November 2020

MEMO

Fiscal Benefits of the Mary River Project

Important Notes to Readers

The estimations of economic benefits outlined in this memo are based from a point in time on scenarios and hypothesis taking place in future years as outlined in Technical Supporting Document 25 submitted through the Phase 2 Nunavut Impact Review Board led Environmental Assessment for Baffinland as well as from internal Baffinland records. No conclusion or inference should be made based on the content of this report regarding investment or financial decisions about the Mary River Project, Baffinland Iron Mines Corporation (Baffinland), iron ore, the mining sector in general or the Nunavut and Canadian economy.

All monetary values are expressed in Canadian Dollars (CAD)

Introduction

The following memo outlines the fiscal benefits of the 30 million tonnes per year Mary River Project to Inuit Organizations and Governments throughout the life of mine (2038).

Government of Nunavut [1]

Fiscal revenues paid to the Government of Nunavut are paid against the following requirements:

- Payroll Taxes
- Petroleum (Fuel) Taxes
- Corporate Income Taxes
- Personal Income Tax

Baffinland has paid the following to the Government of Nunavut as of September 30, 2020:

- Payroll Taxes: $32,940,658
- Petroleum (Fuel) Taxes: $20,744,900
- Total: **Over $53 million**

<u>Expected payments to the Government of Nunavut over the life of mine (2038):</u>

- Corporate Income Tax: $321 million
- Territorial Petroleum (Fuel) Tax: $182.5 million
- Payroll Taxes: $51.3 million [2]
- Other Fiscal Revenues (this includes payments to government by Baffinland suppliers, contractors, and other smaller payments): $125 million
- Total: **$679 million**

Government of Canada

Fiscal revenues paid to the Government of Canada are paid against the following requirements:

- Fuel Tax
- Corporate Income Tax

[1] Calculations of projected payments to the Government of Nunavut have not considered the potential implications of Devolution.
[2] Baffinland future payroll tax payment calculations are based on very conservative modelling scenarios to not overstate payments to Government.

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- Aggregate Royalties (Crown Land)

To date Baffinland has made no payments to the Government of Canada against the requirements outlined above.

Phase 2 expected payments to the Government of Canada over the life of mine (2038):

- Corporate Income Tax: $359.7 million
- Fuel Tax: $80.2 million
- Aggregate Royalties (Crown Land): $35.8 million
- Other Fiscal Revenues (this includes payments to government by Baffinland suppliers, contractors, and other smaller payments): $1.2 billion
- Total: **Over $1.5 billion**

Inuit Organizations

Nunavut Tunngavik Incorporated (NTI)

Deposit No. 1 is located on grandfathered federal mining leases that have been designated as Inuit surface and subsurface lands. As such, a Federal Mining Royalty (FMR) will be payable to Indian and Northern Affairs Canada (Crown Indigenous Relations and Northern Affairs Canada) under the Nunavut Mining Regulations (Territorial Lands Act), but the monies will be passed to NTI. Resources collected by NTI from FMR are placed in the "Resource Revenue Trust". Revenues from the operating fund of the Trust are distributed to the NTI and all three Regional Inuit Associations (RIAs) according to NTI's Resource Revenue Policy (NTI 2011). The revenue from the operating fund is distributed as follows:

- 30% - NTI
- 10% - Regional Inuit Organization (each)
- 40% - Regional Inuit Organization (each, divided on per capita basis)

Mines in Nunavut are required to make annual royalty payments to the Crown based on the mine's total output during the fiscal year. The royalty payable is the lesser of:

- 13% of the value of the output of the mine, and
- A graduated rate depending on the value of the mine's output during the fiscal year, at prescribed percentages from 5% to 14%.

The value of the output from a mine is determined by the sum of the market value of minerals produced less deductible expenses which include transportation costs, operating costs, a depreciation allowance for capital assets (up to 100% of historical costs incurred), a development allowance (up to 100% of historical mine development costs incurred), exploration costs and contributions made to a mining reclamation trust.

As the depreciation and development allowance are deductible at a rate of up to 100% of historical costs incurred, a mine can generally recover its historical capital costs (through depreciation and development allowance) prior to paying mining royalties.

To date, no payments have been made by Baffinland towards the Federal Mining Royalty. Payments towards the Federal Mining Royalty are expected to begin in 2030.

Expected payments to Nunavut Tunngavik Inc. over the life of mine (2038):

- Federal Mineral Royalty[3]: **$1.4 billion**

Qikiqtani Inuit Association (QIA)

QIA is a Designated Inuit Organization as outlined in the Nunavut Agreement. Baffinland and the QIA have an Inuit Impact and Benefit Agreement (IIBA) and a Commercial Lease.

Through the IIBA, Inuit benefit financially from the Project through the provision of royalty payments to the QIA as per Article 5 of the IIBA. At present, Baffinland pays the QIA 1.19% of Net Sales Revenue as the royalty for mining at Mary River.

Through the Commercial Lease with the QIA, Baffinland is required to make lease payments, tipping fees for waste disposal, quarry fees and aggregate use fees.

As of September 30, 2020 Baffinland has paid to the QIA the following in accordance with the IIBA. This does not include payments to QIA for ongoing IIBA implementation:

- Advance Payments $38 million
- Quarterly Royalty Payments: $3.14 million
- Commercial lease: $25 million
- Total: **$66 million**

As agreed in the Inuit Certainty Agreement (ICA), the IIBA will be amended to include significant increases in Royalty payments to the QIA over the life of the mine should Phase 2 be approved.

Assuming January 1, 2021 as the date of Phase 2 approval and an assumed iron ore price of $75/ Dry Metric Tonnes, 62%Fe index, Baffinland expects it will pay the QIA over **$969 million** in royalties between 2021- 2038.

Expected payments to the Qikiqtani Inuit Association over life of mine (2038):

- IIBA Implementation Costs: $29.25 million ($2.250 m / 13 calendar quarters)
- Commercial Lease Payments: $73.1 million
- Aggregate Royalties: $27.6 million
- Royalties: $969 million
- Total: **Over $1 billion**

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[3] The federal Mineral Royalties (FMR) calculations use several variables, including the volume of iron ore produced (tons), the revenues per ton that BIM may expect, expected operating costs per ton to extract, process and ship the ore to markets, the Total Depreciation Allowed (TDA) which takes into account the capital costs and the royalty rate. The total amount of FMR was calculated using the following formula:

FMR = ((Tons of ore produced x (Revenues per ton – Costs per ton))-Depreciation) x Royalty rate

FMR = ((391.29 MT x ($69.07-$20.63))-$8.02 B) x 13 % = $1.4 B