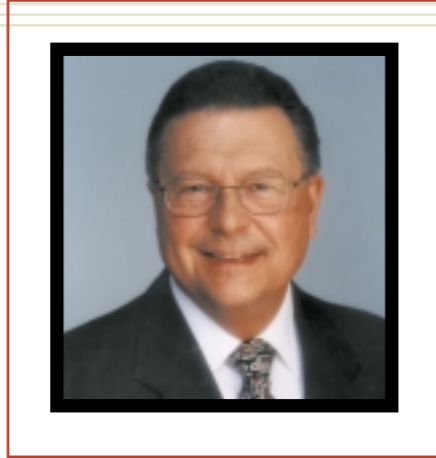




Investment Tax Credit for Exploration in Canada



Mining is an integral part of Canada's technology-driven, knowledge-based economy. The Government of Canada wants to ensure that this resource sector prospers and grows to its full potential. Exploration is vital to ensuring that Canada remains a global leader in mining, and that this sector continues to contribute to the prosperity of Canadian communities in the 21st century.

This is why the Government of Canada introduced the 15 percent federal exploration tax credit for flow-through share investors in its October 2000 Economic Statement. This measure will stimulate investment in mineral exploration throughout Canada.

Canada already leads the world in mine financing and in the application of innovative, high-tech exploration techniques. Our expertise, whether it's developing new technologies or providing a wide range of equipment and services, is second to none.

I am convinced that, by working together, we will continue to show that we are the world's smartest mining nation — the most high-tech, the most environmentally friendly, the most socially responsible, the most productive and competitive — a living model of successful sustainable development.

Ralph Goodale
Minister of Natural Resources Canada

Program's Purpose and Scope

In the Economic Statement and Budget Update of October 18, 2000, the Honourable Paul Martin, Minister of Finance, announced a temporary, 15% investment tax credit for investors in flow-through shares of mineral exploration companies.

This Investment Tax Credit for Exploration (ITCE) is a measure designed to assist junior mining companies in raising new equity through the issuance of flow-through shares. This additional financing should help exploration companies to maintain, or increase, their level of exploration activities in Canada. The ITCE applies to eligible exploration expenses incurred after October 17, 2000, and before January 1, 2004.

The program applies only to preliminary mineral exploration activities conducted from or above ground. It does not apply to oil and gas, coal, bituminous sands or oil shale; expenses incurred to explore underground, or for the purpose of bringing a mine into production, are also excluded.

The information included below is based on Finance Canada publications up to December 21, 2000, and is intended as a general guide only. In cases of doubt the wording of the Finance Canada publications takes precedence.

Program Benefits

A tax credit of 15% of eligible expenses can be applied against a taxpayer's federal income tax otherwise payable for the taxation year during which the investment is made. The ITCE is a non-refundable tax credit that can be carried back three years and carried forward seven years. A taxpayer claiming the ITCE will also be allowed to claim the normal 100% Canadian Exploration Expense (CEE) deduction, which applies for both federal and provincial/territorial income tax purposes. Use of the ITCE will reduce the taxpayer's Cumulative Canadian Exploration Expense account. Taxpayers residing in provinces/territories that provide additional exploration incentives are allowed to claim them in combination with the ITCE, but the use of any tax credit offered by provinces/territories will reduce the amount of expenses eligible for the ITCE and the amount of deductible CEE.



Who qualifies for the tax credit?

Individuals (other than a trust) who are deemed to incur eligible exploration expenses, either individually or through a partnership, pursuant to a flow-through share agreement with a “principal-business corporation,” are eligible for the credit. Principal-business corporations, for these purposes, are corporations whose principal business is exploration, mining and mineral processing.

Which exploration expenses are eligible?

Eligible expenses for the purposes of the ITCE are specifically defined as “flow-through mining expenditures” (FTME). Technically, FTME are restricted to the portion of a Canadian Exploration Expense that is described in paragraph (f) of its definition, in subsection 66.1(6) of the federal *Income Tax Act* (ITA), and that meet additional criteria referred to in subparagraph 16(d) of the Notice of Ways and Means Motion in the October 2000 Economic Statement and Budget Update, and in the December 21, 2000, Finance Canada news release.

In general terms, FTME must be incurred:

- for the purpose of determining the existence, location, extent and quality of a “mineral resource,” which, for ITCE purposes,
 - is a deposit of base or precious metals, diamonds, ammonite gemstones, halite, sylvite, calcium chloride, gypsum, kaolin, or other industrial minerals subject to

certification by the Minister of Natural Resources Canada (as described in Section 248 (1) of the ITA),

- but excludes a deposit of coal, bituminous sands or oil shale;
- after October 17, 2000, and before January 1, 2004;
 - in respect of a mining exploration activity that is conducted from or above the surface of the earth, and that includes prospecting, geological, geophysical and geochemical surveys, drilling (rotary, diamond, percussion or other methods), and “specified sampling” that includes the collecting and testing of samples in respect of a mineral resource to the extent that:
 - the weight of each sample collected does not exceed 15 tonnes;
 - and the total weight of all samples (other than samples that are less than one tonne in weight) collected in respect of any one mineral resource in a calendar year by any person or partnership or any combination of persons and partnerships does not exceed 1000 tonnes.

Can Canadian Exploration Expenses that do not qualify as FTME still be renounced to flow-through share investors?

The rules related to eligible exploration expenses for flow-through shares have not been changed. All Canadian Exploration Expenses (CEE) that are described in paragraphs

(f) and (g) of subsection 66.1(6) of the ITA, which include underground and “pre-production development expenses,” can still be renounced to flow-through share investors. However, only the portion of the expenses that meets the requirements of the FTME is eligible for the ITCE.

The rules that specify the time periods during which CEE related to flow-through shares must be incurred apply to the ITCE.

Does this mean that corporations carrying out exploration will have to keep track of the different types of exploration and of where they conduct exploration work?

The ITCE is only available for expenses related to exploration carried out from or above the surface of the earth. However, a corporation, in the course of its exploration program, may also incur expenses that qualify only for the Canadian Exploration Expense deduction. Therefore, the onus will be on the corporation to correctly identify and renounce the different categories of exploration expenses for federal income tax purposes. The corporation should keep proper records documenting the expenses that are eligible to be renounced and that qualify for the ITCE.

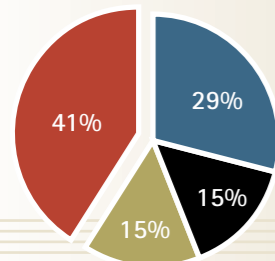
What are the advantages for the individual taxpayer of investing in flow-through shares that involve expenses eligible for the ITCE?

Because the federal investment incentive is delivered in the form of a tax credit, its value is the same for all individual investors, irrespective of their marginal federal income tax rates. However, a large portion of federal flow-through share incentives is still delivered in the form of an income tax deduction (as a Canadian Exploration Expense), the value of which varies with a taxpayer’s marginal tax rate. Due to the variability of provincial/territorial incentives for flow-through shares, the after-tax situation of a taxpayer will also depend on his/her province or territory of residence.

The figure below illustrates the average after-tax cost of a flow-through share investment for individual taxpayers facing the average top marginal tax rate under specific assumptions. The underlying calculations are for illustrative purposes only and may not reflect the particular circumstances of any specific taxpayer.

The ITCE program benefits are contingent on the particular conditions of the flow-through share agreement. Due to the complex nature of the income tax rules applying to flow-through shares, qualified professional advice should be sought to help structure such agreements.

Average Tax Reductions and Incentives Available to an Investor in Flow-Through Shares



Provinces/Territories Without Additional Exploration Tax Incentives

- Federal Personal Income Tax Reduction
- Federal Tax Credit
- Provincial/Territorial Personal Income Tax Reduction
- Net Cost to Investor

Note: In provinces/territories that offer additional exploration incentives, the net after-tax cost of a flow-through share investment would be reduced in proportion to the incentive provided.



Further information is available from:

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