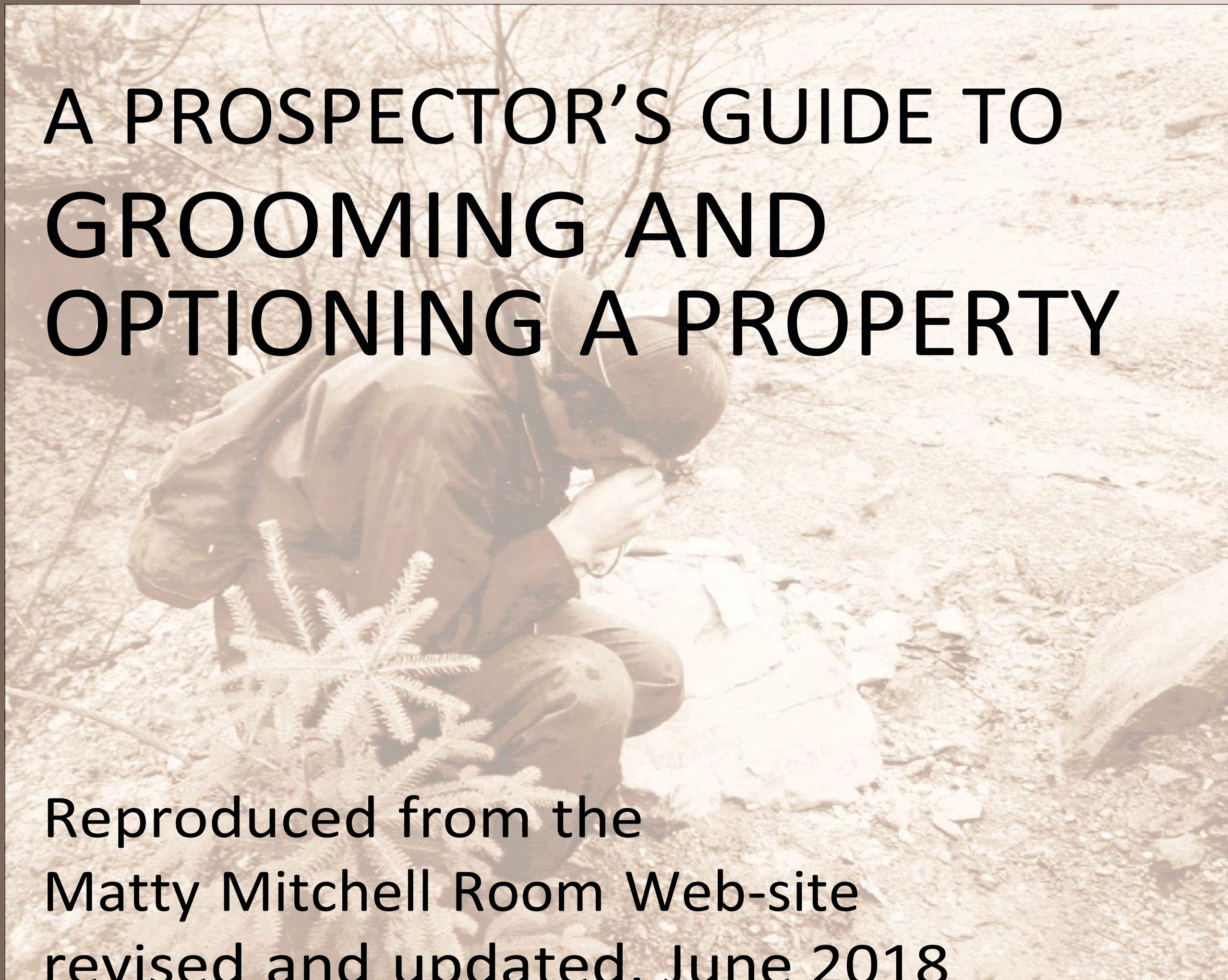

A PROSPECTOR'S GUIDE TO GROOMING AND OPTIONING A PROPERTY

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Matty Mitchell Prospectors Resource Room
Information Circular Number 2

MM
PROSPECTORS
RESOURCE ROOM

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A PROSPECTOR'S GUIDE TO GROOMING AND OPTIONING A PROPERTY

Please Note: An Option Agreement is a legal document. These notes are intended for background information only. It is always advisable to obtain professional legal advice before signing any such agreement.

Congratulations!

You've discovered a new mineral showing. "What next?", you ask? Here are a few points you might wish to consider as you plan your strategy to upgrade, groom and market your new property.

What Additional Work is Needed Before You Begin Marketing Your Property?

It is important to upgrade your property. Not only does it put you in a better negotiating position with a potential buyer, but it also helps the company geologist sell his or her manager on the view that your property is worth exploring. However, you can quickly reach the point of diminishing returns, or worse, spoil or kill your own property. Don't overdo it with your own exploration – leave something to the imagination of potential buyers! Remember that most properties, having been explored, ultimately turn out to have no commercial value. Don't run the risk of using your cash to demonstrate to a visiting company geologist that your property is yet another example of this statistic. A quality property with good assay results will usually sell itself. During a property visit, let the rocks do most of the talking, and hope that the company geologist is asking them the right questions.

You may try to establish the strike length and width of the mineralized rocks in the immediate area and, if applicable, that of the surrounding altered rocks. It might be necessary to do some stripping or trenching in order to establish this. Chip or channel samples from the mineralized outcrops will give you – and the potential buyer – a much better idea of representative grades than do grab samples. You should consider channel sampling your best mineralization.

Soil sampling is an effective survey that you can carry out yourself to outline the potential extension of the known mineralization elsewhere on your property. Make sure you sample along a regular spacing, using a paced and flagged grid.

Depending on the style of mineralization, you may wish to do your own small-scale geophysical survey to outline potential extensions of the mineralized zone. Certain instruments (EM-16, BeepMat) can be borrowed from the Department of Natural Resources, at no cost.

Can you define the style of mineralization? For example, is the mineralization in veins? ...along fractures? ...disseminated? ...massive? ...bedded? Try to make some rough estimate of the percentage of mineralization in the outcrop.

Make note of the presence of chlorite, sericite, magnetite, hematite or other easily identifiable alteration minerals. Can you establish the type(s) of rocks that host the mineralization? Make a stab at identifying the type of deposit that might be on your property (e.g., VMS, porphyry, skarn, etc.). All of this is useful information that may help bring (more) companies to your property.

Remember, preparation is needed to present your information clearly and factually to prospective buyers. Also consider contacting the Mines Branch or Geological Survey of the Department of Natural Resources to ask that one of their geologists visit your property. The department's staff are required to keep any proprietary information gained from such a visit, or from any discussions with you, in confidence.

Be comfortable with your land position. Make sure you've staked enough ground to cover the potential extensions of your showings. In certain instances, the discovery of significant mineralization hitherto unknown in a certain geological region or setting may require that you stake a large parcel of land. Nevertheless, keep in mind that companies most likely won't pay more for additional property that isn't necessary to them.

A few additional words of caution.... Ensure that there is clear title to the property, and that it is free from liens, disputes and encumbrances. Make sure that any previous agreements you have with your other partners are clearly defined and agreed upon – on paper. Memories of the details of verbal agreements may be variously affected by news of a 20 m drill intersection of high-grade mineralization on the property that you, your buddies and your buddies' in-laws pooled your resources to stake.

Who Should You Approach? And When?

Check out your prospective buyers. The most comprehensive list of exploration and mining companies is given in the annual *Canadian Mines Handbook.* This compendium is available at the Geological Survey Library in St. John's, and some public libraries, and gives important information about these companies, including contact addresses. You can also research press releases and trade journals such as The Northern Miner to get a feel for who is picking up what types of properties.

Typically, junior companies are aggressive and very much market-driven, and chiefly interested in commodities and deposit types that are currently in vogue within the industry. Decisions affecting your property can be made quickly, as the chain of command within the company is usually short. Juniors are also interested in many deposits that would be too small to interest major companies. Majors are cash-rich (given the right project). They are constantly in competition with other producers and thus want properties with the potential for significant tonnages of significant grade. It is always wise to research the types of deposits that both the majors and juniors are currently exploring. As a first pass, try to match your prospect and your ideas with a like-thinking company. Many juniors and all majors have websites that will help you get started in your task.

Locally-based juniors can be approached any time. However, most Canadian juniors and majors are based in Toronto or Vancouver, and are unlikely to send a geologist with the sole purpose to visit your property. It may help to arrange property visits to coincide with mining or exploration conferences – such as the annual Canadian Institute of Mining, Metallurgy and Petroleum – CIM meeting (early November). Keep your ears open and find out which companies have geological staff in the province during the field season (*ca.* April–October). They can and should be contacted, and be made aware of your properties. Contact the Department of Natural Resources (Phil Saunders, Mineral Exploration Consultant; telephone 709-729-6193) or other departmental staff and let your intentions be known regarding any properties. The department's staff are constantly in contact with explorationists active in the province and they can help bring your property to the attention of potential buyers. They can also advise you on aspects of option agreements.

Take your property on the road. Make sure it is listed in the Matty Mitchell Room's current "Properties for Option" booklet. Participate in the local CIM prospector's tent. Large national and international annual mining and exploration meetings such as the Cordilleran Round-Up (late January in Vancouver) and the Prospectors and Developers Association of Canada (PDAC: mid- to late March, in Toronto) provide opportunities to showcase your properties. Both have an "Atlantic Canada Rock Room" or equivalent, at which you (or your representative) can display samples, results and maps. The Matty Mitchell Room (first floor, Natural Resources Building, St. John's) can help you prepare display materials and handouts to help you promote your property.

A Property Visit: What to Expect and How to Prepare.

Be there.

Have your assay sheets (and sketch maps, if you have them) available, and all your information clear in your mind. Be prepared to show the visiting geologist representative examples of mineralization, alteration and host rocks. (If you are trying to option a property that has been explored by others previously, make sure you are familiar with these efforts and results; bring along maps from previous geological, geochemical or geophysical surveys.

Make sure you have your sample sites marked. Don't remove all the best exposed mineralization; leave some quality material for the visitors to see.

Expect the visiting geologist to want to independently verify what you've told them. Some samples will have to be collected by the potential buyer, but remember that you are not allowing the person to do exploration at this stage. That – hopefully – will follow.

Don't expect an offer on the spot. Do expect to be quizzed as to your expectations regards the terms of a deal. Be prepared by having a feel for what the current market will bear.

You may wish to have a visiting company sign a confidentiality agreement prior to the property visit. This will ensure that any information obtained as a result of their visit to your property will remain confidential for a set period of time. It should also set out an area of influence surrounding your claims, and provide a guarantee that assay results from samples collected on your property will be shared with you as soon as the company receives them. It is important to let the company know in advance that you want to sign a confidentiality agreement with them. A sample agreement can be found at the end of this article.

The Deal: What Should You Ask For?

The more you know about your prospect, the better able you are to establish its value. Aside from familiarizing yourself with what current market conditions will bear, try to get a feel for how your property fits into current plans and exploration projects of your potential buyer (are you adjacent to an area where the company is planning a major drill program?). Check recent news releases to see the broad terms of recently signed option agreements.

Regardless, you first need to be reimbursed for your leg-work up to now, plus your staking cost and other expenses. You also want to ensure that enough work will be done to ensure the property's proper evaluation. Finally, you also want to ensure that you share in the profits if exploration leads to mine development. The company will be looking for enough time to explore the prospect and decide its merit, before having to commit to a major outlay of cash. Both sides should be reasonable, realistic and fair. Be confident.

The Option Agreement

This is a formal binding legal agreement between you (the prospector, also known as the optionor) and the company (also known as the optionee). Why go to all this trouble? Even though the odds are very much against you and the company, your property may someday become a very profitable mine. You can forget about trying to negotiate details after a fabulous new discovery has been made on the property. It has to be done now, and it has to be done properly.

Once again, it's good to check recent press releases; these are available on-line and in the Matty Mitchell Prospectors Resource Room. Certain details of agreements with publically-traded companies are public information. These will help guide you in the search for your bottom line.

You may decide to ask for cash or shares up front, payable on signing the agreement papers. This is an opportunity to recover cash you've expended to date, coupled with what you consider fair value for the property, given the style, extent and grade of mineralization, together with its potential for future development. The agreement may also outline payments in cash or shares, on an annual basis, normally with a gradual yearly increase. Asking too much, too soon, may result in a situation where the company has to make tough decisions about your property (e.g., return it) before they’ve had the opportunity to complete proper evaluation. Determine whether the shares paid to you are free-trading or held in escrow (shares held in escrow can only be sold at specified times in specified volume). And don’t let the promise of huge cash payments in the latter years of an agreement cloud your thinking. By that time, the company will have made a production decision or dropped your property.

Next to consider is the company's commitment to spend exploration dollars. Like the annual payments, the annual work commitments should increase gradually, but significantly. Each property is different. Much depends on how advanced your project is, as well as the nature of mineralization, to name but two factors. A company’s minimum commitment should be to keep the claims in good standing for a 12-month period.

You then have to agree on the period over which the company earns control of the property. You should consider letting the company earn 100% interest, and keep your interest in the form of a royalty. The earn-in period would normally be in the 3- to 5-year range.

The main royalty to be agreed upon is the NSR or net smelter return. This translates into a percentage (usually 1 to 3%) of the value of all production of minerals from your property that is ultimately shipped from the smelter. You can also negotiate a buy-out or partial buy-out clause, whereby the company purchases your royalty. The cost is variable, but often in the range of 1 to 3 million dollars. Most properties never reach this stage, so it can be a reasonable easy point upon which to find agreement. You may try to retain a small fraction of the original NSR.

Another production-based revenue royalty that can be negotiated instead of a NSR is the NPI or net profits interest. It is based on profits generated from the future mine after all preproduction and development costs and interest costs are recovered by the mine owners. An NPI is normally in the 10 to 15% range. The NPI, however, can be difficult to determine and expensive to verify. Carefully read the fine print related to your royalty, as more and more eligible deductions are being introduced. An additional point: make yourself aware of the effect of federal and provincial taxes on these potential revenues (e.g., the Mining and Mineral Rights Tax Legislation), and factor this into your decision-making.

In some instances, you may be able to negotiate an advance royalty. This royalty would be paid to you while awaiting production, but is charged against your NSR. Once a company earns complete interest in your property, you might find that it resides in limbo for years within the company’s inventory, for any number of reasons. The annual advanced royalty cheque would look good in this situation.

The agreement should also have a drop clause, which ensures that you will have the claims transferred back to you, in the event the optioning company decides to drop the claims at some later date.

You might try to negotiate employment for yourself on the property.

Try to negotiate a clause that requires the buyer to pay for your legal fees up to some maximum. And use a lawyer with mining industry experience.

Don't shop offers, as the credibility loss will limit your ability to attract future partners.

Consult someone in the industry, whom you trust; ask their opinion.

Good Luck!

In preparing this summary, the Matty Mitchell Room has drawn freely from several sources of information and included suggestions from a number of individuals. We particularly acknowledge the website of the British Columbia and Yukon Chamber of Mines and the British Columbia Geological Survey Report 1986-4, “Introduction to Prospecting”. Local prospectors would be wise to investigate both of these resources.

Here is an example of a letter of confidentiality which includes the major points that need to be covered. This is an example only! Please get expert advice before drafting a Letter of Confidentiality.

Letter of Confidentiality

This letter is a confidentiality agreement relating to a planned mineral property visit by representatives of COMPANY X on claims held by PROSPECTOR. The mineral property is located ___________________________________ , N.T.S. ___________________. COMPANY X agrees to the following terms and conditions:

1. All technical information and other information gathered from PROSPECTOR and related to the property visit remains confidential for a period of __________ from the date of the property visit.

2. A zone or area of influence surrounding this property is controlled by the prospector listed above in this letter. The area of influence surrounding the mineral property has dimensions of _____ kms by _____ kms in a _____ direction. This zone of influence is in place for a period of __________. If either of the two parties (COMPANY X) (PROSPECTOR) or anyone acting on their behalf acquire claims in this area of influence, it will be incorporated within the property COMPANY X is visiting should an agreement to option the property be reached.

3. All analytical results pertaining to samples collected on the property by COMPANY X during the site visit will be reported to the prospector listed above upon receipt of the results by COMPANY X from the analytical firms.

4. This letter pertains to conditions for a site visit. Should COMPANY X enter into an option agreement on the property, all of the previous listed terms and conditions within this letter will be included in the formal agreement between the property owner and COMPANY X.

5. The terms and conditions of this letter are valid for a period of __________ effective the date of the property visit.

6. COMPANY X acknowledges that their company does not have an exclusive right to visit the property, meaning that the property owners can enter into other property visit arrangements.

7. This letter shall itself remain confidential for a period of __________.

Signed on behalf of the property owners.

____Date ______________________

Signed on behalf of COMPANY X

____ Date ______________________