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July 11, 2011

Mr. Bernie McLissac, Director of Operations
Aboriginal Affairs and Northern Development Canada (AANDC)
Water Resources Division
Nunavut Regional Office
Iqaluit, NU X0E 0H0

Re: 2AM-JER0410 – Shear Diamonds (Nunavut) Corp. – Application for Renewal – Indian and Northern Affairs Canada Intervention to June 20-21, 2011 Pre-Hearing Technical Meeting

This letter is in response to matters raised in your letter on behalf of Indian and Northern Affairs Canada, now referred to as Aboriginal Affairs and Northern Development Canada (AANDC), dated June 13, 2011.

Shear prepared written responses to the 88 intervenor comments including all the issues identified by AANDC. These responses were then discussed during the course of the Pre-Hearing Conference held in Cambridge Bay, June 20-21, 2011. As a result of this a list of commitments was generated by the Nunavut Water Board for all parties. In the spirit of the original and ongoing discussions with INAC, Shear facilitated a site visit to Jericho for AANDC and their consultants the day after the Hearings.

At the Pre-Hearing Conference it was acknowledged by AANDC and their consultant that they were evaluating and commenting solely on the documents that Shear had filed in support of its Water Licence renewal application, and not the comprehensive list of documents filed by the original owner, Tahera. These documents formed the basis for construction and operation of the original mine: documents which, through its purchase of the Jericho Diamond Mine, bind Shear's operation of the Mine to the same extent as those new plans (once approved by the NWB) it has provided in support of the licence renewal.

The following sets out Shear's response to specific key issues raised in your letter of June 13th.

Firstly, your letter states **“it appears that activities will focus on care and maintenance, exploration, analysis of existing conditions and infrastructure, responding to known and as yet unknown site conditions requiring intervention and remediation.”** AANDC goes on to recommend that **“any renewed licence permit only those activities for which Shear plans to undertake within the next 18-24 months, and which are supported by well-developed operational plans.”**

Shear is concerned that these statements indicate a misperception of Shear's objectives for the Jericho Diamond Mine (the Mine) and for the Type A Water Licence that Shear currently holds and is applying for renewal, and of the process agreed to by all concerned parties, including AANDC, in late 2010. Shear purchased the Mine - a property for which AANDC was responsible for oversight of care and maintenance since December 2008. Shear purchased the Mine assets specifically for the purpose of re-commencing diamond production, mining and operations – not for the purpose of keeping it in a state of care and

maintenance. The Mine was purchased with a full Type A Water Licence, a licence under which the original owner constructed and operated the Mine until the operation was suspended on a temporary basis for financial reasons. Being put into a stage of care and maintenance has not prevented other northern mines in the Nunavut jurisdiction from being issued a Type A Water Licence while in this phase and at this time, no rationale has been put forward for imposing such an impediment on this Mine.

The Type A Water Licence is a key asset of the Mine and in order for the Mine to be operational again, the full Type A Water Licence will need to be renewed. The renewed Type A water licence is essential to Shear's ability to successfully re-open the Mine in a timely manner. Discussions with INAC prior to the acquisition of Jericho gave Shear the confidence that Shear would be given a fair opportunity to renew Jericho's water licence. The assertions made by INAC in those discussions formed an important element upon which Shear based its decision to acquire the Jericho property.

In terms of the plans referred to by yourself, the approach and procedures to be followed by Shear to seek renewal of the current NWB licence was established through consultation of all concerned parties, including AANDC, and culminated in an 'agreed to' process in October 2010. On this basis, Shear initiated studies and developed plans, many of which have been filed sequentially in accordance with the schedule agreed to by the parties. In addition, and based on the information it had at the time, Shear prepared a workplan that was filed, on a voluntary basis, with the NWB on January 31, 2011. That plan did indeed focus, in part, on the matters set out in your letter. However, the workplan also detailed some of the potential activities that Shear might undertake but at no time excluded additional activities or the acceleration of re-commencement of active processing of ore and mining.

By its very nature, a workplan is dynamic and subsequent plans that Shear has filed with the NWB have already changed the January 31, 2010 workplan. Since filing the original workplan, Shear has been collecting and analyzing data (geological, environmental and economic), observing conditions on site, and identifying and addressing deficiencies. Where plans had not been filed by previous owners in compliance with the Type A Water Licence, Shear developed plans and has either filed them or will be doing so in the near future. Further details were presented at the technical meeting that was held June 20, 2011. Because of the dynamic nature of the process in which we have been engaged, and the results of our analysis, there is the potential to initiate ore processing as early as the late summer to fall of 2011. For example, on February 8, 2011 Shear announced new audit results on stockpiled kimberlite and subsequently, on May 31, 2011 announced the plan to accelerate the processing of such material for diamonds. On June 6, 2011 Shear informed the NWB of our intent to initiate process evaluation in accordance with our Type A Water Licence 2AM-JER0410.

It is essential that Shear be issued a full renewed Type A Water Licence that enables it to re-commence full scale mining in addition to support current ongoing activities at site (that include current plant processing at site) at a time when Shear is ready (or Shear's choosing).

Secondly, your letter states: **"Shear has noted in their application and supporting materials their knowledge of the site conditions is incomplete, and plans submitted in support of the water licence renewal application are interim until more complete information is obtained. The plans are thus tentative and lack the detail required to conduct a meaningful technical evaluation."**

As noted, Shear has openly acknowledged that the legacy information from the previous operator and overseers is limited. A number of the plans required under the water licence had not been filed and/or approved for a variety of reasons. After determining the status of various plans, Shear developed and submitted 18 plans to the NWB. In developing those plans, Shear reviewed the previous submissions by Tahera and the comments on the public registry. Shear also included best industry standards and applicable legislation requirements and guidelines wherever possible. For the most part these plans are NOT interim in nature and Shear has received commendation from other federal departments (Environment Canada and Department of Fisheries and Oceans) for their thoroughness and practicality. To quote Environment Canada's submission dated June 10, 2011 to the NWB in respect to Shear's Type A water licence renewal: *"Overall, EC was pleased with the detail and clarity presented in the submissions, and would like to commend the proponent for a thorough submission....."*

Shear is currently operating under the terms and conditions of Type A Water Licence 2AM-JER0410. Upon assuming ownership of the Jericho Diamond Mine assets in late August 2010, Shear conducted a compliance audit for the Jericho Mine and provided the report of the assessment to the NWB in November 2010 at the same time as Shear filed an application to assign the Water Licence and a 60 day extension to the term of the licence. On January 31, 2011 Shear applied for an emergency amendment to the term of the Water Licence until March 1, 2012. In support of this application Shear submitted a Care & Maintenance plan in accordance with Schedule J (2A) of the existing Jericho Water Licence.

The full Type A licence renewal application package with all associated plans was filed by February 28, 2011 including those remaining supporting plans that had been identified as being required in the compliance report.

A number of plans in any mining operation are of necessity interim in nature. For example, an Interim Closure and Reclamation plan is finite and known - until the end of the mine life at which time a company files a Proposed Final Closure & Reclamation Plan. We recognize that the Jericho Water Licence Part M (5) states that at the time of licence renewal a Proposed Final Closure & Reclamation Plan would be submitted. Recognizing that the mine had operated for less than two years of its eight year Water Licence, a Proposed Final Closure & Reclamation Plan would provide no more detail at this point than the Interim plan submitted by Shear, because the information required by Schedule M (2) is not available until later in the life of the mine. We firmly believe that the level of detail provided in the plans submitted by Shear in conjunction with all prior project plans filed with the NWB, enable reviewers to conduct a meaningful technical review for the purpose of licence renewal.

Thirdly, your letter states: **"It appears that several key plans and designs (including, but not limited to, Aquatic Effects Monitoring Plan for Operations, updated Mine Plan, Processed Kimberlite Containment Area Management Plan, Landfill Management and Design Plans, Facility Operation and Maintenance Plans, Abandonment and Restoration Plan) will not be adequately developed in advance of the planned hearing."**

Shear strongly disagrees with this statement. With the purchase of the Jericho Mine and the subsequent assignment of the existing Type A Water Licence, Shear assumed not only the responsibility for all previously approved plans but also the authority to implement them. In the Shear Type A Water Licence renewal application, Shear submitted additional plans and intends to augment those plans as required. All other approved plans remain in place including, but not limited to, the 2005 Mine Plan, design plans, facility operation and maintenance plans.

One issue that may have caused confusion is in relation to the Care and Maintenance Plan. Neither Tahera nor its successor filed one with the NWB. A Contingency Management Plan was filed by Tahera after suspension of production but this lacked the detail on how the Mine would be operated under care and maintenance. In accordance with Schedule J, 2a of the current Type A Water Licence, Shear submitted a Care and Maintenance Plan that addressed activities that have been required at site since June 2008. As part of this Care and Maintenance Plan Shear determined that the following plans were required:

- Aquatic Effects Monitoring Plan,
- Site Water Management Plan,
- General Monitoring Plan and
- Processed Kimberlite Management Plan.

Each of these plans, with the exception of the Processed Kimberlite Management Plan (PKCA), describes conditions during care and maintenance as well as the transition to production. Although the 2006 PKCA Management Plan that Tahera submitted adequately describes the management of the PKCA, Shear will update it for Operations and submit it prior to the public hearing. Since no Operations, Maintenance and

Surveillance Manual for the PKCA Dams had been approved, Shear submitted this with the Water Licence renewal application.

Lastly, AANDC has recommended that **“any renewed licence permit only those activities for which Shear plans to undertake within the next 18-24 months and which are supported by well-developed operational plans. We would then anticipate that further development in the project would be authorized through an amendment of the licence.”**

Shear is applying for a licence that includes the full range of activities that would allow Shear to continue with operations and re-open the Mine. The Mine has been constructed and was operated for almost two years. Shear has pro-actively, thoroughly and within the timetable set by all concerned parties, undertaken steps to bring the Mine back into compliance so it can recommence production and operations as soon as possible. Shear is building on what is in place now and is rectifying or improving the compliance status of the Jericho Mine site based on what we have found. We believe the Mine can be a profitable operation that will make a positive contribution to the northern economy. Shear also believes that there are practical solutions to overcome unnecessary impediments to operationalizing this modest but important resource for the people of the north.

In summary, Shear has been working diligently to bring the Jericho Diamond Mine into compliance with its historic regulatory licences and is applying to the NWB for renewal of the Mine's current Type A Water Licence which will provide Shear with the flexibility that we believed, at the time of purchase, we would have to resume full scale mining operations as soon as we have determined economic feasibility, a process that is actively and currently underway.

In conformity with the deadlines set by the NWB, we will be addressing the issues that were identified in the public pre-hearing technical meetings in June and confirmed by the NWB in their July 4, 2011 decision document as being the only issues outstanding which Shear needs to address. We trust that if AANDC has any additional issues specific to the full renewal of our licence, AANDC will clearly articulate this well in advance of the public hearings scheduled for October 13-14, 2011 in Kugluktuk.

Sincerely,



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



Julie Lassonde
Executive Chairman & CEO

CC:

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