

**A STRATEGY TO ENSURE THE LONG-TERM
COMPETITIVENESS OF THE CANADIAN MINERAL INDUSTRY**

Submission by the
Prospectors and Developers Association of Canada
on behalf of the Canadian mineral exploration industry
to the
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EXECUTIVE SUMMARY

This submission, presented by the Prospectors and Developers Association of Canada to the 2006 Mines Ministers' Conference, contains three sections. The first examines the current state of the mineral exploration industry. The second reiterates the case, proposed in 2005, for Canada to adopt a long-term mineral exploration strategy that will assure Canada's competitiveness now and into the future, and the third discusses additional issues of strategic importance that, without resolution, will negatively affect this country's mineral exploration sector going forward.

CURRENT STATE OF THE INDUSTRY

Canada is one of the world's principal destinations for mineral exploration investment and a dominant player in the global exploration industry in terms of activity and as a source of funds for exploration. High global demand and consequent high commodity prices have spurred mineral exploration activity in Canada and abroad. Exploration expenditures in Canada are expected to increase to \$1.4 billion in 2006. World exploration spending has also increased, reaching \$US 5.1 billion in 2005, of which Canada attracted 19%. Junior companies (small and medium enterprises) accounted for 62% of total exploration spending in Canada in 2005. Since October 2000, when the federal exploration tax credit was implemented, close to \$1.9 billion has been raised by companies issuing flow-through shares for exploration in Canada. In 2004 \$11.4 billion, or 48% of total global equity financing, was raised on Canadian markets for exploration and development. Canadian companies are financing 7,895 exploration projects, 4,385 of which are in Canada and 3,510 abroad.

THE CASE FOR CANADA TO ADOPT A LONG-TERM MINERAL EXPLORATION STRATEGY

Because of this country's rich endowment of natural resources and high mineral potential, Canada is in an excellent position to supply much of the global demand for commodities. This, together with a vibrant junior exploration sector, represents an excellent economic and social opportunity for Canada. Among the principal challenges that could potentially compromise Canada's ability to benefit from these opportunities are: the levels of this country's mineral reserves which are being depleted faster than new discoveries are being made; intense global competition for exploration investment; and the cyclical nature of the mineral industry. To overcome these challenges, Canada must institute a long-term strategy that will: assure high levels of investment in grassroots exploration over an extended period; further the potential for discovering mines in Canada; enable Canada to replenish its reserves; maintain its competitive position in mineral exploration; and retain this country's foremost position in global exploration and mining expertise. The strategy proposed contains two major elements: a) investment in geoscience; and b) exploration incentives.

1. Investment in geoscience

Recommendation 1: That the federal government fund the Cooperative Geological Mapping Strategies (CGMS) without delay.

The Cooperative Geological Mapping Strategies (CGMS) is a plan developed by the federal, provincial and territorial governments to improve Canada's geoscience knowledge base, i.e., geological data and maps. A ten-year commitment of \$25 million annually by the federal government would trigger matching contributions from provincial and territorial

governments. The total investment would be \$50 million per year for ten years. Once implemented, the CGMS will generate new or updated geological information, particularly in the North, where the potential for new mineral discoveries is high.

2. Investment in exploration incentives

Recommendation 2: That the federal government establish the Mineral Exploration Tax Credit in a series of rolling three-year phases, supplemented with annual reviews of the program's benefits.

The Mineral Exploration Tax Credit or "super" flow-through program will be expiring in March 2007. This tax credit, which has been in place for most of the time since October 2000, is credited with increasing exploration investment in Canada. Because of its focus on grassroots exploration, the program has also made a significant contribution to new mineral discoveries in Canada, from a low of 15 in 1999 to a high of 268 in 2005. While the program was originally introduced to stimulate exploration in Canada during a period of very low investment, it is now needed to maintain Canada's competitiveness in a period of fierce global competition for exploration investment.

Recommendation 3: That the federal government, as part of a long-term strategy for mineral exploration, clarify, by legislative amendment if necessary, that Canadian Exploration Expense includes the costs of community consultations, environmental baseline studies and feasibility studies.

Currently, the costs of community consultations (including those consultations with aboriginal communities), baseline environmental studies, and feasibility studies do not qualify for Canadian Exploration Expense, even though such activities are recognized as good business practices and are recommended or required by governments in Canada as a pre-condition to permit approval. The costs of consultation, particularly in the North, can be very high. Junior companies undertaking these activities must pay for them with funds raised by means other than flow-through shares, and for many this imposes an onerous and unnecessary financial burden.

Recommendation 4: That exploration for base metals in the vicinity of existing and formerly operating mines be treated as Canadian Exploration Expense.

Canada's need to replenish its base metal reserves requires special measures to encourage companies to search for base metal deposits. The treatment of base metal exploration costs in the vicinity of former producing or operating mines (areas of known prospectivity) as CEE will give impetus to junior exploration and senior producing companies, financed through flow-through shares, to explore in those areas.

Recommendation 5: That the federal government modify the Income Tax Act so that a resource property on the site of a former mine that has been shut down or inactive for a continuous period of at least 60 months is deemed to be a "new mine."

Mines that have been shut down in the past often become exploration targets today. There is confusion as to whether this kind of exploration qualifies for CEE. If the property is deemed a "new mine," then it does. The *Income Tax Act* does not define "new mine." By modifying the *Income Tax Act* to define a resource property on the site of a former producing mine that has been shut down or inactive for a continuous period of at least 60 months as a "new mine" would clarify this situation and would enable companies to categorize exploration and development expenditures in the assessment and development of a property correctly and assist in raising the required financing. The modification would also encourage exploration around former mines.

Recommendation 6: That the federal government implement a 20% deep drilling tax credit to encourage exploration below 300 metres, to discover deep ore deposits and extend the reserve life of existing mines.

The PDAC continues to support the Mining Association of Canada's recommendation for a 20% deep drilling investment tax credit for exploratory drilling below 300 metres. The tax credit would encourage companies to make the large investments necessary to search for deeper mineral deposits and to replenish reserves.

SUSTAINING THE MINERAL EXPLORATION INDUSTRY IN CANADA

1. The mineral industry and Canada's aboriginal peoples

Mineral exploration and new mines, particularly in the North, offer great potential for the creation of wealth and prosperity for aboriginal communities. While there are a number of current initiatives designed to inform aboriginal communities about the mineral industry, governments can contribute by taking the lead in the continuing development of the aboriginal workforce and by improving access to essential skills and industry training for aboriginal peoples.

Impact Benefit Agreements (IBAs) are negotiated between specific communities and companies. However, some jurisdictions are ensuring that a broader range of communities benefit from the resource sector through revenue sharing agreements. The result is a greater degree of certainty and cooperation among all affected parties and support for mineral development within the region.

The PDAC supports aboriginal peoples and governments in their efforts to speed up the land claim resolution process. Communities and companies are doing their best to accommodate one another, but governments in Canada must act expeditiously to resolve land jurisdictional issues and must provide direction on consultation in order to clarify the approval process and help reduce the potential for disputes.

2. Northern issues

Canada's North is very important in the search for new mineral deposits. However, the complexity of much of the North's policy and regulatory regime is having a negative impact on the region's investment climate. Economic development ranks lower in importance than aboriginal and environmental affairs for Indian and Northern Affairs Canada (INAC). This issue of balance should be addressed by a re-activated Northern Mines Ministers Conference.

Improvements to the NWT regulatory system must be a top priority. INAC's actions concerning prospecting permits in the NWT during its negotiations with First Nations contravened the Canada Mining Regulations. Industry calls for more effective management of land claim negotiations and a more open, transparent, and inclusive process that takes industry's needs into consideration.

3. Improving Canada's system for mobility of professional geoscientists

Canada's current system for mobility of professional practice among provinces and territories is not satisfactory. Bureaucratic procedures and costs are deterring many geoscientists from joining the professional associations, leading to low compliance with existing systems and compromising the ability of the Self Regulatory Organizations to maintain standards and protect the public interest. The PDAC is working with others towards an internationally recognized, Canada-wide approach to professional practice

that would, ideally, comprise a Canada-wide system of registration that is provincially/territorially administered. To this end, the association calls on all governments to work collaboratively in the harmonization of the necessary statutes and regulations.

4. Streamlining Fisheries and Oceans Canada's procedures

The interpretation of legislation by Fisheries and Oceans Canada (DFO) has sometimes caused delays to mineral exploration projects. A resource industry group is working with DFO to generate a list of low impact work practices that will not require a specific DFO permit. A compilation of exploration best practices will assure those companies in compliance with a timely and streamlined permitting process.

5. Ensuring an adequate labour force for the mineral industry

The PDAC is in the preliminary planning stages for a strategy to address the labour requirements of the mineral exploration sector. The strategy's aims are: a) to create awareness of the kinds of employment opportunities that the mineral industry offers; b) to attract young people to careers in prospecting, geosciences, mineral deposits geology, and the exploration business; and c) to ensure that those who have already chosen to work in mineral exploration receive adequate education and training.

6. Improving Canada's securities regulatory system

The agreement by most Canadian jurisdictions to adopt the "passport" system is a step towards streamlining this country's securities regulatory system. However, the PDAC believes that Canadians would benefit most from a securities regulatory system featuring a single securities regulator, a common body of securities law and a single fee structure.

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A STRATEGY TO ENSURE THE LONG-TERM COMPETITIVENESS OF THE CANADIAN MINERAL INDUSTRY

INTRODUCTION

This submission is presented by the Prospectors and Developers Association of Canada on behalf of Canada's mineral exploration industry. Its contents have been developed in collaboration with members of the Canadian Mineral Industry Federation.

The PDAC is a national organization with 6,000 members representing the range of companies and individuals in mineral exploration. Our corporate members include senior producing companies and junior companies (small and medium enterprises [SMEs]). Our individual members include prospectors, geoscientists, geological consultants, company executives, and junior exploration and senior mining companies. Our members also include people in the financial, legal, and academic communities, students, and those who supply services and equipment to the mineral industry.

The PDAC values this opportunity to meet with Canada's mines ministers and to bring to this forum the views of our industry. The meeting in 2005 proved to be especially valuable. Mines ministers unanimously endorsed a strategy proposed by the PDAC and aimed at increasing the level of exploration activity in this country. This consensus was translated, following their meeting, into a letter signed by all mines ministers and sent to the federal finance minister urging him to take action on the strategy.

The industry very much appreciated this action by its mines ministers and commends them for it. We look to this country's top policy and decision makers to create partnerships between government and industry, and the level of agreement reached last year was evidence of a healthy partnership.

The theme of our presentation this year, *A strategy to ensure the long-term competitiveness of the Canadian mineral industry*, very directly addresses the topic for this year's stakeholder presentation during the open session: *Securing competitiveness in Canada's minerals and metals sector: Framework for partnership*.

Our primary objective this year is to emphasize the strategy that was presented and agreed to last year but has yet to be implemented. Our submission is divided into three sections. The first examines the current state of the industry. The second reiterates the case, proposed in 2005, for Canada to adopt a long-term mineral exploration strategy that will assure Canada's competitiveness now and into the future. In this section, we identify the key components of the strategy, focusing on two principal areas: investment in geoscience and incentives for grassroots exploration. The third and final section focuses on additional issues of strategic importance that, without resolution, will have a negative impact on this country's mineral exploration sector going forward. Where applicable, we report on measures that are being taken to resolve them.

CURRENT STATE OF THE INDUSTRY

Canada is one of the world's key destinations for mineral exploration

The mineral exploration industry has experienced a remarkable resurgence over the past four years. High commodity prices, fuelled by global demand, have in turn spurred mineral exploration activity in Canada and abroad. Natural Resources Canada's data show that projected exploration expenditures in this country will reach \$1.4 billion, up from \$1.3 billion in 2005, \$1.1 billion in 2004, and a significant increase from 1999 when expenditures totaled \$504.35 million. Metals Economics Group reports that global exploration spending in 2005 reached \$US 5.1 billion, up by 34% from 2004.

These current levels of exploration expenditures in Canada represent a very significant proportion of the global pool of exploration spending. According to Metals Economics Group (MEG), Canada attracted 19% of total world exploration expenditures in 2005. In comparison, our closest competitors, Australia and the USA, attracted 13% and 8% respectively of the world's exploration spending during the same year.

Exploration expenditures by junior companies surpassed that of senior companies for the first time in 2004 and rose to an estimated 62% of total exploration spending in Canada in 2005.

The principal focus of junior companies is exploration. Less commonly do they operate mines, and, as a consequence, they have no revenue from production. They must rely on the capital markets or private investment to fund their exploration. Since October 2000, Canadian junior companies have had the benefit of a federal tax credit for exploration or "super" flow-through, a program introduced by Canada's federal government to help the industry withstand the effects of a severe global downturn in the mineral industry. This program allows investors a 15% tax credit on their flow-through share investments in companies engaged in grassroots mineral exploration in Canada. The program has encouraged a steady flow of capital for junior companies exploring in this country. Natural Resources Canada (NRCan) estimates that from October 2000 to March 2006, companies raising capital for exploration in Canada through the issuance of flow-through shares raised close to \$1.9 billion.

Canada is a dominant player in global mineral exploration

Canada also continues to play a dominant role in the global mineral exploration industry both in terms of exploration activity and as the source of funds for this exploration activity. In 2004 \$11.4 billion in equity financing was raised on Canadian markets for exploration and development. This represents 48% of total equity financing raised globally. In comparison, Australia raised 15%; the United Kingdom 11%; and South Africa 10%.

Of the 1,440 companies with exploration budgets exceeding \$US100,000 that are tracked by Metals Economics Group, 888 or 62% are Canadian, 24% are Australian, 5% are U.S. companies, and 4% are based in the United Kingdom.

NRCan's 2005 statistics show that Canadian companies are financing a total of 7,895 exploration projects worldwide. Of these 4,385 are in Canada and 3,510 in the rest of the world.

THE CASE FOR CANADA TO ADOPT A LONG-TERM MINERAL EXPLORATION STRATEGY

A. The opportunities and challenges facing Canada's mineral industry

The data above demonstrate that Canada continues to be a leader in global mineral exploration. We also show that this country continues to be a principal destination for mineral exploration in the world, and that exploration expenditures in this country increased to \$1.3 billion in 2005.

This is good news and the recovery of the industry is welcome. It follows one of the bleakest downturns that the industry has ever experienced. At its lowest point during the period 1997 to 2001, exploration expenditures in Canada dropped to \$504.4 million, and worldwide expenditures on exploration plummeted from a high of \$6.6 billion in 1997 to an all-time low of \$2.5 billion in 2002. As a consequence, exploration activity, particularly grassroots exploration, dropped in Canada and there was a dearth in the number of new discoveries of mineral deposits in this country.

In our brief to mines ministers in 2005 we pointed out the opportunities and challenges for Canada and for this country's mineral industry. In the brief, we outlined the *opportunities* as follows:

- **Canada's ability to supply much of the global demand for commodities**
There is today an almost unprecedented demand for mineral commodities from the world's emerging economies, particularly those of China, India and Brazil. This demand, largely for copper, lead, zinc, nickel, and uranium, but also for coal, iron ore, molybdenum, titanium, platinum and palladium, is expected to continue long into the future. Because of our rich endowment of natural resources and mineral potential, supplying much of this demand represents an excellent economic and social opportunity for Canada.
- **Canada's vibrant junior exploration sector**
This country's junior exploration sector has evolved as the primary player in the Canadian and world exploration business. In 2005, junior company spending on exploration in Canada overtook that of senior companies, accounting for 62% of the total in this country and 30% of that of the world. There is evidence also that junior companies have shifted their focus away from precious metal targets to base metals, given the strong demand for base metals and continuing strength in commodity prices.

The *challenges* are as follows:

- **Steep decline in this country's mineral reserves**
In order for Canada to benefit from the strong demand for mineral commodities, this country's inventories of key commodities, particularly base metals, e.g., nickel, zinc, copper, and iron, must be sufficient to meet the demand (the mineral reserves or inventories in a country are judged to be those known mineral deposits or parts of the deposits that have a reasonable prospect for economic extraction). Unfortunately, this is not the case. NRCan's data show a steep decline in proven and probable base metal reserves over the past quarter century. New mineral deposits are the *only* way in which inventories can be restored to adequate levels.

In spite of the recovery of the industry and increased levels of investment over the past four years, commodity experts are unanimous in their conclusion that existing reserves of many commodities cannot supply the anticipated demand. Exacerbating this situation was the severe downturn in the industry from 1997 to 2002 as mentioned above. This took a heavy toll on the exploration industry, and the consequent low levels of exploration activity and investment resulted in fewer new discoveries in the pipeline.

Canada's base metal reserves are depleting faster than new discoveries are being made, reinforcing a need for long-term and higher levels of investment in exploration to fuel new discoveries. Given that only one in a thousand discoveries will become a mine and that one discovery typically takes ten years before reaching commercial production, sustained and prolonged investment in grassroots exploration and development today is critical for a sustainable future over the long term.

- **The negative effects for Canada of declining reserves**
The decline in Canada's reserves presents its own set of challenges, above and beyond compromising this country's future ability to take full advantage of the global commodity demand. These include the potential closure of smelters and refineries, lost employment opportunities, and serious economic hardship for those communities that rely on mining for their wellbeing.
- **The intense global competition for exploration investment**
Exploration by its very nature is competitive. Junior exploration companies compete for investor interest and funding on the capital markets, and, because of the high risk nature of exploration, will look for projects with the most potential. At the same time, countries compete for exploration investment. At the PDAC's 2006 convention, for example, an estimated 100 countries were represented. Of these, 70 governments sent official delegations or had a significant presence in the trade show. All were promoting the mineral potential of their respective countries and were looking to attract exploration companies and exploration investment to their respective jurisdictions.
- **Other challenges to exploration in Canada**
Other challenges that act as impediments or barriers to exploration investment in Canada include: lack of infrastructure, particularly in the North; extreme variations in temperature and climate rendering exploration seasons short; extensive land mass with remote regions and isolated communities; a complex regulatory regime; uncertainty of mineral title, in many cases due to unresolved land claims; and inaccessibility to prospective land because of land-use restrictions.
- **Cyclical nature of the mineral industry**
The cyclical nature of the mineral industry is well known; the peaks and troughs that are characteristic of this cyclicity can have profound and longstanding effects. In downturns, such as we saw from 1997 to 2001, mineral exploration activity in Canada and abroad went into a free fall. Junior exploration companies were finding it exceedingly difficult to raise capital, many rejecting mineral exploration and turning their attention to the burgeoning high-tech industry. This had negative consequences for exploration activity, particularly grassroots exploration, and led to a dearth in the number of new discoveries, a situation with which we are still grappling in 2006.

Other consequences of downturns include: loss of jobs; a decline in employment opportunities making the industry an unattractive career choice; a decline in business for suppliers of services and equipment; and negative effects on the economies of local communities, particularly those in northern or rural regions.

To face and overcome the challenges that we have identified and to be in a position to benefit from the economic opportunities that the world is presenting, we believe that Canada must be willing to institute a solid, long-term strategy that will: assure high levels of investment in grassroots exploration over an extended period; further the potential for discovering mines in Canada; enable Canada to replenish its reserves; maintain its competitive position in mineral exploration; and keep this country at the forefront as an industry leader providing global exploration and mining expertise.

B. Key components of a long-term strategy for Canada's mineral exploration sector

As we discussed at the beginning of this submission, the strategy presented at the 2005 Mines Ministers Conference was unanimously supported by all mines ministers and a letter signed by all mines ministers was sent to the federal Minister of Finance endorsing its adoption. The elements of this strategy require budgetary commitments from both the federal and provincial governments. Because of a change in government at the federal level, this commitment was not achieved. The reasons for the strategy, outlined above, still pertain. One year later we would say that there are even more pressing reasons for Canada to adopt the strategy.

For example, the Chinese economy is growing at a faster pace than ever, increasing in the first quarter of 2006 by 10.2 percent. According to Chinese officials, the country is now building up its stockpiles of minerals to help meet escalating demands and to provide a buffer against supply disruptions.

The Canadian strategy that we propose is two-pronged and focuses on two principal elements: 1) investment in **geoscience** which is critical to successful exploration and the discovery of new mines; and 2) **exploration incentives** that will help the junior exploration sector compete for investor interest, keep exploration investment in Canada and raise the potential for new mine discoveries in this country.

I. Investment in geoscience

Canada's geoscience knowledge base, the accumulation of geological data and maps for our country, is one of our most valuable competitive advantages. Among other benefits, it enables us to identify our mineral resources and assess our country's geological potential. It is particularly crucial at this time when our inventories are in decline and discoveries of new mineral deposits are needed to replenish them.

Six years ago, all of Canada's mines ministers, recognizing the deteriorating quality of our database and the benefits to be derived from investment in geoscience, approved the establishment of the Cooperative Geological Mapping Strategies (CGMS). The total investment by federal, provincial and territorial governments would be \$50 million per year for ten years. A federal government commitment to direct funds of \$25 million annually to the CGMS would trigger matching contributions for provincial and territorial governments.

The Cooperative Geological Mapping Strategies (CGMS), once implemented, would serve to provide new or updated geological information, particularly in the North. This is an exciting

and promising prospect. Canada has a vast land mass and there are large tracts of land, particularly in the northern reaches, that have never been adequately mapped. The highest potential for new discoveries is there.

The acquisition and publication of new geoscience data attract new exploration activity and company interest. The geoscience and exploration activity alone stimulates social, economic and fiscal returns. When a new mine is discovered, of course, the returns escalate by orders of magnitude.

Unfortunately, despite assurances to the contrary, no commitment has yet been forthcoming by the federal government to fund this important program.

The PDAC believes that funding the Cooperative Geological Mapping Strategies is an integral element of a long-term strategy for mineral exploration in Canada. Indeed, in our view, the implementation of the CGMS is now more pressing than ever, particularly in view of Canada's need for new discoveries and mines.

Recommendation 1: We strongly urge the federal government to fund the Cooperative Geological Mapping Strategies (CGMS) without delay.

2. Investment in exploration incentives

a) Federal tax credit for exploration

The Investment Tax Credit for Exploration, known familiarly as 'super' flow-through, was introduced in late 2000 by the federal government to revitalize the mineral industry in Canada. The program provides investors in companies exploring for minerals in Canada with a 15% tax credit on flow-through shares that they purchase. Since its inception, the program was extended twice before expiring at the end of 2005. In May 2006, the new federal government honoured its pre-election promise by bringing back the program as the Mineral Exploration Tax Credit and extending it to March 2007.

The action by the federal government in May gave rise to the re-instatement of a provincial tax credit by the Government of Manitoba. The provinces of British Columbia, Ontario, and Quebec elected to retain their provincial tax credit programs for exploration even when the federal program came to an end.

The PDAC regards this tax credit as fundamental to any strategy that aims to increase exploration activity in Canada. Funds raised by flow-through shares can only be spent in Canada, and, while the program was originally designed to shore up Canada's dwindling exploration levels, it is now credited with attracting additional exploration investment to Canada in the face of very significant competition offshore. This country's share of global funds available for mineral exploration climbed from 15% in 2000 to 19% in 2005. This is precisely what this country needs.

The tax credit, because of its focus on grassroots exploration, has also proven its worth in stimulating the discovery of new mineral reserves in Canada. A detailed analysis of exploration activity and results over the past nine years, recently conducted by the PDAC, reveals that the number of discoveries (see appendix A) has risen steadily from a low of 15 in 1999 to a high of 268 in 2005. Of the 268, 199 are significant extensions to previously known discoveries (expanding reserves of known occurrences and deposits is an essential part of the

exploration process leading to the development of new mines) and 69 are brand new. Our data also indicate that the majority of these discoveries involved flow-through share funding, so that much of this increase can be directly attributable to flow-through shares and in particular to the super flow-through share program focused on grassroots projects.

With its emphasis in Canada, the tax credit stimulated exploration activity, providing direct and indirect employment opportunities in this country and supporting the growth and development of many suppliers and service providers.

The program is ideally suited to address the need for maintaining a high level of exploration investment in Canada across a broad spectrum of commodities, including base metals. Significantly it is designed to focus on grassroots exploration (the earliest stage of exploration), when the investment risk is high and the difficulty in raising funds is greatest, even in the best of times. *It is grassroots exploration that is most needed at this time to maximize our effectiveness in making new discoveries.*

The exploration tax credit program was originally introduced to stimulate exploration in Canada during a period of very low investment. However, the program is now needed to maintain Canada's competitiveness in a period of fierce global competition for exploration investment.

The Mineral Exploration Tax Credit will be expiring at the end of March 2007. We believe that the program's expiry will immediately reduce Canada's ability to attract the high levels of exploration investment needed, particularly grassroots exploration, to make the discoveries of new mineral deposits that this country requires. Its expiry will also present a threat to Canada in the face of intense international competition for exploration dollars. We urge the federal government to maintain this important and strategic program as part of the long-term strategy for mineral exploration.

Recommendation 2: Specifically, we recommend that the federal government establish the Mineral Exploration Tax Credit in a series of rolling three-year phases, supplemented with annual reviews of the program's benefits.

b) Tax treatment of costs of community consultation, baseline environmental studies and feasibility studies

Junior mineral exploration companies fund much of their exploration activity through the issuance of flow-through shares. Investors in flow-through shares can deduct certain qualifying expenditures against personal income for tax purposes. Those exploration activities funded by flow-through shares must qualify for Canadian Exploration Expense (CEE) as defined under the *Income Tax Act*.

Currently, the costs of community consultations (including those consultations with aboriginal communities), baseline environmental studies, and feasibility studies do not qualify for CEE, even though such activities are recognized as good business practices and are recommended or required by governments in Canada as a pre-condition to permit approval.

The costs of community consultations are not associated with a company's *acquisition* of title to land to undertake exploration (which would disqualify their treatment as CEE). Rather, they are expenditures made to *assure access* to the land for the purpose of exploration.

To consult with people in the vicinity of an exploration project is a sound and wise business decision. An effective consultation process before and during an exploration project is more likely to win the cooperation of the local community and to assure the integrity of the project. Furthermore, local communities have come to expect to be consulted about mineral exploration activities close to their homes. Provincial governments are recommending that exploration companies consult with members of local communities at various stages of an exploration project, and Indian and Northern Affairs Canada has published guidelines for community consultations. At the same time, costs of consultation, particularly in the North, can be very high.

Similarly, the undertaking of environmental baseline studies (water and soil sampling during the course of an exploration project) is good business practice. Essentially, the company is monitoring and documenting whether or not its exploration project is having an impact on the natural environment.

Feasibility studies are an integral part of assessing the quality of a mineral deposit and, therefore, meet the definition of CEE. However, costs associated with these studies are not being treated as CEE.

Federal government officials continue to interpret these three sets of costs as not qualifying for CEE. As a consequence, a company undertaking these activities must pay for them with funds raised by means other than the issue of flow-through shares. For many junior exploration companies, this is difficult and imposes an onerous and unnecessary financial burden.

For several years now, the PDAC has requested that CEE be re-interpreted to include the costs of community consultations, baseline environmental, and feasibility studies. We believe that this action on the part of the federal government would bring CEE up-to-date, reconciling it with today's business practices and public priorities, and encourage companies to "do the right thing." We also believe that it belongs in a long-term strategy for mineral exploration in Canada.

Recommendation 3: We urge the federal government, as part of a long-term strategy for mineral exploration, to clarify, by legislative amendment if necessary, that Canadian Exploration Expense includes the costs of community consultations, environmental baseline studies and feasibility studies.

c) Tax treatment for base metal exploration in the vicinity of former producing or operating mines

Canada's need to replenish its base metal reserves requires special measures and a long-term strategy that will further motivate companies to search for base metal deposits. We believe that treating exploration for base metals in the vicinity of former producing or operating mines as CEE, rather than Canadian Development Expense, would encourage junior exploration and senior producing companies, financed through flow-through shares, to explore in areas of known prospectivity.

The discovery of new mineral deposits close to existing mines will provide new feed for local smelters and refineries and maintain jobs for communities across Canada.

Recommendation 4: The PDAC recommends that, to increase the potential for discoveries of new base metal deposits, exploration for base metals in the vicinity of existing and formerly operating mines be treated as Canadian Exploration Expense

d) Definition of a new mine for income tax purposes

Currently there is considerable confusion as to whether exploration around former producing mines is eligible for CEE treatment. The primary issue is whether the resource property constitutes a “new mine” for Canadian income tax purposes. If it is deemed a new mine, then the exploration activity qualifies for CEE. There is no definition of a “new mine” within the *Income Tax Act* and reliance has been placed on a jurisprudence dating back over 35 years to argue positions. Mines that have been shut down in the past because of a shortage of economic mineral reserves or because commodity prices make the mining operation uneconomic often become exploration targets for today’s junior exploration companies. These companies can use modern day technology to determine the economic promise of the properties.

A modification to the *Income Tax Act* that would deem a resource property on the site of a former producing mine that has been shut down or inactive for a continuous period of at least 60 months as a “new mine” would clarify this situation. The *Mining Tax Act (Ontario)* already contains this provision which is relevant for accessing certain incentives contained in that statute. The clarification that we propose would enable companies to categorize exploration and development expenditures in the assessment and development of a property correctly and assist in raising the required financing. The proposed measure would also encourage exploration around former mines, potentially leading to the re-opening of past producing mines which would have a positive impact on northern communities.

Recommendation 5: We encourage the federal government to modify the *Income Tax Act* so that a resource property on the site of a former mine that has been shut down or inactive for a continuous period of at least 60 months is deemed to be a “new mine.”

e) Deep drilling tax credit

The PDAC continues to support the Mining Association of Canada’s recommendation for a 20% deep drilling investment tax credit that would apply to any exploratory drilling below 300 metres. Such a tax credit would encourage companies to make the large investments necessary to search for deeper mineral deposits and to replenish reserves, particularly those of base metals and those in the vicinity of existing mines and communities.

Recommendation 6: As part of a long-term strategy for mineral exploration, the PDAC urges the implementation of a 20% deep drilling tax credit to encourage exploration below 300 metres, to discover deep ore reserves and extend reserve life around existing communities.

SUSTAINING THE MINERAL EXPLORATION INDUSTRY IN CANADA

We have set out the reasons for and principal components of a long-term strategy for Canada's mineral exploration sector. This we regard as fundamental to the industry's ongoing success and sustainability, assuring its ability and capacity to contribute to the economic wellbeing of Canada, its communities and its citizens and to enable Canada to continue to compete on the international stage.

The remainder of this submission highlights additional issues of strategic importance to the exploration sector and, where appropriate, the measures that are being taken to resolve them.

1. The mineral industry and Canada's aboriginal peoples

a) Exploration and mine development can help to sustain aboriginal communities

Mineral exploration and the development of new mines, particularly in the North, offer great potential for the creation of wealth and prosperity for aboriginal communities.

According to the Aboriginal Human Resource Development Council of Canada, aboriginal workers represent the fastest growing labour pool in Canada, and this country's aboriginal youth population is growing at a rapid rate. Many aboriginal communities face the challenge of overcoming the social consequences of chronic poverty and providing employment opportunities, education, training, housing, health and other public services. Research by NRCan indicates that there are approximately 1,200 aboriginal communities located within 200 kilometres of some 2,100 exploration properties across Canada. The mineral industry requires skilled workers and services (supplies, food, transportation etc.) to operate in remote areas, and these needs provide opportunities both for direct employment and for the development of aboriginal-owned service businesses.

There are a number of current initiatives designed to inform aboriginal communities about the mineral industry. Among them is a mining information kit for aboriginal communities which will be launched during the 2006 Mines Ministers Conference. The kit has been developed by the PDAC in partnership with NRCan, Indian Affairs and Northern Development, the Canadian Aboriginal Minerals Association, and the Mining Association of Canada and includes information on training, jobs and business opportunities.

Governments can also make a positive and lasting contribution by taking the lead in the continuing development of the aboriginal workforce and by improving access to essential skills and industry training for rural, remote and aboriginal communities.

b) Aboriginal engagement and economic development

There are a number of guidelines and tools that encourage industry members to engage aboriginal communities in consultation on land use and field practices as early as possible, and as often as practical, in the exploration process. Among them are the PDAC's e3 Environmental Excellence in Exploration and the Association for Mineral Exploration British Columbia's Mineral Exploration, Mining and Aboriginal Engagement Guidebook.

Many companies and communities also develop Impact and Benefits Agreements (IBAs) that recognize the interests of First Nations in their traditional territories and seek to involve those First Nations communities affected in project exploration, development and mine

operation. There are a number of examples. Nova Gold Canada Inc. and the Tahltan Nation have an agreement to explore and develop mineral resources in the Galore Creek Valley in northwestern British Columbia. The agreement provides for employment and business opportunities and sets out procedures to fully engage the Tahltan in all aspects of environmental protection.

While IBAs are relatively limited in scope because they are negotiated between specific communities and companies, some jurisdictions, both in Canada and internationally, are ensuring that a broader range of communities benefit from the resource sector through revenue sharing agreements. For example, in Quebec, La Paix des Braves (signed between the Cree Nation and the Government of Quebec in February 2002) serves to strengthen the political, economic, and social relations between Quebec and the Cree Nation through a defined revenue sharing formula. Mining royalties received by the Quebec government as mining taxes from operations in the territory defined by the agreement are shared with communities of the Cree Nation. Revenue from hydroelectric production and forestry is included in the agreement and a Cree Mineral Exploration Board assists with identifying and developing business opportunities. The result is a greater degree of certainty and cooperation among all affected parties and support for mineral development within the region.

The industry supports the principle of IBAs and revenue sharing agreements. However, there is the potential for confusion, delay and frustration when changes are being made to established resource management decision-making processes. Roles, procedures, timelines, and expectations must, where possible, be clearly defined to avoid uncertainty and conflict during the planning stage and once the agreements are in place.

c) Land jurisdictional issues and consultation

Long-standing unresolved land jurisdictional issues can bring companies and communities into conflict over land use. The PDAC supports First Nations and governments in their efforts to speed up the land claim resolution process. Other solutions to jurisdictional disputes include increased aboriginal business involvement in mining and resource revenue sharing, which has already been successfully implemented in a number of Canadian jurisdictions.

Recent Supreme Court decisions have emphasized that the consultation process requires good faith and reasonableness on the part of government and aboriginal peoples. The Court has further stated that, while governments can delegate some practical, on-the-ground aspects of consultation to third parties, for example to resource companies, governments cannot delegate the legal obligation of consultation. All parties involved in or affected by resource activities such as exploration, development and mining require clarity with respect to the requirements for consultation.

Communities and companies are doing their best to accommodate one another, and a number of governments, including Saskatchewan (May 2006) and Ontario (June 2006), have developed guidelines to be used by government officials in consultations with aboriginal peoples. However, governments in Canada must act expeditiously to resolve land jurisdictional issues and must provide direction on consultation in order to clarify the approval process and help reduce the potential for disputes.

2. Northern issues

Canada's North is very important in the search for new mineral deposits. This huge land mass is relatively unexplored and is highly prospective for many commodities, particularly base metals. The region, therefore, offers the greatest hope of Canada's ability to increase its mineral reserves and for its mineral industry to maintain its competitiveness.

Unfortunately, the complexity of much of the North's policy and regulatory regime has sullied the region's reputation as a destination for exploration investment. A special industry-government overview committee (IGOC) was established in 2001 to examine the regulatory regime of the North, including the Yukon and Northwest Territories and Nunavut, and to recommend improvements. More specifically the committee was charged with identifying ways in which the mandate of INAC could be re-balanced to recognize the importance of economic development in the North and to examine how the permitting and regulatory regime governing exploration and mining might be improved. The committee also worked with territorial governments to prepare a case for increased geoscience funding in northern Canada. This followed a Northern Mines Ministers Conference in April 2002 when Robert Nault, then Minister of Indian and Northern Affairs, requested that IGOC submit a proposal for bringing the geoscience databases of Canada's three territories up to the level of the provinces.

a) Balance between northern development, aboriginal affairs and environmental matters

Economic development continues to be the junior partner in INAC, and aboriginal and environmental affairs dominate the ministry's mandate. We recommend that this issue of balance be dealt with by the Northern Mines Ministers Conference and call upon INAC Minister James Prentice to re-activate this conference, committing to its being held within the next twelve months.

b) Regulatory and permitting issues

The NWT regulatory regime remains the largest source of frustration for IGOC industry members, particularly the management of the NWT boards and agencies. Although progress has been made with more financing for the boards, greater involvement by INAC, and the establishment of the board forum, we recommend that improvements to the NWT regulatory system be a top priority for INAC and that the ministry maintain its focus on the Auditor General's recommendations.

Prospecting permits

Difficult land claim negotiations with First Nations in the NWT led to a concession made by INAC that no prospecting permits would be issued in the First Nations' traditional territories without their prior consent. This contravened the Canada Mining Regulations. As a consequence, INAC informed four companies in 2005 that their permits would not be granted. Further problems arose with the Dehcho First Nation when prospecting permits were issued.

These kinds of incidents have a deleterious effect on exploration investment in the NWT. At risk is the free entry system, a hallmark of Canada's mining regulations. Industry is looking for more effective management of land claim negotiations, specifically a more open, transparent, and inclusive process that takes industry's needs into consideration.

3. Improving Canada's system for mobility of professional geoscientists

To work as a professional geoscientist in a Canadian province or territory, an individual must first meet that jurisdiction's requirements for registration as established by provincial / territorial legislation and administered by a Self Regulatory Organization (SRO). However, membership size, professional standards, financial resources and monitoring capacity of the SROs vary widely across jurisdictions and produce inconsistencies that pose risks to practitioners, regulators, and the general public.

The PDAC defines mobility of professional practice as the ability of geoscientists to work in any jurisdiction in Canada on the basis of their having registered in one Canadian jurisdiction. Our research and discussions with geoscientists indicate that Canada's current system for mobility among provinces and territories is far from satisfactory. Bureaucratic procedures and costs are deterring many geoscientists from joining the professional associations, and, while there is a high need for mobility, there is low compliance with existing systems. This situation is likely to compromise the financial viability and monitoring capacity of the SROs, their ability to maintain standards and to protect the public interest.

Improvements are needed to ensure that Canadian geoscientists and the companies that employ them can compete internationally. Many other professions in Canada have managed to resolve these structural challenges by reducing and eliminating interprovincial and jurisdictional barriers to mobility in accordance with the objectives of the provincial and federal Agreement on Internal Trade (AIT).

The PDAC supports the professional registration of geoscientists in Canada and is currently working with affected individuals, organizations and governments towards an internationally recognized, Canada-wide approach to professional practice that will promote consistent standards of practice, high rates of compliance, cost effective administration, improved flexibility, national productivity and competitiveness and enhanced protection of the public. The association strongly favours a Canada-wide system of registration that is provincially/territorially administered.

The associations that represent geoscientists in Canada have a responsibility to the public and to the profession. By cooperating on the development of a model for a Canada-wide system of registration, we can ensure that the profession is regulated in a manner that better protects the public and meets the needs of geoscientists and government.

Given the provincial and territorial responsibility for licensing, there will be a need to review and modify the governing regulations to allow for the optimal level of mobility for geoscientists. The PDAC encourages the federal, provincial and territorial governments to work collaboratively to facilitate the harmonization of the various statutes and regulations.

4. Streamlining Fisheries and Oceans Canada's procedures

The process of mineral exploration, because of its potential impact on water courses and fish habitat, has come under the scrutiny of Fisheries and Oceans Canada (DFO). In certain instances, the interpretation of legislation by DFO officials has caused delays to projects and, occasionally, has threatened to bring parts of the industry to a standstill.

Activities such as the erection of temporary bridges and the building of culverts and winter roads have relatively low impacts on waterways. The PDAC and representatives of five other resource industry groups are now working with DFO officials to produce a list of work

practices that will be nationally recognized as having little or no impact on fish habitat and which will, therefore, not require a specific DFO permit.

The mineral industry has also taken the initiative to compile a list of best practices that are specific to exploration for DFO approval. Once that approval has been received, those industry members complying with the best practices can be assured of a timely and streamlined permitting process. We anticipate that the implementation of these nationally recognized operating statements will reduce duplication of effort and speed up project processing times.

The resource industries group is also encouraging DFO to implement and use a one-window approach to permitting across national, regional and local lines.

In British Columbia, the Association for Mineral Exploration BC and the Mining Association of BC have been working with the BC Chamber of Commerce, Council of Forest Industries BC and the BC Agriculture Council on a series of recommended amendments to the Fisheries Act and to DFO policies. Areas of principal concern include provisions for habitat protection, pollution prevention, administration of the legislation, and enforcement. The document will be released in August 2006.

5. Ensuring an adequate labour force for the mineral industry

The human resources challenges that the mineral industry faces are now well known. With 50% of mining industry workers now over 40 years old and 40% of employees expecting to retire over the next decade, the expectation is that between 36,000 and 80,000 skilled workers and professionals will be needed to replace them.

The Mining Industry Human Resource Council (MiHR) will be the lead agency to address these challenges for the industry. In its coordinating and managerial role, it is charged with the provision of products, services, and programs aimed at increasing labour capacity for the sector.

To supplement the MiHR programs, the PDAC is in the preliminary planning stages for a strategy aimed at addressing the labour requirements specifically in the mineral exploration sector. The principal objectives of the strategy are: a) to create awareness of the kinds of employment opportunities that the mineral industry offers; b) to attract young people to careers in prospecting, geosciences, mineral deposits geology, and the exploration business; and c) to ensure that those who have already chosen to work in mineral exploration receive adequate education and training.

Under the PDAC umbrella and with partners either with an interest in mineral exploration or with special expertise to contribute to particular program elements, the program could include, for example, outreach to grade schools and high schools, prospecting schools, educational initiatives for university geology and mining engineering departments, a scholarship and bursary program for students specializing in field geology and exploration, support for field schools and programs for aboriginal communities. Potential partners include provincial and federal governments, provincial associations, PDAC corporate members and MiHR.

As an example, the PDAC's Student Affairs Committee has launched an annual student-industry training workshop focused on mineral exploration. This exciting and innovative new

project is being funded entirely by industry and will enable twenty post-secondary geoscience students, handpicked from across Canada, to attend an all expenses paid, two week, field focused workshop in May 2007.

6. Improving Canada's securities regulatory system

In their bid to streamline this country's securities regulatory system, most Canadian jurisdictions have agreed to adopt a "passport" system. Under this system, a company meeting all of the requirements of its home jurisdiction can use the passport to do business anywhere else in Canada. The PDAC sees this action as a step in the right direction and hopes that it will result in fewer complexities and reduce the high costs associated with the former system, particularly for smaller issuers, while also providing adequate protection for the investing public.

However, ultimately, the PDAC supports a securities regulatory system which features a single securities regulator, a common body of securities law and a single fee structure.

Canada is the only G8 country that does not have a single national securities regulator, and the PDAC remains firm in its conviction that a uniform set of rules and a single fee structure would enhance the country's ability to compete on the international scene.

CONCLUSION

In 2005, there was unanimous agreement by all of Canada's mines ministers that a long-term strategy was needed that would bring about high and sustained levels of mineral exploration in this country. The reasons for this strategy still exist, and the need for its implementation is increasingly urgent. Canada's ability to meet the global demand for mineral commodities and for Canadians to benefit from this demand are contingent on the ability of our mineral industry to discover new mineral deposits. We are confident that the strategy, once implemented, will serve this purpose.

APPENDIX A

The PDAC has conducted a detailed analysis of exploration projects and exploration results for the period 1997 to 2005. The term 'discoveries' contains two categories: mineral occurrences and mineral deposits. Definitions for each category follow. The PDAC defines a discovery based on the date that it is publicly announced.

Mineral occurrence

A mineral occurrence is defined as mineralization that has been identified on the basis of assay results from systematic surface and/or drill hole sampling. In the case of diamonds, a mineral occurrence is defined as a diamondiferous kimberlite body. This may be a completely new occurrence (no field work or related technical work had been previously performed on the occurrence) or an extension to a previously known occurrence. An extension is defined as a zone that significantly extends the original occurrence.

Mineral deposit

A mineral deposit is defined as a mineralized zone on which a resource or reserve calculation has been completed. It is the result of further work beyond that required for the identification of a mineral occurrence. In the case of diamonds, the term mineral deposit is used when a bulk sample of at least 100 tonnes has been conducted on one or more diamondiferous kimberlite bodies.