

TYPE A WATER LICENSE
2AM-JER1119
Jericho Diamond Mine

QUARTERLY REPORT

For the Quarter Ending: February 29, 2012



shear
diamonds

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1 INTRODUCTION

This Quarterly Report has been prepared in accordance with Part B, Item 3 of the Type A Water License 2AM-JER1119, issued by the Nunavut Water Board (NWB) on February 7, 2012 to Shear Diamonds (Nunavut) Corp., a wholly owned subsidiary of Shear Diamonds Ltd.

The Quarter being reported on is for the three months ended February 29, 2012. Financial statements for this quarter will be provided on May 31, 2012, which is in line with the filing requirements of the securities exchange that the Company reports under.

2 UPDATE OF COMPLIANCE STATUS WITH THE LICENCE

On November 16, 2010, Shear submitted an assignment application to the NWB. In support of the application, Shear completed and provided a compliance assessment of the Type A Water Licence, 2 AM-JER0410.

The compliance assessment revealed that a number of plans were never approved by the NWB. In preparation for the water licence renewal application Shear reviewed the plans and the comments provided by interveners and reviewers. Shear submitted a number of plans in support of the water licence renewal application. These plans incorporated the comments from the interveners and reviewers.

Shear personnel discovered a number of physical non-compliances and historical issues while on site in 2011. Shear is working diligently to address these non-compliances.

During the quarter being reported, Shear conducted weekly internal inspections at site. The internal inspection forms are discussed with the Site Manager and action items are developed where needed. The internal inspection form is being updated for the next quarter to follow the same format as those used by the Water Resource and Lands Officers during their inspections. Shear will use the internal inspection form to self-report to the Inspectors.

Spills

During the quarter being reported three (3) spills were reported, for a total volume of 5 litres of diesel and 1.5 litres of oil. These spills were cleaned up. Contaminated snow was placed inside the Phase I Fuel Farm containment berm. Contaminated spill pads were placed in an empty drum and covered. The spill report numbers are:

- 12-015
- 12-039
- 12-050

The Spill Report Forms submitted to the 24-hour Spill Line can be found in Appendix A.

Monthly Reports

Monthly reports were filed on time for each of the months being reported on for this quarter. The monthly report format is being updated for the next quarter to reflect some of the changes in the new water licence, issued on February 7, 2012.

3 UPDATE DESCRIBING ANY PROPOSED CHANGES TO ANY PLANS

The public hearing was held on November 30 and December 1, 2011 in Kugluktuk. During the public hearing, and in response to the questions raised by interveners and in written submissions, Shear made a number of commitments with regard to revising and updating plans to reflect the comments received.

During the quarter being reported, there were no submissions of any revised plans.

In the upcoming quarter Shear will be filing the following:

- QA/QC Plan – April 30, 2011
- Technical Memo: Revised Pit Infill Rates – April 15, 2011
- Status Update and Clarification of the Aquatic Effects Monitoring Plan – April 1, 2012

4 UPDATE WITH RESPECT TO CONSTRUCTION AND PRODUCTION SCHEDULE

- Processing from stockpiles expected to begin in April 2012.
- There are no construction plans for either the second or third quarter 2012.
- Shear plans to re-start commercial production late 2013. Plans for construction and production schedule to be updated quarterly.

5 CORRESPONDENCE WITHIN THE QUARTER WITH REGULATORY AUTHORITIES

The following summarizes the correspondence with regulatory authorities for the quarter being reported.

December 2011

- December 1, 2011. Public Hearing, Kugluktuk.
- December 21, 2011 – Positive recommendation from the NWB to AANDC regarding water license

January 2012

- Jan 4, 2012 – Shear Legal counsel discussion with KIA legal counsel regarding final documents with respect to water compensation.
- Jan 6, 2012 – email with Andrew Keim (AANDC)
- January 9, 2012 – Payment of water use fees for the Jericho Project to the NWB
- Jan 11, 2012 – email with Dionne Filitrault (NWB)
- Jan 14, 2012 – email with Andrew Keim (AANDC)
- Jan 16, 2012 – email with Tanya Trenholm (AANDC)
- Jan 24, 2012 – email with Mohan Denetto (AANDC)
- Jan 24, 2012 - Meeting with the KIA during Round-Up Conference in Vancouver
- Meeting with AANDC,

February 2012

- February 13, 2012 – Approval of Type A water license received from AANDC that took effect on February 7, 2012
- February 13, 2012 – email with Mohan Denetto (AANDC)
- February 17, 2012 – email from Gilles Binda (AANDC)
- February 24, 2012 – email with Mohan Denetto (AANDC)
- February 28, 2012 – email with Dionne Filitrault (NWB)
- February 29, 2012 – email with Dionne Filitrault (NWB)
- February 27, 2012 – email from Geoff Clarke regarding effective date of the water license