The 2004 Rayonier Incentive Stock and Management Bonus Plan (the "Plan") was adopted by the Board of Directors of Rayonier Inc. and approved by its shareholder to be effective January 1, 2004.

The maximum number of common shares of Rayonier Inc. (the "Common Shares") for which incentive stock options may be issued under the Plan is one million (1,000,000). The total number of shares available under the Plan registered currently on Form S-8 with the Securities & Exchange Commission is four million five hundred thousand (4,500,000).

In addition to non-qualified stock options and incentive stock options, the committee administering the Plan (the "Committee") may grant stock appreciation rights ("SAR's") in connection with options to those employees who are considered directors or executive officers for purposes of Section 16(b) of the Securities Exchange Act of 1934, as amended. The Plan permits the Committee to award performance shares and restricted stock, as well as non-qualified stock options, incentive stock options, SAR's, Restricted Stock units and senior management bonus awards in stock or in cash. Reference is made to the text of the Plan herein for a complete description of awards permitted under the Plan and the relevant provisions and conditions applicable thereto.

The prospectus does not cover resales of Common Shares acquired pursuant to the provisions of the Plan. Resales may be subject to restrictions or limitations imposed by the Securities Act of 1933 and the Securities Exchange Act of 1934.

The Plan is not subject to any of the provisions of the Employee Retirement Income Security Act of 1974. Furthermore, Section 401 of the Internal Revenue Code relating to certain qualified pension, profit-sharing and stock bonus plans does not apply to the Plan.

Plan participants receive information with respect to their participation, including the date of grant, the exercise price, the amount exercisable and the expiration date, applicable information concerning performance shares or restricted stock and bonus awards that may be relevant to them.

The Plan contains a 1.16 million share limitation on the number of shares which may be issued as restricted or performance share awards, as well as an annual limitation on the number of shares which one employee may be awarded annually.

1. Purpose

The purpose of the 2004 Rayonier Incentive Stock and Management Bonus Plan is to motivate and reward superior performance on the part of employees of Rayonier and its subsidiaries and to thereby attract and retain employees of superior ability. In addition, the Plan is intended to further opportunities for stock ownership by such employees in order to increase their proprietary interest in Rayonier and, as a result, their interest in the success of the Company. Awards will be made, in the discretion of the Committee, to Key Employees (including officers and directors who are also employees) whose responsibilities and decisions directly affect the performance of any Participating Company and its subsidiaries. Such incentive awards may consist of stock options, stock appreciation rights payable in stock or cash, performance shares, restricted stock, performance bonus awards or any combination of the foregoing, as the Committee may determine.

2. Definitions

When used herein, the following terms shall have the following meanings:

“Act” means the Securities Exchange Act of 1934.

“Award” means an award granted to any Key Employee in accordance with the provisions of the Plan in the form of Options, Rights, Performance Shares, Restricted Stock or Performance Bonus Awards, or any combination of the foregoing.

“Award Agreement” means the written agreement evidencing each Award, other than Performance Bonus Awards, granted to a Key Employee under the Plan.

“Beneficiary” means the estate of a Key Employee or such other beneficiary or beneficiaries lawfully designated pursuant to Section 11 to receive the amount, if any, payable under the Plan upon the death of a Key Employee.

“Board” means the Board of Directors of the Company.

“Change in Control” has the meaning specified in the Retirement Plan.

“Code” means the Internal Revenue Code of 1986, as now in effect or as hereafter amended. (All citations to sections of the Code are to such sections as they may from time to time be amended or renumbered.)

“Committee” means the Compensation and Management Development Committee of the Board or such other committee as may be designated by the Board to administer the Plan.

“Company” means Rayonier Inc. and its successors and assigns.

“Fair Market Value”, unless otherwise indicated in the provisions of this Plan, means, as of any date, the composite closing price for one share of Stock on the New York Stock Exchange for the most recently completed trading day or, if no sales of Stock have taken place on such date, the composite closing price on the most recent date on which selling prices were quoted, the determination to be made in the discretion of the Committee.

“GAAP” means U.S. Generally Accepted Accounting Principles.

“Incentive Stock Option” means a stock option qualified under Section 422 of the Code.

“Key Employee” means an employee (including any officer or director who is also an employee) of any Participating Company whose responsibilities and decisions, in the judgment of the Committee, directly affect the performance of the Company and its subsidiaries.

“Limited Stock Appreciation Right” means a stock appreciation right that shall become exercisable automatically upon the occurrence of a Change in Control as described in Section 10 of the Plan.

“Option” means an option awarded under Section 5 of the Plan to purchase Stock of the Company, which option may be an Incentive Stock Option or a non-qualified stock option.

“Participating Company” means the Company or any subsidiary or other affiliate of the Company; provided, however, for Incentive Stock Options only, “Participating Company” means the Company or any corporation that at the time such Option is granted qualifies as a “subsidiary” of the Company under Section 425(f) of the Code.

“Participant” means each Key Employee of the Participating Company selected by the Committee as eligible for a Performance Bonus Award who could potentially be described in Section 162(m)(3) of the Code, as well as, in the discretion of the Committee, the President and Chief Executive Officer and any Key Employee reporting directly to the President and Chief Executive Officer.

“Performance Bonus Award” means the right of a Participant to receive cash following the completion of a Performance Period based upon performance in respect of one or more of the Performance Goals during such Performance Period, as specified in Section 9.

“Performance Goals” means or may be expressed in terms of any, but not limited to, of the following business criteria: (i) net income, (ii) earnings per share, (iii) operating income, (iv) operating cash flow, (v) earnings before income taxes and depreciation, (vi) earnings before interest, taxes, depreciation and amortization, (vii) operating margins (viii) reductions in operating expenses, (ix) sales or return on sales (x) total stockholder return (xi) return on equity, (xii) return on total capital, (xiii) return on invested capital, (xiv) return on assets, (xv) economic value added, (xvi) cost reductions and savings, (xvii) increase in surplus, (xviii) productivity improvements, (xix) an executive’s attainment of personal objectives with respect to any of the foregoing criteria or other criteria such as growth and profitability, customer satisfaction, leadership effectiveness, business development, negotiating transactions and sales or developing long term business goals. A Performance Goal may be measured over a Performance Period on a periodic, annual, cumulative or average basis and may be established on a corporate-wide basis or established with respect to one or more operating units, divisions, subsidiaries, acquired businesses, minority investments, partnerships or joint ventures. Unless otherwise determined by the Committee, the Performance Goals will be determined using GAAP consistently applied during a Performance Period by no later than the earlier of the date that is ninety days after the commencement of the Performance Period or the day prior to the date on which twenty-five percent of the Performance Period has elapsed.

“Performance Objective” means the level or levels of performance required to be attained with respect to specified Performance Goals in order that a Key Employee shall become entitled to specified rights in connection with a Performance Share or Performance Bonus Award.

“Performance Period” means the calendar year, or such other shorter or longer period designated by the Committee, during which performance will be measured in order to determine a Key Employee’s entitlement to receive payment of a Performance Share or Performance Bonus Award, respectively.

“Performance Share” means a performance share awarded under Section 6 of the Plan.

“Plan” means the 2004 Rayonier Incentive Stock and Management Bonus Plan, as the same may be amended, administered or interpreted from time to time.

“Plan Year” means the calendar year.

“Retirement” means eligibility to receive immediate retirement benefits under a Participating Company pension plan.

“Restricted Stock” means Stock awarded under Section 7 of the Plan subject to such restrictions as the Committee deems appropriate or desirable.

“Restricted Stock Unit” has the meaning set forth in Section 6 of the Plan.

“Retirement Plan” means the Retirement Plan for Salaried Employees of Rayonier Inc., as amended effective July 18, 1997, and as the same may be thereafter amended from time to time prior to the occurrence of a Change in Control.

“Right” means a stock appreciation right awarded in connection with an option under Section 5 of the Plan.

“Share Limit” has the meaning set forth in Section 3.

“Stock” means the common shares of the Company.

“Total Disability” means the complete and permanent inability of a Key Employee to perform all of his or her duties under the terms of his or her employment with any Participating Company, as determined by the Committee upon the basis of such evidence, including independent medical reports and data, as the Committee deems appropriate or necessary.

“Voting Securities” means any securities of the Company that vote generally in the election of directors.

3. Shares Subject to the Plan

The aggregate number of shares of Stock that may be awarded under the Plan is 4.5 million.

No more than 1.16 million of such total number of shares shall be available for restricted stock and Performance Share Awards. In addition to the foregoing, in no event shall more than one million (1,000,000) shares of Stock be cumulatively available for Awards of incentive stock options under the Plan. For any Plan Year, no individual employee may receive an Award of Options, Performance Shares, Restricted Stock or Rights for more than four percent (4%) of the total number of shares authorized under the Plan (with respect to any Key Employee, his or her “Share Limit”). The number of shares available in each category hereunder shall be subject to adjustment as provided in Section 14 in connection with a Stock split, Stock dividend, or other extraordinary transaction affecting the Stock.

Subject to the above limitations, shares of Stock to be issued under the Plan may be made available from the authorized but unissued shares, or from shares purchased in the open market. For the purpose of computing the total number of shares of Stock available for Awards under the Plan, there shall be counted against the foregoing limitations the number of shares of Stock that equal the maximum number of Performance Share Awards issuable in any outstanding grant, in each case determined as at the dates on which such Awards are granted. If any Awards under the Plan are forfeited, terminated, expire unexercised, are settled in cash in lieu of Stock or are exchanged for other Awards, the shares of Stock that were theretofore subject to such Awards shall again be available for Awards under the Plan to the extent of such

forfeiture or expiration of such Awards. Further, any shares that are exchanged (either actually or constructively) by optionees as full or partial payment to the Company of the purchase price of shares being acquired through the exercise of a stock option granted under the Plan may be available for subsequent Awards.

4. Grant of Awards and Award Agreements

(a) Subject to the provisions of the Plan, the Committee shall (i) determine and designate from time to time those Key Employees or groups of Key Employees to whom Awards are to be granted; (ii) determine the form or forms of Award to be granted to any Key Employee; (iii) determine the amount or number of shares of Stock subject to each Award; and (iv) determine the terms and conditions of each Award.

(b) Each Award, other than Performance Bonus Awards, granted under the Plan shall be evidenced by a written Award Agreement. Such agreement shall be subject to and incorporate the express terms and conditions, if any, required under the Plan or required by the Committee.

5. Stock Options and Rights

(a) With respect to Options and Rights, the Committee shall (i) authorize the granting of Incentive Stock Options, non-qualified stock options, or a combination of Incentive Stock Options and non-qualified stock options; (ii) authorize the granting of Rights that may be granted in connection with all or part of any Option granted under this Plan, either concurrently with the grant of the Option or at any time thereafter during the term of the Option; (iii) determine the number of shares of Stock subject to each Option or the number of shares of Stock that shall be used to determine the value of a Right; and (iv) determine the time or times when and the manner in which each Option or Right shall be exercisable and the duration of the exercise period.

(b) Any Option issued hereunder that is intended to qualify as an Incentive Stock Option shall be subject to such limitations or requirements as may be necessary for the purposes of Section 422 of the Code or any regulations and rulings thereunder to the extent and in such form as determined by the Committee in its discretion.

(c) Rights may be granted only to Key Employees who may be considered directors or officers of the Company for purposes of Section 16 of the Act.

(d) The exercise period for a non-qualified stock option and any related Right shall not exceed ten years from the date of grant, and the exercise period for an Incentive Stock Option and any related Right shall not exceed ten years from the date of grant.

(e) The Option price per share shall be determined by the Committee at the time any Option is granted and shall be not less than the Fair Market Value of one share of Stock on the date the Option is granted.

(f) No part of any Option or Right may be exercised until the Key Employee who has been granted the Award shall have remained in the employ of a Participating Company for such period after the date of grant as the Committee may specify, if any, and the Committee may further require exercisability in installments; provided, however, the period during which a Right is exercisable shall commence no earlier than six months following the date the Option or Right is granted.

(g) The purchase price of the shares as to which an Option shall be exercised shall be paid to the Company at the time of exercise either in cash or Stock already owned by the optionee having a total Fair Market Value equal to the purchase price, or a combination of cash and Stock having a total fair market value, as so determined, equal to the purchase price. The Committee shall determine acceptable methods for tendering Stock as payment upon exercise of an Option and may impose such limitations and prohibitions on the use of Stock to exercise an Option as it deems appropriate.

(h) Unless Section 10 shall provide otherwise, Rights granted to a director or officer shall terminate when such person ceases to be considered a director or officer of the Company subject to Section 16 of the Act.

(i) In case of termination of employment, the following provisions shall apply:

(A) If a Key Employee who has been granted an Option shall die before such Option has expired, his or her Option may be exercised in full by the person or persons to whom the Key Employee's rights under the Option pass by will, or if no such person has such right, by his or her executors or administrators, at any time, or from time to time, within five years after the date of the Key Employee's death or within such other period, and subject to such terms and conditions as the Committee may specify, but not later than the expiration date specified in Section 5(d) above.

(B) If the Key Employee's employment by any Participating Company terminates because of his or her Retirement or Total Disability, he or she may exercise his or her Options in full at any time, or from time to time, within five years after the date of the termination of his or her employment or within such other period, and subject to such terms and conditions as the Committee may specify, but not later than the expiration date specified in Section 5(d) above. Any such Options not fully exercisable immediately prior to such optionee's Retirement shall become fully exercisable upon such Retirement unless the Committee, in its sole discretion, shall otherwise determine.

(C) Except as provided in Section 10, if the Key Employee shall voluntarily resign before eligibility for Retirement or he or she is terminated for cause as determined by the Committee, the Options shall be cancelled coincident with the effective date of the termination of employment.

(D) If the Key Employee's employment terminates for any other reason, he or she may exercise his or her Options, to the extent that he or she shall have been entitled to do so at the date of the termination of his or her employment, at any time, or from time to time, within three months after the date of the termination of his or her employment or within such other period, and subject to such terms and conditions as the Committee may specify, but not later than the expiration date specified in Section 5(d) above.

(j) No Option or Right granted under the Plan shall be transferable other than by will or by the laws of descent and distribution. During the lifetime of the optionee, an Option or Right shall be exercisable only by the Key Employee to whom the Option or Right is granted.

(k) With respect to an Incentive Stock Option, the Committee shall specify such terms and provisions as the Committee may determine to be necessary or desirable in order to qualify such Option as an "incentive stock option" within the meaning of Section 422 of the Code.

(l) With respect to the exercisability and settlement of Rights:

(i) Upon exercise of a Right, the Key Employee shall be entitled, subject to such terms and conditions as the Committee may specify, to receive upon exercise thereof all or a portion of the excess of (A) the Fair Market Value of a specified number of shares of Stock at the time of exercise, as determined by the Committee, over (B) a specified amount that shall not, subject to Section 5(e), be less than the Fair Market Value of such specified number of shares of Stock at the time the Right is granted. Upon exercise of a Right, payment of such excess shall be made as the Committee shall specify in cash, the issuance or transfer to the Key Employee of whole shares of Stock with a Fair Market Value at such time equal to any excess, or a combination of cash and shares of Stock with a combined Fair Market Value at such time equal to any such excess, all as determined by the Committee. The Company will not issue a fractional share of Stock and, if a fractional share would otherwise be issuable, the Company shall pay cash equal to the Fair Market Value of the fractional share of Stock at such time.

(ii) For the purposes of Subsection (i) of this Section 5(l), in the case of any such Right or portion thereof, other than a Right related to an Incentive Stock Option, exercised for cash during a “window period” specified by Rule 16b-3 under the Act, the Fair Market Value of the Stock at the time of such exercise shall be the highest composite daily closing price of the Stock during such window period.

(iii) In the event of the exercise of such Right, the Company’s obligation in respect of any related Option or such portion thereof will be discharged by payment of the Right so exercised.

6. Performance Shares

(a) Subject to the provisions of the Plan, the Committee shall (i) determine and designate from time to time those Key Employees or groups of Key Employees to whom Awards of Performance Shares are to be made, (ii) determine the Performance Period and Performance Objectives applicable to such Awards, (iii) determine the form of settlement of a Performance Share and (iv) generally determine the terms and conditions of each such Award. At any date, each Performance Share shall have a value equal to the Fair Market Value of a share of Stock at such date; provided that the Committee may limit the aggregate amount payable upon the settlement of any Award.

(b) The Committee shall determine a Performance Period of not less than two nor more than five years with respect to the award of Performance Shares. Performance Periods may overlap and Key Employees may participate simultaneously with respect to Performance Shares for which different Performance Periods are prescribed.

(c) The Committee shall determine the Performance Objectives of Awards of Performance Shares. Performance Objectives may vary from Key Employee to Key Employee and between groups of Key Employees and shall be based upon such Performance Goals as the Committee may deem appropriate. The Performance Objective shall be established by the Committee prior to, or reasonably promptly following the inception of, a Performance Period but, to the extent required by Section 162(m) of the Code, by no later than the earlier of the date that is ninety days after the commencement of the Performance Period or the day prior to the date on which twenty-five percent of the Performance Period has elapsed.

(d) Following the completion of each Performance Period, the Committee shall certify in writing, in accordance with the requirements of Section 162(m) of the Code to the extent applicable, whether the Performance Objective and other material terms for paying amounts in respect of each Performance Share Award related to that Performance Period have been achieved or met. Unless the Committee determines otherwise, Performance Share Awards shall not be settled until the Committee has made the certification specified under this Section 6(d).

(e) The Committee is authorized at any time during or after a Performance Period to reduce or eliminate the Performance Share Award of any Key Employee for any reason, including, without limitation, changes in the position or duties of any Key Employee with the Participating Company during or after a Performance Period, whether due to any termination of employment (including death, disability, retirement, voluntary termination or termination with or without cause) or otherwise. In addition, to the extent necessary to preserve the intended economic effects of the Plan to the Participating Company and the Key Employee, the Committee shall adjust Performance Objectives, the Performance Share Awards or both to take into account: (i) a change in corporate capitalization, (ii) a corporate transaction, such as any merger of the Company or any subsidiary into another corporation, any consolidation of the Company or any subsidiary into another corporation, any separation of the Company or any subsidiary (including a spin-off or the distribution of stock or property of the Company or any subsidiary), any reorganization of the Company or any subsidiary or a large, special and non-recurring dividend paid or distributed by the Company (whether or not such reorganization comes within the definition of Section 368 of the Code), (iii) any partial or complete liquidation of the Company or any subsidiary or (iv) a change in accounting or other relevant rules or regulations (any adjustment pursuant to this Clause (iv) shall be subject to the timing requirements of the last sentence of the definition of

Performance Goal set forth in Section 2 of the Plan); provided, however, that no adjustment hereunder shall be authorized or made if and to the extent that the Committee determines that such authority or the making of such adjustment would cause the Performance Bonus Awards to fail to qualify as “qualified performance-based compensation” under Section 162(m) of the Code with respect to a particular Key Employee.

(f) At the beginning of a Performance Period, the Committee shall determine for each Key Employee or group of Key Employees the number of Performance Shares or the percentage of Performance Shares that shall be paid to the Key Employee or member of the group of Key Employees if Performance Objectives are met in whole or in part.

(g) If a Key Employee terminates service with all Participating Companies during a Performance Period because of death, Total Disability, Retirement, or under other circumstances where the Committee in its sole discretion finds that a waiver would be in the best interests of the Company, that Key Employee may, as determined by the Committee, be entitled to an Award of Performance Shares at the end of the Performance Period based upon the extent to which the Performance Objectives were satisfied at the end of such period, which Award, in the discretion of the Committee, may be maintained without change or reduced and prorated for the portion of the Performance Period during which the Key Employee was employed by any Participating Company; provided, however, the Committee may provide for an earlier payment in settlement of such Performance Shares in such amount and under such terms and conditions as the Committee deems appropriate or desirable, but only to the extent consistent with the requirements of Section 162(m) of the Code to the extent applicable in respect of such Key Employee. If a Key Employee terminates service with all Participating Companies during a Performance Period for any other reason, then such Key Employee shall not be entitled to any Award with respect to that Performance Period unless the Committee shall otherwise determine.

(h) Each Award of a Performance Share shall be paid in whole shares of Stock, or cash, or a combination of Stock and cash either as a lump sum payment or in annual installments, all as the Committee shall determine, with payment to commence as soon as practicable after the end of the relevant Performance Period but no earlier than following the determination made in Section 6(d) hereof. Subject to the terms of the applicable program, the Award may also be paid in shares of Stock or Restricted Stock.

(i) With respect to Performance Shares that may be settled through the grant of Stock, a Key Employee shall not be granted Performance Shares for all of the Performance Periods commencing in a calendar year that permit the Key Employee to earn Stock covering more than the Share Limit in respect of such Key Employee. In addition, separate and apart from the limit in the previous sentence, with respect to Performance Share Awards to be settled in cash, a Key Employee shall not be granted Performance Share Awards for all of the Performance Periods commencing in a calendar year that permit the Key Employee in the aggregate to earn a cash payment in excess of the Fair Market Value of the Share Limit as of the first day of the first Performance Period commencing in such calendar year.

(j) Performance Share Awards may be structured in the form of Restricted Stock Units or any substantially similar instrument evidencing the right to receive a share of Stock, or a cash payment equal to the Fair Market Value of a share of Stock, at some future date upon the lapse of the applicable restrictions established by the Committee or upon the satisfaction of any applicable Performance Goals established by the Committee hereunder. To the extent provided for by the Committee, the rules of Section 7 shall apply to Restricted Stock Units payable in Stock.

7. Restricted Stock

(a) Restricted Stock shall be subject to a restriction period (after which restrictions will lapse), which shall mean a period commencing on the date the Award is granted and ending on such date as the Committee shall determine (the “Restriction Period”). The Committee may provide for the lapse of restrictions in installments where deemed appropriate.

(b) Except when the Committee determines otherwise pursuant to Section 7(d), if a Key Employee terminates employment with all Participating Companies for any reason before the expiration of the Restriction Period, all shares of Restricted Stock still subject to restriction shall be forfeited by the Key Employee and shall be reacquired by the Company.

(c) Except as otherwise provided in this Section 7, no shares of Restricted Stock received by a Key Employee shall be sold, exchanged, transferred, pledged, hypothecated or otherwise disposed of during the Restriction Period.

(d) In cases of death, Total Disability or Retirement or in cases of special circumstances, the Committee may, in its sole discretion when it finds that a waiver would be in the best interests of the Company, elect to waive any or all remaining restrictions with respect to such Key Employee's Restricted Stock.

(e) The Committee may require, under such terms and conditions as it deems appropriate or desirable, that the certificates for Stock delivered under the Plan may be held in custody by a bank or other institution, or that the Company may itself hold such shares in custody until the Restriction Period expires or until restrictions thereon otherwise lapse, and may require, as a condition of any Award of Restricted Stock that the Key Employee shall have delivered a stock power endorsed in blank relating to the Restricted Stock.

(f) Nothing in this Section 7 shall preclude a Key Employee from exchanging any shares of Restricted Stock subject to the restrictions contained herein for any other shares of Stock that are similarly restricted.

(g) Subject to Section 7(e) and Section 8, each Key Employee entitled to receive Restricted Stock under the Plan shall be issued a certificate for the shares of Stock. Such certificate shall be registered in the name of the Key Employee, and shall bear an appropriate legend reciting the terms, conditions and restrictions, if any, applicable to such Award and shall be subject to appropriate stop-transfer orders.

8. Certificates for Awards of Stock

(a) The Company shall not be required to issue or deliver any certificates for shares of Stock prior to (i) the listing of such shares on any stock exchange on which the Stock may then be listed and (ii) the completion of any registration or qualification of such shares under any federal or state law, or any ruling or regulation of any government body that the Company shall, in its sole discretion, determine to be necessary or advisable.

(b) All certificates for shares of Stock delivered under the Plan shall also be subject to such stop-transfer orders and other restrictions as the Committee may deem advisable under the rules, regulations, and other requirements of the Securities and Exchange Commission, any stock exchange upon which the Stock is then listed and any applicable federal or state securities laws, and the Committee may cause a legend or legends to be placed on any such certificates to make appropriate reference to such restrictions. The foregoing provisions of this Section 8(b) shall not be effective if and to the extent that the shares of Stock delivered under the Plan are covered by an effective and current registration statement under the Securities Act of 1933, or if and so long as the Committee determines that application of such provisions is no longer required or desirable. In making such determination, the Committee may rely upon an opinion of counsel for the Company.

(c) Except for the restrictions on Restricted Stock under Section 7, each Key Employee who receives Stock in settlement of an Award of Stock, shall have all of the rights of a shareholder with respect to such shares, including the right to vote the shares and receive dividends and other distributions. No Key Employee awarded an Option, a Right or Performance Share shall have any right as a shareholder with respect to any shares covered by his or her Option, Right or Performance Share prior to the date of issuance to him or her of a certificate or certificates for such shares.

9. Management Performance Bonus Awards

(a) Form of Award. The Committee is authorized to grant Awards pursuant to this Section 9. An Award shall represent the conditional right of the Participant to receive cash, or at the discretion of the Committee (and subject to the limitations in Section 3), in whole or in part in shares of stock, based upon achievement of one or more pre-established Performance Objectives during a Performance Period, subject to the terms of this Section 9 and the other applicable terms of the Plan. Awards shall be subject to such conditions, including deferral of settlement, risks of forfeiture, restrictions on transferability and other terms and conditions as shall be specified by the Committee. The Performance Bonus Award hereunder may take the form of a percentage of a bonus pool the magnitude of which shall be determined in a manner consistent with the determination of individual Performance Bonus Awards based on individual Performance Objectives hereunder for all of the members in the pool, with the time period for establishing the magnitude of the pool and the fixing of the applicable percentage available to any individual determined in accordance with the requirements of Section 162(m) of the Code applicable to any such individuals in the pool.

(b) Performance Objectives. The Committee shall establish the Performance Objective for each Performance Bonus Award, consisting of one or more business criteria permitted as Performance Goals hereunder, one or more levels of performance with respect to each such criteria, and the amount or amounts payable or other rights that the Participant will be entitled to upon achievement of such levels of performance. The Performance Objective shall be established by the Committee prior to, or reasonably promptly following the inception of, a Performance Period but, to the extent required by Section 162(m) of the Code, by no later than the earlier of the date that is ninety days after the commencement of the Performance Period or the day prior to the date on which twenty-five percent of the Performance Period has elapsed.

(c) Additional Provisions Applicable to Performance Bonus Awards. More than one Performance Goal may be incorporated in a Performance Objective, in which case achievement with respect to each Performance Goal may be assessed individually or in combination with each other. The Committee may, in connection with the establishment of Performance Objectives for a Performance Period, establish a matrix setting forth the relationship between performance on two or more Performance Goals and the amount of the Performance Bonus Award payable for that Performance Period. The level or levels of performance specified with respect to a Performance Goal may be established in absolute terms, as objectives relative to performance in prior periods, as an objective compared to the performance of one or more comparable companies or an index covering multiple companies, or otherwise as the Committee may determine. Performance Objectives shall be objective and shall otherwise meet the requirements of Section 162(m) of the Code. Performance Objectives may differ for Performance Bonus Awards granted to any one Participant or to different Participants.

(d) Duration of the Performance Period. The Committee shall establish the duration of each Performance Period at the time that it sets the Performance Objectives applicable to that Performance Period. The Committee shall be authorized to permit overlapping or consecutive Performance Periods.

(e) Certification. Following the completion of each Performance Period, the Committee shall certify in writing, in accordance with the requirements of Section 162(m) of the Code, whether the Performance Objective and other material terms for paying amounts in respect of each Performance Bonus Award related to that Performance Period have been achieved or met. Unless the Committee determines otherwise, Performance Bonus Awards shall not be settled until the Committee has made the certification specified under this Section 9(e).

(f) Adjustment. The Committee is authorized at any time during or after a Performance Period to reduce or eliminate the Performance Bonus Award of any Participant for any reason, including, without limitation, changes in the position or duties of any Participant with the Participating Company during or after a Performance Period, whether due to any termination of employment (including death, disability, Retirement, voluntary termination or termination with or without cause) or otherwise. In addition, to the extent necessary to preserve the intended economic effects of the Plan to the Participating Company and the Participants, the Committee shall adjust Performance Objectives, the Performance Bonus Awards or both to

take into account: (i) a change in corporate capitalization, (ii) a corporate transaction, such as any merger of the Company or any subsidiary into another corporation, any consolidation of the Company or any subsidiary into another corporation, any separation of the Company or any subsidiary (including a spin-off or the distribution of stock or property of the Company or any subsidiary), any reorganization of the Company or any subsidiary or a large, special and non-recurring dividend paid or distributed by the Company (whether or not such reorganization comes within the definition of Section 368 of the Code), (iii) any partial or complete liquidation of the Company or any subsidiary or (iv) a change in accounting or other relevant rules or regulations (any adjustment pursuant to this Clause (iv) shall be subject to the timing requirements of the last sentence of the definition of Performance Goal set forth in Section 2 of the Plan); provided, however, that no adjustment hereunder shall be authorized or made if and to the extent that the Committee determines that such authority or the making of such adjustment would cause the Performance Bonus Awards to fail to qualify as “qualified performance-based compensation” under Section 162(m) of the Code.

(g) Timing of Payment. Except as provided below, any amounts payable in respect of Performance Bonus Awards for a Performance Period will generally be paid as soon as practicable following the determination in respect thereof made pursuant to Section 9(e).

(h) Deferral of Payments. Subject to such terms, conditions and administrative guidelines as the Committee shall specify from time to time, a Participant shall have the right to elect to defer receipt of part or all of any payment due with respect to a Performance Bonus Award.

(i) Maximum Amount Payable Per Participant Under This Section 9. A Participant shall not be granted Performance Bonus Awards for all of the Performance Periods commencing in a calendar year that permit the Participant in the aggregate to earn a payment in excess of 200% of the Participant’s base salary in effect at the beginning of such calendar year.

(j) Termination of Employment. In the event a Participant terminates employment for any reason during a Performance Period or prior to the Performance Bonus Award payment, he or she (or his or her Beneficiary, in the case of death) shall not be entitled to receive any Performance Bonus Award for such Performance Period unless the Committee, in its sole and absolute discretion, elects to pay all or any part of a Performance Bonus Award to such Participant.

10. Change in Control

Notwithstanding any provisions in this Plan to the contrary:

(a) Each outstanding Option granted under the Plan shall become immediately exercisable in full for the aggregate number of shares covered thereby and all related Rights shall also become exercisable upon the occurrence of a Change in Control and shall continue to be exercisable in full for cash for a period of 60 calendar days beginning on the date that such Change in Control occurs and ending on the 60th calendar day following that date; provided, however, that no Option or Right shall be exercisable beyond the expiration date of its original term.

(b) Options and Rights shall not terminate and shall continue to be fully exercisable for a period of seven months following the occurrence of a Change in Control in the case of an employee who is terminated other than for just cause or who voluntarily terminates his or her employment because he or she in good faith believes that as a result of such Change in Control he or she is unable effectively to discharge the duties of the position he or she occupied just prior to the occurrence of such Change in Control. For purposes of Section 10 only, termination shall be for “just cause” only if such termination is based on fraud, misappropriation or embezzlement on the part of the employee that results in a final conviction of a felony. Under no circumstances, however, shall any Option or Right be exercised beyond the expiration date of its original term.

(c) Any Right or portion thereof may be exercised for cash within the 60-calendar-day period following the occurrence of a Change in Control with settlement, except in the case of a Right

related to an Incentive Stock Option, based on the "Formula Price" that shall be the highest of (A) the highest composite daily closing price of the Stock during the period beginning on the 60th calendar day prior to the date on which the Right is exercised and ending on the date such Right is exercised, (B) the highest gross price paid for the Stock during the same period of time, as reported in a report on Schedule 13D filed with the Securities and Exchange Commission or (C) the highest gross price paid or to be paid for a share of Stock (whether by way of exchange, conversion, distribution upon merger, liquidation or otherwise) in any of the transactions set forth in the definition of "Change in Control" in the Retirement Plan.

(d) Upon the occurrence of a Change in Control, Limited Stock Appreciation Rights shall automatically be granted as to any Option with respect to which Rights are not then outstanding; provided, however, that Limited Stock Appreciation Rights shall be provided at the time of grant of any Incentive Stock Option subject to exercisability upon the occurrence of a Change in Control. Limited Stock Appreciation Rights shall entitle the holder thereof, upon exercise of such rights and surrender of the related Option or any portion thereof, to receive, without payment to the Company (except for applicable withholding taxes), an amount in cash equal to the excess, if any, of the Formula Price as that term is defined in Section 10 over the exercise price of the Stock as provided in such Option; provided that in the case of the exercise of any such Limited Stock Appreciation Right or portion thereof related to an Incentive Stock Option, the Fair Market Value of the Stock at the time of such exercise shall be substituted for the Formula Price. Each such Limited Stock Appreciation Right shall be exercisable only during the period beginning on the first business day following the occurrence of such Change in Control and ending on the 60th calendar day following such date and only to the same extent the related Option is exercisable. Upon exercise of a Limited Stock Appreciation Right and surrender of the related Option, or portion thereof, such Option, to the extent surrendered, shall not thereafter be exercisable.

(e) The restrictions applicable to Awards of Restricted Stock issued pursuant to Section 7 shall lapse upon the occurrence of a Change in Control and the Company shall issue stock certificates without a restrictive legend. Key Employees holding Restricted Stock on the date of a Change in Control may tender such Restricted Stock to the Company that shall pay the Formula Price as that term is defined in Section 10; provided, such Restricted Stock must be tendered to the Company within 60 calendar days of the Change in Control.

(f) If a Change in Control occurs during the course of a Performance Period applicable to an Award of Performance Shares pursuant to Section 6, then the Key Employee shall be deemed to have satisfied the Performance Objectives and settlement of such Performance Shares shall be based on the Formula Price, as defined in this Section 10.

11. Beneficiary

The Beneficiary of a Key Employee shall be the Key Employee's estate, which shall be entitled to receive the Award, if any, payable under the Plan upon his or her death. A Key Employee may file with the Company a written designation of one or more persons as a Beneficiary in lieu of his or her estate, who shall be entitled to receive the Award, if any, payable under the Plan upon his or her death, subject to the enforceability of the designation under applicable law at that time. A Key Employee may from time-to-time revoke or change his or her Beneficiary designation, with or without the consent of any prior Beneficiary as required by applicable law, by filing a new designation with the Company. Subject to the foregoing, the last such designation received by the Company shall be controlling; provided, however, that no designation, or change or revocation thereof, shall be effective unless received by the Company prior to the Key Employee's death, and in no event shall it be effective as of a date prior to such receipt. If the Committee is in doubt as to the right of any person to receive such Award, the Company may retain such Award, without liability for any interest thereon, until the Committee determines the rights thereto, or the Company may pay such Award into any court of appropriate jurisdiction and such payment shall be a complete discharge of the liability of the Company therefore.

12. Administration of the Plan

(a) Each member of the Committee shall be both a member of the Board, a “non-employee director” within the meaning of Rule 16b-3(b)(3)(i) under the Act or successor rule or regulation and an “outside director” within the meaning of Section 162(m) of the Code.

(b) All decisions, determinations or actions of the Committee made or taken pursuant to grants of authority under the Plan shall be made or taken in the sole discretion of the Committee and shall be final, conclusive and binding on all persons for all purposes.

(c) The Committee shall have full power, discretion and authority to interpret, construe and administer the Plan and any part thereof, and its interpretations and constructions thereof and actions taken thereunder shall be, except as otherwise determined by the Board, final, conclusive and binding on all persons for all purposes.

(d) The Committee’s decisions and determinations under the Plan need not be uniform and may be made selectively among Key Employees, whether or not such Key Employees are similarly situated.

(e) The Committee may, in its sole discretion, delegate such of its powers as it deems appropriate; provided, however, that the Committee may not delegate its responsibility (i) to make Awards to executive officers of the Company; (ii) to make Awards that are intended to constitute “qualified performance-based compensation” under Section 162(m) of the Code; or (iii) to certify the satisfaction of Performance Objectives pursuant to Sections 6(d) or 9(e) in accordance with Section 162(m) of the Code. The Committee may also appoint agents to assist in the day-to-day administration of the Plan and may delegate the authority to execute documents under the Plan to one or more members of the Committee or to one or more officers of the Company.

(f) If a Change in Control has not occurred and if the Committee determines that a Key Employee has taken action inimical to the best interests of any Participating Company, the Committee may, in its sole discretion, terminate in whole or in part such portion of any Option (including any related Right) as has not yet become exercisable at the time of termination, terminate any Performance Share Award for which the Performance Period has not been completed or terminate any Award of Restricted Stock for which the Restriction Period has not lapsed.

13. Amendment, Extension or Termination

The Board may, at any time, amend or terminate the Plan and, specifically, may make such modifications to the Plan as it deems necessary to avoid the application of Section 162(m) of the Code and the Treasury regulations issued thereunder. However, no amendment shall, without approval by a majority of the Company’s stockholders, (a) alter the group of persons eligible to participate in the Plan, (b) except as provided in Section 14 increase the maximum number of shares of Stock that are available for Awards under the Plan, or (c) except for adjustments pursuant to Section 14 or as otherwise provided for in the Plan, decrease the Option price for any outstanding Option after the date the Option is granted or accept the surrender of any outstanding Option as consideration for the grant of a new Option with a lower price than the Option being surrendered. If a Change in Control has occurred, no amendment or termination shall impair the rights of any person with respect to a prior Award.

14. Adjustments in Event of Change in Common Stock

In the event of any recapitalization, reclassification, split-up or consolidation of shares of Stock or stock dividend, merger or consolidation of the Company or sale by the Company of all or a portion of its assets, the Committee shall make such adjustments in the Stock subject to Awards, including Stock subject to purchase by an Option, or the terms, conditions or restrictions on Stock or Awards, including the price payable upon the exercise of such Option, as the Committee deems equitable; provided however, that in the event of a stock split, stock dividend or consolidation of shares, the number of shares subject to an outstanding Option and the exercise price thereof, and the number of outstanding Performance Shares, shall be proportionately

adjusted to reflect such action. With respect to Awards intended to qualify as “performance-based compensation” under Section 162(m) of the Code, such adjustments shall be made only to the extent that the Committee determines that such adjustments may be made without a loss of deductibility for such Awards under Section 162(m) of the Code.

15. Forfeiture of Gains on Exercise. Except following a Change in Control, if the Key Employee terminates employment in breach of any covenants and conditions subsequent set forth in Section 16 and becomes employed by a competitor of the Company within one year after the date of exercise of any Option or the receipt of any Award, the Key Employee shall pay to the Company an amount equal to any gain from the exercise of the Option or the value of the Award other than Options, in each case measured by the amount reported as taxable compensation to the Key Employee by the Company for federal income tax purposes and in the case of Options that are incentive stock options, in an amount equal to the amount that would have been reported as taxable income were such Options not incentive stock options, and in each case without regard to any subsequent fluctuation in the market price of the shares of common stock of the Company. Any such amount due hereunder shall be paid by the Key Employee within thirty days of becoming employed by a competitor. By accepting an Option or other Award hereunder, the Key Employee is authorizing the Company to withhold, to the extent permitted by law, the amount owed to the Company hereunder from any amounts that the Company may owe to the Key Employee in any capacity whatsoever.

16. Conditions Subsequent. Except after a Change in Control, the exercise of any Option or Right and the receipt of any Award shall be subject to the satisfaction of the following conditions subsequent: (i) that Key Employee refrain from engaging in any activity that in the opinion of the Committee is competitive with any activity of the Company or any Subsidiary, excluding any activity undertaken upon the written approval or request of the Company, (ii) that Key Employee refrain from otherwise acting in a manner inimical or in any way contrary to the best interests of the Company, and (iii) that the Key Employee furnish the Company such information with respect to the satisfaction of the foregoing conditions subsequent as the Committee shall reasonably request. In addition, except as may otherwise be excused by action of the Committee, the Key Employee by the exercise of the Option or the receipt of the Award agrees to remain in the employ of the Company, unless earlier terminated by the Company or by the Key Employee by reason of his or her death, disability or retirement.

17. Miscellaneous

(a) Except as provided in Section 10, nothing in this Plan or any Award granted hereunder shall confer upon any employee any right to continue in the employ of any Participating Company or interfere in any way with the right of any Participating Company to terminate his or her employment at any time. No Award payable under the Plan shall be deemed salary or compensation for the purpose of computing benefits under any employee benefit plan or other arrangement of any Participating Company for the benefit of its employees unless the Company shall determine otherwise. No Key Employee shall have any claim to an Award until it is actually granted under the Plan. To the extent that any person acquires a right to receive payments from the Company under this Plan, such right shall be no greater than the right of an unsecured general creditor of the Company. All payments to be made hereunder shall be paid from the general funds of the Company and no special or separate fund shall be established and no segregation of assets shall be made to assure payment of such amounts except as provided in Section 7(e) with respect to Restricted Stock.

(b) The Committee may cause to be made, as a condition precedent to the payment of any Award, or otherwise, appropriate arrangements with the Key Employee or his or her Beneficiary, for the withholding of any federal, state, local or foreign taxes.

(c) The Plan and the grant of Awards shall be subject to all applicable federal and state laws, rules, and regulations and to such approvals by any government or regulatory agency as may be required.

(d) The terms of the Plan shall be binding upon the Company and its successors and assigns.

(e) Captions preceding the sections hereof are inserted solely as a matter of convenience and in no way define or limit the scope or intent of any provision hereof.

(f) To the extent Awards issued under the Plan are intended to be exempt from the application of Section 162(m) of the Code, which restricts under certain circumstances the Federal income tax deduction for compensation paid by a public company to named executives in excess of \$1 million per year, the Committee may, without stockholder approval, amend the Plan retroactively or prospectively to the extent it determines necessary in order to comply with any subsequent clarification of Section 162(m) of the Code required to preserve the Company's Federal income tax deduction for compensation paid pursuant to the Plan.

18. Effective Date, Term of Plan and Shareholder Approval

The effective date of the Plan is January 1, 2004. The Plan will continue in effect for existing Awards as long as any such Award is outstanding. Unless the Company determines otherwise, Section 6 and 9 of the Plan and the definition of "Performance Goal" shall be submitted to the Company's stockholders at the first stockholder meeting that occurs in the fifth year following the year in which the Plan was last approved by stockholders (or any earlier meeting designated by the Board), in accordance with the requirements of Section 162(m) of the Code.

FEDERAL INCOME TAX TREATMENT

The following is a brief summary of the current Federal income tax rules generally applicable to options, stock appreciation rights, performance shares and restricted stock. Recipients of Awards and Substitute Stock Options should consult their own tax advisors as to the specific Federal, state and local tax consequences applicable to them.

A. Options and Stock Appreciation Rights

Options granted under the Plan may be either non-qualified options or "incentive stock options" qualifying under Section 422 of the Internal Revenue Code. The Substitute Stock Options are non-qualified options.

Non-qualified Options

An optionee is not subject to Federal income tax upon grant of a non-qualified option. At the time of exercise, the optionee will realize compensation income (subject to withholding) to the extent that the then fair market value of the stock exceeds the option price. The amount of such income will constitute an addition to the optionee's tax basis in the optioned stock. Sale of the shares will result in capital gain or loss (long-term or short-term depending on the optionee's holding period). Rayonier is entitled to a Federal tax deduction at the same time and to the same extent that the optionee realizes compensation income.

Incentive Stock Options ("ISOs")

Options under the Plan denominated as ISOs are intended to constitute incentive stock options under Section 422 of the Internal Revenue Code of 1986, as amended. An optionee is not subject to Federal income tax upon either the grant or exercise of an ISO. If the optionee holds the shares acquired upon exercise for at least one year after issuance of the optioned shares and until at least two years after grant of the option, then the difference between the amount realized on a subsequent sale or other taxable disposition of the shares and the option price will constitute long-term capital gain or loss. To obtain favorable tax treatment, an ISO must be exercised within three months after termination of employment (other than by retirement, disability, or death) with Rayonier or subsidiary. To obtain favorable tax treatment, an ISO must be exercised within three months of retirement or within one year of cessation of employment for disability (with no limitation in the case of death), notwithstanding any longer exercise period permitted under the terms of the Plan. Rayonier will not be entitled to a Federal tax deduction with respect to the grant or exercise of the ISO.

If the optionee disposes of the shares acquired under an ISO before the requisite holding period, he or she will be deemed to have made a “disqualifying disposition” of the shares and will realize compensation income in the year of disposition equal to the lesser of the fair market value of the shares at exercise or the amount realized on their disposition over the option price of the shares. (However, if the disposition is by gift or by sale to a related party, the compensation income must be measured by the value of the shares at exercise over the option price.) Any gain recognized upon a disqualifying disposition in excess of the ordinary income portion will constitute either short-term or long-term capital gain. In the event of a disqualifying disposition, Rayonier will be entitled to a Federal tax deduction in the amount of the compensation income realized by the optionee.

The option spread on the exercise of an ISO is an adjustment in computing alternative minimum taxable income. No adjustment is required, however, if the optionee made a disqualifying disposition of the shares in the same year as he or she is taxed on the exercise.

Stock Appreciation Rights (“SARs”)

SARs may be awarded to officers and directors of Rayonier subject to Section 16(b) of the Securities Exchange Act of 1934 with respect to both incentive stock options and non-qualified options granted under the Plan. An optionee is not taxed upon the grant of SARs. An optionee exercising SARs for cash will realize compensation income (subject to withholding) in the amount of the cash received. Rayonier is entitled to a tax deduction at the same time and to the same extent that the optionee realizes compensation income.

B. Performance Shares

A recipient of performance shares generally will realize compensation income (subject to withholding) when and to the extent that payment is made, whether in the form of cash or shares of Rayonier Common Shares. To the extent that payment is made in the form of stock, income shall be measured by the then fair market value of the shares, which shall constitute an addition to the recipient’s tax basis in such shares. Rayonier will be entitled to a Federal tax deduction for the value of payment at the time of payment.

C. Restricted Stock

A recipient of restricted stock generally will realize compensation income (subject to withholding) when and to the extent that the restrictions on the shares lapse, as measured by the value of the shares at the time of lapse. The recipient’s holding period for the shares will not commence until the date of lapse, and dividends paid during the restriction period will be treated as compensation. The income realized on lapse of the restrictions will constitute an addition to the recipient’s tax basis in the shares.

In lieu of deferred recognition of income, the recipient may file an election with the Internal Revenue Service, within 30 days of award, to realize compensation income at the time of award, as measured by the fair market value of the stock on the date of award determined without regard to the restrictions. The income realized will constitute an addition to the tax basis of the shares. In the case of such election, any appreciation (or depreciation) on the shares during the restriction period will give rise to capital gain (or capital loss). In the event that the recipient terminates employment during the restriction period and forfeits his or her shares, no deduction may be claimed and the taxes paid on award of the shares shall be forfeited.

Rayonier will be entitled to a Federal tax deduction at the same time and to the same extent that the recipient realizes compensation income.

Rayonier Inc. and Subsidiaries
Ratio of Earnings to Fixed Charges
(Unaudited, thousands of dollars)

	<u>Six Months Ended June 30,</u>	
	<u>2006</u>	<u>2005</u>
Earnings:		
Income from Continuing Operations	\$ 66,082	\$ 76,415
Add:		
Income tax expense	9,879	(3,815)
Amortization of capitalized interest	938	1,194
	<u>76,899</u>	<u>73,794</u>
Adjustments to earnings for fixed charges:		
Interest and other financial charges	24,063	25,140
Interest factor attributable to rentals	361	238
	<u>24,424</u>	<u>25,378</u>
Earnings as adjusted	<u>\$ 101,323</u>	<u>\$ 99,172</u>
Fixed Charges:		
Total fixed charges above	\$ 24,424	\$ 25,378
Ratio of earnings as adjusted to total fixed charges	<u>4.15</u>	<u>3.91</u>

CERTIFICATION

I, W. L. Nutter, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rayonier Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 2, 2006

/s/ W. L. NUTTER

W. L. Nutter
*Chairman, President and
Chief Executive Officer, Rayonier Inc.*

CERTIFICATION

I, Hans E. Vanden Noort, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rayonier Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 2, 2006

/s/ HANS E. VANDEN NOORT

Hans E. Vanden Noort
Senior Vice President and
Chief Accounting Officer, Rayonier Inc.

CERTIFICATION

I, Carl E. Kraus, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Rayonier Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer(s) and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f)) for the registrant and have:
 - a. Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
 - b. Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles;
 - c. Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
 - d. Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and
5. The registrant's other certifying officer(s) and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
 - a. All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
 - b. Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: August 2, 2006

/s/ CARL E. KRAUS

Carl E. Kraus

Senior Vice President - Finance, Rayonier Inc.

CERTIFICATION

The undersigned hereby certify, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, 18 U.S.C. Section 1350, that:

1. The quarterly report on Form 10-Q of Rayonier Inc. (the "Company") for the period ended June 30, 2006 (the "Report") fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934; and
2. The information in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

August 2, 2006

/s/ W. L. NUTTER

W. L. Nutter
*Chairman, President and
Chief Executive Officer*

/s/ HANS E. VANDEN NOORT

Hans E. Vanden Noort
*Senior Vice President and
Chief Accounting Officer*

/s/ CARL E. KRAUS

Carl E. Kraus
Senior Vice President, Finance

A signed original of this written statement required by Section 906 has been provided to Rayonier and will be retained by Rayonier and furnished to the Securities and Exchange Commission or its staff upon request.