



Aboriginal Affairs and Northern Development Canada  
Nunavut Regional Office  
Resource Management Directorate  
P.O. Box 100  
IQALUIT, NU X0A 0H0

August 24, 2012

Our reference:  
IQALUIT-#567804

Ms. Julie Lassonde  
Chief Executive Officer  
Shear Diamonds (Nunavut) Inc.  
6 Adelaide Street East, Suite 220  
Toronto, ON M5C 1H6

*Sent via email*

**RE: Status of Security for Type “A” Water Licence 2AM-JER1119**

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Dear Ms. Lassonde:

In follow-up to my letter of July 30, 2012 and subsequent discussions between Shear Diamonds (Nunavut) Inc. (Shear) and Aboriginal Affairs and Northern Development Canada (AANDC) on August 9, August 17, and August 22, 2012, I wish to clarify the status of security required for the Jericho Mine water licence 2AM-JER1119.

Water licence 2AM-JER1119 for the Jericho Mine came into effect on February 7, 2012, with a requirement, supported by Section 76 (1) of the *Nunavut Waters and Nunavut Surface Rights Tribunal Act*, for Shear to provide an additional \$1,189,074 in water licence security. The security was due in full on March 8, 2012. Security for water licences in Nunavut must be provided to the Manager Water Resources in the Nunavut regional office of AANDC in a form specified under Section 12 (3) of the *Northwest Territories Waters Regulations*, or in a form deemed satisfactory to the Minister of AANDC.

Shear issued a proposal to AANDC on March 6, 2012, to provide the additional security in two parts, first a reallocation of \$800,000 in letters of credit held under a related and expired water licence, and second, a “secured promissory note substantially in the form previously provided to AANDC” for the remaining security. An additional \$68,000 cash security is also held by AANDC for the expired licence. AANDC agreed to allow time for Shear to arrange reallocation of the \$800,000 in letters of credit from the expired licence, a process that required a site inspection in snow-free conditions to provide due diligence that there were no outstanding liabilities associated with the expired licence. A site inspection was conducted by AANDC on July 4 and 5, 2012, and debris was subsequently removed from the site by Shear on July 19, 2012. Shear provided photos demonstrating that the site was clear on July 24, 2012 and AANDC confirmed by email on the same day that there were no liabilities associated with the expired licence.

Conditions for acceptance of a promissory note for the remaining \$321,074 in security required under the water licence, including a schedule for replacing the promissory note with cash-equivalent security, were provided to Shear in my letter of July 30, 2012. Further to subsequent discussions, AANDC proposed an alternate schedule of payments. Instead of a schedule of

equal payments, AANDC would accept payments equivalent to 10% of the AANDC evaluation to be made following each diamond parcel production at the mine occurring after the July 30, 2012 letter. In any case the full security requirement of the licence must be provided in the form of cash or equivalent before active mining resumes. No other forms of security have been identified as satisfactory to the Minister. To clarify, the full amount of security identified in the water licence must be provided to AANDC, either in a form prescribed in the regulations, or in this case, AANDC would allow that a portion up to \$321,074 may be provided through a secured promissory note under the conditions and schedule described in my letter of July 30, 2012, or under the alternate schedule described here.

In the conference call between AANDC and Shear on August 22, 2012, Shear indicated that the company would expedite the reallocation of the \$800,000 in letters of credit and would reallocate the \$68,000 cash attached to the expired licence, but that the company could not provide any assurance of when the remaining \$321,074 could be paid in cash or equivalent security. Shear indicated that the company had no further questions about the form of security that would be satisfactory to AANDC.

I must advise you that the full amount of security is currently due. The security must be provided in a form prescribed by the regulations with the exception in this case that up to \$321,074 may be provided in a form indicated in this letter. Shear is asked to complete the reallocation of letters of credit by August 31, 2012, and provide the remaining \$321,074 outstanding security within 30 days of the issuance of this letter.

Sincerely,



Murray Ball  
Manager Water Resources  
Nunavut Regional Office  
Aboriginal Affairs and Northern Development  
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Cc:

Phyllis Beaulieu,	Manager of Licensing, Nunavut Water Board
Andrew Keim,	A/Manager of Field Operations, AANDC