

M. Loffthouse

**ROYAL OAK MINES
STATUS UPDATE**

MEI Exec. Mtg
20 May 1997

676780
Just
VCC ROHS / MR / GSB
Fred - pass a copy on to Ed & Ually.
Peter O

BACKGROUND

- April, 1993 - Royal Oak Mines acquired controlling interest in Geddes Resources Ltd. Geddes had spent some \$49 million exploring mineral claims on its Windy Craggy property in the Tatshenshini-Aksek region of B.C.
- October, 1993 - the Province declared the Tatshenshini-Aksek region as a Class "A" Provincial park, promising to fairly compensate mineral claim holders in the area.
- August, 1995 - the Province signed a legally binding Heads of Agreement (HoA) with Royal Oak/Geddes outlining a \$166.16 million financing package to compensate for Windy Craggy and provide incentive for Royal Oak to develop other mineral claims in the Province, specifically the Kemess and Red Mountain properties.
- January, 1996 - Royal Oak invested \$202 million to complete the acquisition of the Kemess and Red Mountain properties.
- April, 1996 - Royal Oak received its project approval certificate for the development of Kemess South, a 210 million tonne copper, gold, and silver deposit, approximately 300 km northwest of Mackenzie. Construction at the mine site began in July, 1996, with production scheduled for mid/1998.
- January, 1997 - Cabinet appointed Charles Kang, Deputy Minister, MEI, to complete negotiations of a Formal Agreement, required to detailed terms and conditions for disbursement of the financing package.

DISCUSSION

- There are seven significant issues delaying completion of the Formal Agreement. These stem from disagreement over interpretation of the HoA or from differing positions on items not explicitly dealt with in the HoA and involve potential increases to the approved financing package and/or potential foregone revenue for the Province.
- Royal Oak has now agreed to a compromise on the issues and the Formal Agreement is being prepared for approval by Treasury Board/Cabinet.
- The financing package is summarized in the attached. The estimated net present value (npv) of the financing package was \$103.8 million, including a \$4.9 million write-down provision for the Royalty Investment. Under the recommended compromise, an \$5.1 million increase is required for the write-down provision.

RO - won't deal with FNs till courts are clear.
June 12 -> Court injunction decision.
- expect roadblocks.

ROYAL OAK MINES ISSUES

Following is an outline of the major issues and attached is a summary of the impact of positions taken and the recommended compromises.

1. Royalty Investment

In calculating the royalty return, the Province made no allowance for handling costs it agreed to pay, as it believed the costs would be insignificant. Royal Oak expected these costs to include post smelting expenses, which would have significantly reduced the royalty return, requiring an increase of more than \$10 million to the \$4.9 million write-down provision.

Wording in the HoA is open to differing interpretation. Furthermore, it has subsequently been recognized that there are significant financial and administrative risks to the proposed copper royalty.

The parties have agreed to convert to a cash royalty. Royal Oak will receive a handling fee of \$.13 US per pound, which will increase the estimated write-down provision of the royalty return by \$5.1 million

2. Limited Partnership

Royal Oak proposed that the royalty investment be made into a Limited Partnership which, if acceptable with Revenue Canada, could provide income tax savings of \$17 million. This would represent foregone tax revenue for the Province of an estimated \$1.9 million npv and could cause friction in relationships with the Federal Government.

The parties have agreed to allow the Limited Partnership structure, recognizing the Revenue Canada has the final say in whether the tax deduction is acceptable.

3. Invoices

Royal Oak has incurred and invoiced the Province for expenses that are eligible for reimbursement. Royal Oak claims payment is overdue and has charged interest of some \$300,000. The invoices have not been paid as the HoA calls for the expenditures to be defined in the Formal Agreement.

The parties have agreed that the invoices will not be processed until the Formal Agreement is signed and, as such, there is no interest outstanding.

4. Power Line Costs

Construction costs for the power line has increased significantly due to increased stumpage rates resulting from introduction of the Forest Practises Code. Royal Oak believes the stumpage rates should be grandfathered to those in effect when the deal was signed or that the Ministry of Forests should use its discretionary powers to minimize the rates. Reducing the stumpage rates would represent \$13 million in foregone revenue for the Province.

The parties have agreed that the current stumpage rates will apply.

5. Transmission Line

Royal Oak will construct and own a 380 kilometre power line, connected to B.C. Hydro by a substation at Kennedy Lake. Transmission losses will occur over the power line and Royal Oak feels it should only pay for the amount of energy arriving at the mine site. The extent of losses depends on the quality of construction undertaken by Royal Oak. In meeting Royal Oaks request, the Province (BC Hydro) would forego potential revenue of \$200-500,000 annually.

The parties have agreed that Royal Oak will be responsible for the line losses.

*Stumpage gone from
\$25d → \$42.90*

6. Disbursements

Under the HoA, disbursements for the Power Line component are a maximum of \$20 million annually, commencing 1996/97 fiscal. Given delays in undertaking the power line construction, Royal Oak will only expend about \$10 million in fiscal 1996/97, however spend \$30 million in 1997/98.

To ensure timely reimbursement for its expenditures, Royal Oak would like to be able to "catch-up" the unclaimed portion of 1996/97, such that the total maximum available to end of 1997/98 can be \$40 million.

The parties have agreed to permit catch-up of unclaimed disbursements.

Sloane Road

Royal Oak initially intended to construct a connector road to truck concentrate to Sloane for rail shipment to Vancouver. With increased stumpage rates and new environmental restrictions, the estimated cost for Sloane has increased from \$14.2 million to \$45 million. As a result, the alternative, trucking a longer distance down the Omenica Road, is a more economical option.

One of the conditions for funding under \$14.16 million Regional Resource component is construction and maintenance of the Sloane Road. In using Sloane, B.C. Rail is the only option for rail transport. With Omenica, there are larger trucking contracts and Royal Oak has an option of rail transport with C.N. Rail to Prince Rupert or eastward. Accordingly, B.C. Rail stands to lose potential revenue.

The parties have agreed that Royal Oak may still receiving funding if using the Omenica Road so long as B.C. Rail is provided first right of refusal to match contracts from other bidders.

ROYAL OAK MINES INC.

SUMMARY OF FINANCING PACKAGE

COMPONENT	Approved (millions)	Approved NPV (8/95)	Compromise NPV (8/95)	PURPOSE
Compensation	*\$29.00	\$26.50	\$26.50	direct compensation for Windy Craggy
Mine Development Fund	\$20.00	\$17.6	\$17.6	for mineral exploration in BC (RO to match)
Human Resource Fund	\$4.00	\$3.6	\$3.6	to finance training and skills development
Regional Infrastructure Fund	\$14.16	\$7.5	\$7.5	to construct/maintain public infrastructure
Power Line Construction	\$49.00	\$43.7	\$43.7	for construction of a 320 km power line
Royalty Investment	\$50.00	**\$4.9	**\$10.0	to help finance mine infrastructure
TOTAL	\$166.16	\$103.8	\$108.9	

* Per terms of the HoA, \$14.5 million paid April 15, 1996 and April 15, 1997.

** Estimated required write-down provision for the Royalty Investment

APPENDIX II
ROYAL OAK MINES
IMPACT OF ISSUE RESOLUTION

ISSUE	POSITIONS			IMPACT TO PROVINCE			IMPACT TO FINANCING		
	Royal Oak	Committee	Compromise	Royal Oak	Committee	Compromise	Royal Oak	Committee	Compromise
Royalty Calculation: disagreement over HoA	- Cash Royalty ** - \$.13/lb handling fee, RO absorbs all costs. - 50% royalty cap on excess production.	Cash Royalty \$.005/lb handling fee, RO absorbs all costs. No royalty cap	Cash Royalty \$.13/lb handling fee, RO absorbs all costs. 50% royalty cap on excess production.	Eliminates risk from copper ownership. Increased write-down provision required. Upside benefits restricted.	same same Upside benefits retained.	same same Upside benefits restricted.	\$ 5.1M npv	\$0.2M npv	\$ 5.1M npv
Limited Partnership: not in HoA	- Royalty Investment to be made into Limited Partnership.	Offset tax loss with reduction in financing package.	Allow Limited Partnership.	Potential foregone tax revenue.	Province kept whole.	Potential foregone tax revenue.	\$ 1.9M npv	-	\$1.9M npv
Invoices: disagree when payable	- Submitted invoices are overdue and interest is payable.	Don't pay until issues resolved, no interest to accrue.	No invoices paid until Agreement finalized, no interest due.	Payment and interest due on submitted invoices.	No funds until Agreement finalized, no interest due.	No funds until Agreement finalized, no interest due.	\$ 0.3M npv	-	-
Power Line: fees increased since HoA	- Grandfather stumpage to former legislation.	Pay current stumpage.	Pay current stumpage.	Province foregoes stumpage revenue.	Province receives full value of stumpage.	Province receives full value of stumpage.	\$13.0M npv	-	-
Transmission Line Losses: not in HoA	- BC Hydro/Province responsible for line losses.	RO responsible for line losses.	RO responsible for line losses	Province foregoes energy revenue.	No foregone revenue	No foregone revenue	\$0.2-.5M p/a	-	-
Disbursement: change requested due to delays in start-up.	- RO can catch-up shortfall to 1996/97 maximum with 1997/98 disbursements.	Disbursements per HoA.	Permit catch-up	Potential budgetary implications	No catch-up, max. \$20M available fiscal 98, balance delayed to fiscal 99.	may claim up to \$40M to end of fiscal 98.	-	-	-
Sloane Road: not in HoA	- Use of Omenica road more economical	Use of Sloane Road required for funding.	Use of Omenica road okay if BC Rail has first right to match contracts.	-BC Rail could lose revenues	BC Rail receives rail contracts.	BC Rail has opportunity for contracts, dissent from other bidders.	-	-	-
Impact to Financing Package							\$5.4M npv	\$0.2M npv	\$5.1M npv
Potential Foregone Revenue							\$15.1M npv	-	\$1.9M npv
Total Concessions							\$20.5M npv	\$0.2M npv	\$7.0M npv

** RO earlier conceded original position of royalty on smelted copper, which would have impacted financing package by a further \$4.5M npv and that Province pay for costs of up to \$.15/lb

