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VIA EMAIL (licensing@nunavutwaterboard.org)

January 31, 2011

Nunavut Water Board
PO Box 119
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Attention: Phyllis Beaulieu, Manager of Licensing

Dear Ms. Beaulieu:

Re: Request for Extension of the Term of Nunavut Water Board Water License 2AM-JER0410 (the "Water Licence")

We are writing to request an extension of the term of the Water License to March 1, 2012 on an emergency basis pursuant to subsections 52(2), 55(5) and 174(1)(a)(ii) of the *Nunavut Waters and Nunavut Surface Rights Tribunal Act* (the "Act").

Pursuant to a decision of the Nunavut Water Board ("NWB"), the Water License was assigned to Shear Diamonds (Nunavut) Corp. ("Shear Nunavut") on December 17, 2010. Shear Nunavut is a wholly owned subsidiary of Shear Diamonds Ltd. ("Shear"). The Water License assignment application included a compliance audit conducted by Shear that outlined the deficiencies and non-compliances with the Water Licence under the ownership of Shear Nunavut's predecessors in interest, Tahera Diamond Corporation ("TDC") and Benachee Resources Inc. TDC and Benachee filed for protection under the *Companies' Creditors Arrangement Act* ("CCAA") on January 16, 2008. Shear also submitted, and was granted on December 17th, 2010, an application to extend the term of the Water License for a maximum 60 days pursuant to the Act. The term of the Water License was extended to March 1, 2011.

The Water License pertains to the Jericho Diamond Mine (the "Jericho Mine"). As outlined in detail below, Shear has identified a number of issues at the mine site that, if left unattended, will result in environmental contamination. An extension of the term of the Water License is necessary to permit Shear to operate the property under an agreed care and maintenance protocol

(“Care and Maintenance”) and conduct site operations over the course of the next year while the NWB undertakes the formal process of reviewing Shear’s renewal application.

Shear has been working on the Water License renewal application with the intent to submit same by the end of February 2011. The application will include updated plans required under the Water License but not approved while under previous TDC ownership. This has been an ambitious undertaking given the quality and state of the plans previously submitted by TDC. The critical plans that relate to water use and waste disposal include: the Aquatic Effects Monitoring Plan, Waste Management Plan, Site Water Management Plan, Waste Rock Management Plan, Wastewater Treatment Management Plan, Process Kimberlite Management Plan, Waste Rock Management Plan, General Monitoring Plan, Landfarm Management Plan, Landfill Management Plan and the Interim Closure and Reclamation Plan.

The Jericho Mine has been on Care and Maintenance since mining operations were suspended in June of 2008. A Care and Maintenance Plan had been required under the Water License and was requested on several occasions by the NWB, Kitikmeot Inuit Association (the “KIA”) and Indian and Northern Affairs Canada (“INAC”), however a formal Care and Maintenance Plan for the site was never submitted.

Through its review of the history of the Jericho Mine, site inspection reports and visits to the site in the fall, Shear has become aware of a number of issues that require immediate attention and action on site during the Care and Maintenance phase of the project. Shear has prepared a Care and Maintenance Plan for the Jericho Mine, enclosed for review and approval, that clearly identifies the site water management undertakings that we believe support the request to amend the term of the licence on an emergency basis. Left unattended, these issues have the potential to jeopardize the integrity of engineered structures and cause serious environmental harm. Additionally, Shear is providing a Workplan for 2011 – 2012 that describes the activities that are required to support the determination of the future of the Jericho Mine.

The activities required and described in the Care and Maintenance Plan cannot be undertaken without a valid Type A water licence. Shear is respectfully requesting that the Nunavut Water Board exercise its authority under the Act to alter the term of the Water License on an emergency basis and extend the Water License to March 1, 2012

The extension of the term of the Water License is necessary for two reasons: (a) to provide Shear with the ability to operate under Care and Maintenance while the renewal application is reviewed, and (b) to provide the NWB with the time it requires to consider the renewal application and, if necessary, hold public hearings with respect to the renewal.

Section 52(2)(c) of the Act provides:

(c) a public hearing need not be held in the case of an application for the amendment of a licence where the Board, with the consent of the Minister, declares the amendment to be required on an emergency basis.

Section 55(5) of the Act provides:

(5) Subsections (1) and (4) [giving public notice of an application in relation to a license] do not apply in respect of an application for the amendment of a licence where the Board, with the consent of the Minister, declares the amendment to be required on an emergency basis.

Similarly, Section 174 of the Act states:

(1) The regulations made under paragraph 33(1)(c) of the *Northwest Territories Waters Act* are deemed, in relation to the use of waters or the deposit of waste in Nunavut, to prescribe, as classes of applications that are exempt from the requirement of a public hearing, the classes of applications in relation to the following:

(a) in the case of a Type A licence,

....

(ii) any amendment that affects the use, flow or quality of waters or alters the term of the licence, where the Nunavut Water Board, with the consent of the Minister, is of the opinion that an emergency exists that requires the amendment,...

The four most critical action items are described below. If the Water License is not extended so that Shear can deal with these items in a responsible manner, these conditions will lead, Shear believes, to contamination of the receiving environment. Accordingly, these conditions form the basis of our request that the NWB declare that an emergency situation exists. The four critical items are as follows:

1. The Processed Kimberlite Containment Area ("PKCA") is a designed structure with a limited storage capacity. Controlled discharge on an on-going basis is necessary to maintain the required one meter of freeboard. The situation at the mine site today is such that the current capacity of the PKCA is equal to the predicted mean year monthly runoff for June. Left unattended, the water levels will breach the geotechnical structures and enter the receiving environment uncontrolled. The analysis of the water prior to discharge and subsequent controlled release of water is required to prevent damage to the retention structures, mitigate the potential for erosion and ensure that waters entering the receiving environment meet regulated discharge criteria.
2. The secondary containment facilities for the bulk storage of fuel contain contaminated soil. These containment facilities fill with melt-water during freshet and during large rain events and the water is subsequently contaminated by contact with the soil. The contaminated water created in these facilities must be managed and treated to prevent an uncontrolled release of contaminated water into the receiving environment. During the past two years, the melt and storm water was pumped directly to the PKCA. Given the limited capacity of the PKCA, it is imperative that contaminated water not be pumped directly to the PKCA. The water needs to be treated before it is pumped to the PKCA.

Shear is currently investigating mobile water treatment facilities that handle hydrocarbon contaminated water. The Care and Maintenance Plan describes how the water will be treated prior to being re-directed to the PKCA.

Shear has determined that improper materials were used to construct the secondary containment berm (Phase I) around the bulk fuel storage facility and critical errors were made in the construction of the berm which has led to significant settling in some areas seriously jeopardizing its already questionable stability. Although the original design submitted was stamped by an engineer, the structure was not built to the engineered specifications and as such no as-builts were generated or submitted.

Environment Canada and INAC have raised concerns during their inspections with regard to the settling occurring at Phase I. This is a direct result of the use of improper materials at the time of construction. Shear has addressed the plans to decommission Phase I in the Workplan enclosed.

3. Each year, site water is collected and pumped to the PKCA because it does not meet discharge criteria. The collected water is discharged upstream of the Divider Dyke which acts as a filter. Shear will need to be on site to collect these waters to ensure they do not enter the receiving environment. As previously stated, the current capacity of the PKCA is precarious and without discharge from the PKCA the introduction of additional waters would be irresponsible and unconscionable.
4. Snow needs to be cleared from the C1 diversion channel annually to avoid the potential of creating a snow block. If left unattended the subsequent melt waters will overflow the channel and lead to erosion and the deposition of deleterious substances into the receiving environment.

In all four of these cases, if the corrective actions noted above are not taken on a timely basis, unnecessary contamination will occur. The Inspector's Direction issued to TDC by INAC on December 11, 2008, shortly before INAC took control over the Mine Site, describes these same concerns and finds that they "may pose a significant risk of damage to the property and the environment occasioned by unauthorized uses of water, deposits of waste, or failures of works."

The pending expiry of the Water License makes it imperative that steps be taken now to avoid contamination. Such is the nature of the emergency situation requiring a consent and declaration to extend the Water License. If the Water License is extended, all reasonable action will be taken by Shear to ensure that the situations outlined above do not result in further contamination and, furthermore, the NWB will have an opportunity to complete its review of the renewal application.

The pending expiry of the licence on March 1, 2011 creates an emergency. It is within the statutory power of the Nunavut Water Board to declare that an emergency exists and amend the license to provide for a limited extension of its term without a public hearing, with your consent. From our discussions with the Nunavut Water Board, Indian and Northern Affairs Canada and the Kitikmeot Inuit Association, it is our understanding that everyone is aware of, and support,

our request. We propose, for practical purposes, that such extension be to March 1, 2012 for the reasons above noted.

We request your attention to this issue on an urgent basis and look forward to a response from your office at your earliest opportunity.

Respectfully yours,

Shear Diamonds Ltd. & Shear Diamonds (Nunavut) Corp.



Pamela Strand, M.Sc., P.Geol.
President



Julie Lassonde, B.Sc.
Executive Chairman

cc: Robin Aitken, Regional Director General, INAC Nunavut Regional Office

Charlie Evalik, President, Kitikmeot Inuit Association

Jim Rogers, Manager Water Resources, INAC Nunavut Regional Office

Glen Stephens, Director, Land and Water Management, INAC Ottawa

Hon. Peter Taptuna, Deputy Premier, Minister of Economic Development & Transportation,
Minister Responsible for Mines, Deputy Premier, Government of Nunavut

Stephanie Autut, Executive Director, NIRB

Sharon Ehaloak, Executive Director, NPC