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Advocate Mines Limited

ANNUAL
REPORT
1979

ADVOCATE MINES LIMITED

(Incorporated under the laws of Ontario)

Directors

J. Jacques Beauchemin Q.C.
E. R. E. Carter Q.C
A. C. Crosbie
J. M. Emsens
Max Graf*
M. Harris
J. R. M. Hutcheson*
Gilbert Kerlin*
J. P. Power
H. F. Teney Q.C.

*Member of the Audit Committee

Officers

E. R. E. Carter Q.C., Chairman of the Board and President
A. R. Dennis, Treasurer
A. W. Oughtred, Secretary
F. J. Lapalme, Assistant Secretary
E. B. McKenna, Mine Manager

Manager

Johns-Manville Canada Inc.

Registrar and Transfer Agent

National Trust Company, Limited
Toronto, Ontario

Shares Listed

The Toronto Stock Exchange

Auditors

Loftus A. Allen & Co., Toronto, Ontario

Head Office

8th floor, 250 University Avenue
Toronto, Ontario M5H 3E9

Mine Office

Baie Verte, Newfoundland

Annual Meeting of Shareholders

11:00 a.m.
June 20, 1980
Manitoba Room
Royal York Hotel
100 Front Street West
Toronto, Ontario

Corporate Profile

Advocate Mines Limited owns and operates an open-pit asbestos mine and mill complex at Baie Verte on the north east coast of Newfoundland. The mine has a projected life of approximately 14 years. The mill has an operating capacity of 6,500 tonnes per day. Fibre production is shipped by boat from the Corporation's warehouse located on tide water one mile from the mine.

Two grades of asbestos cement fibre are produced and sold pursuant to long term sales contracts with Compagnie Financiere Eternit S.A. of Belgium and Johns-Manville Sales Corporation of the United States. Operations are managed by Johns-Manville Canada Inc.

At December 31, 1979 Advocate's work force included 527 hourly paid and 81 salaried employees, who, in 1979, were paid in excess of $12,000,000 in wages, salaries and benefits. In the last three years Advocate has contributed on average approximately $2,600,000 to the economy of Newfoundland in municipal, mining and income taxes and social security benefits.

Environmental control and mine safety programs are active and continuous and involve employees, management and government working together to achieve one goal, a working environment which is safe and clean.

Directors' Report

Your Corporation continued to be plagued by financial problems in 1979 losing $10,301,273 ($1.72 per share) and ending the year in a deficit position. Of this loss approximately $1,301,803 ($.22 per share) is attributable to increased depreciation and amortization charges (net of applicable tax credits) resulting from the re-evaluation of ore reserves referred to below.

The previously announced unaudited loss of $8,999,470 ($1.50 per share), before the increased depreciation and amortization charges, is attributable to substantially lower than anticipated ore recoveries, high waste to ore ratios and rapidly escalating operating costs. The average percent of fibre recovered from ore crushed in 1979 was 2.78% as compared with 3.67% in 1977 and 4.06% in 1976, the last two years in which your Corporation operated profitably. Similarly, waste to ore ratio was 5.32:1 in 1979 as against 4.0:1 in 1977 and 4.3:1 in 1976. The Report of the Manager included herein speaks of the increase in operating costs. For purposes of comparison 1978 figures have not been used because of the 3 month strike that occurred in early 1978.

As indicated in the accompanying Manager's Report operational improvements have been achieved and, it is safe to say, that if 1979 ore recoveries had been as originally projected, the Corporation's position would be substantially improved. Early in 1979, because of lower than anticipated ore recoveries, your manager, Johns-Manville Canada Inc. instituted a geological re-evaluation of the Advocate ore bodies. Results of this study indicate that although the original definition of the ore bodies remains valid, waste and low grade ore occurrences are greater and, in some areas of the ore bodies, more highly concentrated than originally defined. As a result, ore reserves have been recalculated and reduced by 10.2 million tonnes to 28.9 million tonnes. This has resulted in the increased depreciation and amortization charges referred to above and reference is also made to Note 13 to the consolidated financial statements.

Johns-Manville Canada Inc. has studied the results of the geological re-evaluation within the context of the Advocate operation and canvassed several alternative mining plans. The only realistic options available are:

(i) The abandonment of the West Pit with the North Pit to be mined out over the next three to four years, following which operations would cease or;

(ii) a sufficient increase in Advocate asbestos fibre prices and additional financing to cover Advocate's escalating costs, debt and other obligations and to permit the orderly development and mining of the West Pit ore body.

The Board of Directors agrees that these are the only practical alternatives available to the Corporation.

Fortunately, the Corporation is able to proceed with alternative (ii) as agreement has been reached with Advocate's asbestos fibre customers, Compagnie Financiere Eternit S.A. and Johns-Manville Sales Corporation, to a surcharge on the prices of Advocate fibre sold to them and, in addition, certain shareholders and customers of your Corporation have extended an aggregate of $10,000,000 of debt financing to Advocate by way of term loans subordinated to Advocate's bank indebtedness. These loans bear interest at bank prime and mature December 31, 1985. Also, until Advocate has been returned to a more stable financial position Johns-Manville Canada Inc. and Amet Corporation have agreed that management fees payable to them from 1980 forward will be deferred.

Barring unforeseen operational problems, the new pricing structure and injection of new financing should be sufficient to enable Advocate to continue to meet its obligations, return to a positive cash flow position by 1981, and permit the orderly development and mining of substantially all of Advocate's ore reserves. On this basis the Advocate ore bodies should be depleted by 1993. This outlook is contingent upon ore availability, the development of the West Pit ore body and our ability to control costs.

As indicated elsewhere in this report substantial operational improvements were made in 1979 and are continuing. As well, a cost reduction programme has been implemented. The waste removal programme commenced late in 1978 to make additional ore faces available for mining in the North and West Pits continues satisfactorily. As additional sources of ore are developed, the occurrences of pockets of low grade ore and waste in certain areas will not have as substantial an effect on fibre production levels as was the case in 1978 and 1979.

Notwithstanding Advocate's current difficulties, every effort continues to be made to maintain existing and wherever possible, improve environmental conditions. The Corporation's $2.2 million change house comprising shower, double-locker and improved lunch room and sanitary facilities is essentially complete and has been in operation since March, 1980. The new dry rock storage dust filtration system is complete and will be operational by early May, 1980. Environmental projects completed in 1979 included the $2.3 million air handling system in the crusher and dryer building and a drive-through car wash for employees.

In April, 1980 a new labour agreement with hourly paid employees was settled, which expires May 1, 1981.

Your Corporation is deeply indebted to all of those who, in most difficult circumstances, have continued to work to make the Advocate operation successful. The operational gains that have been accomplished are attributable to the efforts of your General Manager, Johns-Manville Canada Inc., your Mine Manager, E. B. McKenna, his staff, and the Advocate work force as a whole. The support of Advocate's customers is, as always, deeply appreciated.

May 5, 1980.

On behalf of the Board,

E. R. E. Carter,
Chairman of the Board and President.

Report of the Manager on 1979 Operations

To the President and Directors of
ADVOCATE MINES LIMITED

Coming off of a most difficult year in 1978 from the effects of the mine slide and other significant adverse factors, it was determined that major efforts would be required in 1979 to counteract these factors and attempt to stabilize the operation.

Mining

The total material moved from the mine in 1979 was 14,985,100 tonnes. This record performance was made possible by significant improvements in the overall mining operations. The present Mine Superintendent, appointed in 1978, completed his first full year in this assignment and dramatically improved many phases of the operation. The drilling and blasting programs were first of all completely revised. Where previously there had been a continual shortage in drilling equipment availability, utilizing three drills, at the end of the year there existed a surplus in equipment availability, utilizing only two drills. Better fragmentation was also achieved through improved blasting techniques, resulting in improved shovel operation. Considerable effort was also expended in improving the pit roads system, resulting in better truck availability and reduced downtime at the crushing operation. There was also a re-organization in supervisory personnel in the mine and through the efforts of the hourly paid work force, several new shift and daily production records were established. Equipment was also augmented to the dewatering system in order to facilitate operations during the spring run-off. The physical configuration of the pit was significantly improved and this should enhance our ability to remove material from the lower levels of the pit in 1980.

Milling

No significant additions were made to milling equipment in 1979, but steps, primarily through process control, were taken to ensure the maximization of the sales value of production. Some dedusters were added to recover fibre presently being lost to the tailings system. Considerable mechanical and electrical difficulties were encountered with the primary crusher, resulting in above normal downtime and costs. These were in the process of being rectified at year-end.

Maintenance

The position of Plant Engineer, which had been vacant for some time, was filled in 1979 by a competent engineer, experienced in the mining industry. Significant improvements in the maintenance area were initiated in 1979, and the new maintenance programs will be fully established in 1980. These include a re-organization of supervisory personnel to ensure better utilization of our maintenance work force, improved preventative maintenance programs, and an increase in the size of stores operations to ensure better availability and efficiency of inventoried parts. The expansion of Advocate's maintenance facilities neared completion at the end of 1979 at a cost of $1,258,000 expended over the last two years.

Costs

There was a dramatic increase in some major cost components at Advocate in 1979. The average annual compounded rate of cost increases over the four years, 1975 through 1979, was 20%. Specifically in 1979 the total dollar increase over 1978 was 128% in tires, 73% in fuels, and 93% in explosives. There were also substantial increases in the cost of maintenance materials and the majority of these were further adversely affected by the fact that they are purchased in U.S. dollars. Mine management responded to these cost increases with an aggressive cost reduction program but it was not possible to completely offset these continuous cost increases by production efficiencies alone. Particular attention was paid to attempting to reduce energy related costs. Substantial reductions were also made in the work force.

Environment

Significant improvements were made in environmental controls at Advocate in 1979. Most notable of these was the construction of an employee change house which neared completion at the end of 1979 and which when completed will have cost $2,187,000. This building will provide our employees with modern up-to-date facilities and is second-to-none in the industry. Other environmental control installations included the completion of the bag house to control dust emissions from our dryer stacks, equipment to add water to our tailings disposal system, automatic facilities for the washing of all vehicles leaving the property, and environmentally controlled lunch rooms for employees.

Mine Manager

The successful completion of all of the above positive factors were administered through the capable and efficient management of the new Mine Manager, E. B. McKenna, who assumed his role on January 1, 1979. His personal contribution to the improved operation at Advocate has been outstanding.

Fibre Production

The major negative aspect of the operations in 1979, apart from rising costs, was fibre production. Total A-25 fibre production was 48,127 tonnes versus a plan of 55,221 tonnes. The difference was caused by an actual A-25 fibre recovery of 2.28% versus a plan of 2.70%. This dramatic fall off in recovery resulted in the formation of a task force to review all of the geological aspects of the Advocate ore body. The task force completed its work at the end of January 1980 and reported to the Advocate Technical Committee in February. Various mining plans were formulated on the basis of the revised geology. In addition, a consulting geologist was retained to review the work of the task force and the conclusions reached. All of the work of the task force was subsequently tabulated and along with recommendations, was presented to the directors in March and April 1980. It was determined that because of rapidly increasing costs a fibre price increase was essential which has been agreed upon by Advocate's fibre customers. In addition $10,000,000 in new financing has been arranged with certain shareholders, and customers. Accordingly the directors, have approved a ten-year mining plan that will require Advocate to continue to move 15,500,000 tonnes of material per year. The approved plan will enable Advocate to develop the north and west zones using traditional methods consistent with previous plans.

Labour Relations

The Corporation's labour agreement with its hourly work force expired on December 31, 1979. Through intensive negotiations, agreement was reached in April 1980 for a 16 month contract that will expire on May 1, 1981.

Operating Data

	1979	**1978**
A-25 Produced	48,127 tonnes	35,311 tonnes
A-35 Produced	11,279 tonnes	4,527 tonnes
Material Mined	14,985,100 tonnes	9,132,961 tonnes
Ore Crushed	2,107,000 tonnes	1,529,300 tonnes
A-25 Recovery	2.28%	2.31%

May 5, 1979

JOHNS-MANVILLE CANADA INC.

J. P. Power,
Vice-President

ADVOCATE MINES LIMITED

(Incorporated under the Laws of Ontario)

Consolidated Balance Sheet

DECEMBER 31, 1979

(with comparative figures for 1978)

ASSETS	**1979**	**1978**
CURRENT ASSETS		
Cash	$ 89,668	$ 127,639
Accounts receivable	2,951,393	2,624,594
Income and mining taxes receivable	374,660	602,321
Fibre inventory	4,654,581	10,106,972
Stores and supplies	3,541,205	2,718,341
Prepaid expenses	170,966	201,390
	$11,782,473	$16,381,257
MINING PROPERTIES AND RIGHTS – (Note 2)	$ 75,000	$ 75,000
FIXED ASSETS		
Property, plant and equipment	$31,060,495	$28,510,315
Less: Accumulated depreciation	14,218,262	10,724,902
	$16,842,233	$17,785,413
OTHER ASSETS		
Mine development costs less amounts written off	$ 2,008,595	$ 2,197,595
	$30,708,301	$36,439,265

Approved on behalf of the Board:

E.R.E. Carter – Director

– Director

LIABILITIES	**1979**	**1978**
CURRENT LIABILITIES		
Bank loans – secured (Note 3)	$11,430,000	$12,340,000
Accounts payable and accrued liabilities	10,476,653	5,280,556
Current portion of long term debt	1,662,198	662,198
	$23,568,851	$18,282,754
LONG TERM LIABILITIES		
Bank loans and credits – (Note 3)	$ 5,900,000	$ 4,500,000
Conditional sales contract – (Note 4)	959,672	1,121,870
	$ 6,859,672	$ 5,621,870
DEFERRED TAXES	$ 1,953,175	$ 3,906,765
SHAREHOLDERS' DEFICIT		
Capital		
Authorized and Issued		
6,000,000 Common shares of $1 par value	$ 6,000,000	$ 6,000,000
Less: Discount on common shares	3,817,995	3,817,995
	$ 2,182,005	$ 2,182,005
Retained Earnings (Deficit)	(3,855,402)	6,445,871
	$ (1,673,397)	$ 8,627,876
	$30,708,301	$36,439,265

The attached notes are an integral part of these financial statements.

ADVOCATE MINES LIMITED

Consolidated Statement of Loss

FOR THE YEAR ENDED DECEMBER 31, 1979
(with comparative figures for 1978)

	1979	1978
Value of fibre produced	$30,958,071	$21,357,433
LESS:		
Operating costs	$37,119,115	$24,350,527
Interest	2,409,330	1,557,097
Depreciation of equipment	1,185,000	790,000
Amortization of mine development costs	115,000	80,000
Special allowance for depreciation and amortization – (Note 13)	2,443,000	—
	$43,271,445	$26,777,624
Loss before taxes	$12,313,374	$ 5,420,191
Recovery of income and mining taxes		
Current	$ 58,511	$ 434,325
Deferred	1,953,590	1,554,426
	$ 2,012,101	$ 1,988,751
Net loss for the year	$10,301,273	$ 3,431,440
Loss per common share	$ 1.72	$ .57

Consolidated Statement of Deficit

FOR THE YEAR ENDED DECEMBER 31, 1979
(with comparative figures for 1978)

	1979	1978
Retained Earnings – beginning of year	$ 6,445,871	$ 9,877,311
Less: Net loss for the year	10,301,273	3,431,440
Retained Earnings (Deficit) – end of year	$ (3,855,402)	$ 6,445,871

The attached notes are an integral part of these financial statements.

ADVOCATE MINES LIMITED

Consolidated Statement of Changes in Financial Position

FOR THE YEAR ENDED DECEMBER 31, 1979

(with comparative figures for 1978)

	1979	1978
SOURCE OF WORKING CAPITAL:		
Conditional sales contract	$ ——	$ 1,284,068
Proceeds on sale of fixed assets	51,901	8,958
Long term debt	2,400,000	——
	$ 2,451,901	$ 1,293,026
USE OF WORKING CAPITAL:		
Net loss	$10,301,273	$ 3,431,440
Add: Items not affecting working capital		
Depreciation	(1,185,000)	(790,000)
Amortization of mine development costs	(115,000)	(80,000)
Special allowance for depreciation and amortization	(2,443,000)	——
Gain on sale of fixed assets	49,456	8,958
Deferred income taxes, reduction	1,953,590	1,554,426
Applied to operations	$ 8,561,319	$ 4,124,824
Purchase of fixed assets	2,613,265	2,628,800
Payment of long term debt	162,198	——
Current portion of long term debt	1,000,000	662,198
	$12,336,782	$ 7,415,822
Decrease in working capital	$ 9,884,881	$ 6,122,796
Working capital (deficiency) – beginning of period	(1,901,497)	4,221,299
Working capital deficiency – end of period	$11,786,378	$ 1,901,497

The attached notes are an integral part of these financial statements.

Auditors' Report to the Shareholders

We have examined the consolidated balance sheet of Advocate Mines Limited as at December 31, 1979 and the consolidated statements of loss, deficit and changes in financial position for the year then ended. Our examination was made in accordance with generally accepted auditing standards, and accordingly included such tests and other procedures as we considered necessary in the circumstances.

In our opinion, these consolidated financial statements present fairly the financial position of the company as at December 31, 1979 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles applied on a basis consistent with that of the preceding year.

Toronto, Ontario
April 18, 1980.

Loftus A. Allen & Co.
Chartered Accountants

ADVOCATE MINES LIMITED

Notes to Consolidated Financial Statements

DECEMBER 31, 1979

1. ACCOUNTING POLICIES

a) Consolidation

The consolidated financial statements combine the accounts of the Company with those of its wholly owned subsidiary, Advocate Concessions Exploration Company Limited

b) Determination of Income and Valuation of Inventories

The determination of income based on value of production is considered appropriate because:

i) annual fibre production is covered by sales commitments;

ii) annual sales could vary depending upon the length of shipping season and availability of vessels.

Accordingly, the fibre inventory is valued at net realizable value determined by using net selling price at the end of the year and the value of production is determined by using average net selling prices throughout the year.

c) Fixed Assets

Fixed assets are stated at acquisition cost. Depreciation expense was provided for the year on a straight-line basis, using the lesser of the expected life of the asset or the mine life. Based on ore reserves and current production, the mine life is approximately 14 years from 1979.

d) Capitalization of Lease Obligations

The Company leases with options to purchase, various types of mine equipment where the lease period approximates the estimated useful life.

Where there is evidence that substantially all the benefits and risks of ownership have been transferred to the lessee, The Canadian Institute of Chartered Accountants now requires with respect to those leases entered into after January 1, 1979 that:

i) the leased equipment be accounted for as assets and

ii) the future obligation under the leases be accounted for as a liability.

The Company has adopted this recommendation on a prospective basis. Amortization of leased equipment will be provided on a basis that is consistent with the depreciation policy for other similar assets.

e) Mine Development Costs

All costs incurred in developing and placing the mine in production have been capitalized and amortized on the basis of ore reserves and tons mined.

f) Income Taxes

The Company follows the tax allocation method of accounting for income taxes under which full provision for taxes is provided on reported net income regardless of when transactions are recognized for tax purposes.

Deferred income taxes on the balance sheet result principally from claiming capital cost allowance and mine development costs for tax purposes in excess of depreciation and amortization provided in these financial statements.

Provincial mining taxes are calculated on net income and are therefore included with provisions for Federal and Provincial income taxes.

g) Comparative Figures

For purposes of comparison, the 1978 figures for miscellaneous taxes payable (other than income and mining taxes) have been combined with accounts payable and accrued liabilities to conform with 1979 presentation.

2. MINING PROPERTIES AND RIGHTS

The company holds:

a) Two 50 year mining leases covering 623 acres expiring in the years 2014 and 2019 respectively where the Company is carrying on its present mining operations.

b) A 20% interest in the net profits (as defined) from all mining operations carried on by Consolidated Rambler Mines Limited on two 21 year mining leases (known as the Ming Extension), after recovery of all exploration and preproduction expenses incurred by that company. The cumulative net profits from the Ming Extension have not yet exceeded the exploration expenses and no income was due to Advocate in 1979.

c) One extended license (covering 16 mining claims) held under an agreement with Selco Mining Corporation Limited under which Advocate has a 7½% non-assessable undivided interest in the mining property and a right to a further 5% undivided interest upon paying 5% of the cost of bringing any designated mine into production.

d) Approximately 500 acres of land held in fee simple on which the Company's dock, mill, office, garage and houses are located.

During the year the Company allowed five development licenses to expire.

3. BANK LOAN AND CREDITS

The bank operating loan, bank term credit and bankers' acceptances credit are secured by a debenture dated November 15, 1976 in the total amount of $22,000,000, registered in the names of Canadian Imperial Bank of Commerce and The Bank of Nova Scotia constituting a first floating charge on all the company's undertakings, property and assets.

The bank operating loan is repayable on demand and is subject to annual review.

The bank term credit and the bankers' acceptances credit provide for repayments at $750,000 per annum subject to review in 1981. Interest is payable on the bank term credit at the banks' minimum lending rate plus 1% per annum. The interest payable and the service fee on the bankers' acceptances credit is the current rate in effect from time to time.

If at any time no market exists for bankers' acceptances so that Advocate is unable to issue bankers' acceptances, the amount of such bankers' acceptances shall be advanced by the banks to Advocate under the bank term credit and thereafter shall be treated in all respects as an advance under the bank term credit.

The detail of the outstanding amount as shown on the balance sheet is –

Bankers' acceptances credits		$ 7,400,000
Instalments due and shown as a current liability –		
1979 paid January 1980	$ 750,000	
1980 due December 1980	750,000	1,500,000
		$ 5,900,000

4. CONDITIONAL SALES CONTRACT

In 1978 the company acquired certain fixed assets under a conditional sales contract which provides that title is to remain with the seller until the full purchase price is paid. The principal payments are $13,516 per month for 96 months with interest at ½% over prime.

The details of the outstanding amount at December 31, 1979 are as follows:

Total Liability	$ 1,121,870
Instalments due in 1980 and shown as a current liability	162,198
	$ 959,672

5. LEASE OBLIGATIONS

The Company has entered into capital lease agreements prior to January 1, 1979 with varying expiry dates to 1986. The rental expense charged to operating costs in 1979 was $3,636,998 (1978 – $3,163,951).

Had such leases been accounted for as capital leases on a retroactive basis, leased equipment would have been included as an asset on the balance sheet:

	1979	1978
Equipment	$19,133,571	$19,133,571
Less: Accumulated amortization	6,917,505	4,632,821
	$12,216,066	$14,500,750

The amortization which would have been charged to operating costs had such leases been accounted for as capital leases is $2,284,684 for 1979 and $1,708,789 for 1978.

The future minimum lease payments (excluding sales tax and calculated at base interest rates) under capital leases (entered into prior to January 1, 1979) that have non-cancellable lease terms in excess of one year are as follows:

	1979	1978
1979	$ —	$ 3,173,388
1980	3,251,442	3,251,442
1981	3,387,477	3,387,477
1982	3,294,431	3,294,431
1983	2,891,142	2,891,142
1984	343,699	343,699
To 1986	606,978	606,978
Total minimum lease payments	$13,775,169	$16,948,557
Less: Imputed interest	2,261,593	3,349,135
Present value of minimum lease payments	$11,513,576	$13,599,422
Portion of obligation due in one year	2,357,755	2,085,846
Non-current portion of obligation	$ 9.155,821	$11,513,576

Had such leases been accounted for as capital leases, the present value of the minimum lease payments of $9,155,821 (1978 – $11,513,576) would have been shown as a long term liability and $2,357,755 (1978 – $2,085,846) as a current liability. Interest expense related to this liability would have been $1,087,542 for 1979 (1978 – $1,212,409).

The net loss for 1979 would have decreased by $123,000 (1978 – $113,000) had such leases been accounted for as capital leases.

There were no capital leases entered into in 1979.

6. REMUNERATION OF DIRECTORS AND OFFICERS

The aggregate remuneration paid to the directors and the five highest paid employees of the Company for 1979 was $186,926 (1978 – $173,933).

7. PENSION PLANS

The Company maintains pension plans which cover substantially all of its employees. The unfunded past service liability of the employees' pension plan at December 31, 1979 is $607,100 (1978 – $628,800). The unfunded liability will be paid and charged to earnings over 17 years by annual instalments of $56,400 including interest.

8. LEGAL ACTIONS

The Company together with others, is a defendant in product liability suits in the United States in which substantial damages are claimed for alleged injuries to the health of asbestos workers by reason of inhalation of asbestos fibre. The Company denies all liability in these actions. Neither the existence of liability nor the extent of any possible damages can be determined at this time and accordingly, no provision for such liability, if any, has been made in the financial statements.

In 1977, the company wharf, at Baie Verte, Newfoundland, was damaged by a ship during loading operations and the Company sued the ship's owners for approximately $20,000. The ship's owners filed a counter suit in which they claim damages of approximately $250,000 to the ship by reason of alleged failure by the Company to provide a safe berth. There is insufficient information available at this time to determine the merits of the counter suit.

9. INCOME TAX RE-ASSESSMENT

Late in 1978, the Company received a Federal income tax re-assessment in respect of the 1976 taxation year for approximately $375,000 arising principally from the disallowance of earned depletion. The Company, on advice from legal counsel, has filed a notice of objection to the re-assessment and maintains that it is entitled to the deduction for earned depletion. Full provision for income taxes has been made in the financial statements for adjustments other than the disallowance for earned depletion.

10. POTENTIAL FUTURE TAX BENEFITS

As at December 31, 1979, the Company has the following future tax benefits:

i) loss carry forwards of approximately $11,827,000 available for deduction against future taxable incomes of which $3,125,000 expires in 1983 and $8,702,000 expires in 1984;

ii) earned depletion base of approximately $2,685,000 which is available as a deduction from income for tax purposes at the rate of 25% of resource income, and

iii) investment tax credits of approximately $850,000 which may be applied against future tax of which $50,000 expires in 1982, $42,000 expires in 1983 and $758,000 expires in 1984.

The potential future tax benefit attributable to these deductions is approximately $8,106,000.

In accordance with generally accepted accounting principles, this potential tax benefit has not been recognized in the accounts.

11. PREFERENCE SHAREHOLDERS' AGREEMENT

On December 31, 1976 the Company redeemed, out of working capital and borrowed funds, its then outstanding 125,058 4½% cumulative redeemable preference shares of the par value of $100 each. By agreement dated as of November 30, 1976, substantially all of the holders of the preference shares agreed to pay to the Company the amount, if any, by which the net after tax cost of servicing the bank indebtedness, incurred to redeem the preference shares and to replace the working capital used to redeem the preference shares, exceeded the dividends that would have been paid on the preference shares had they not been redeemed in 1976. For the purposes of the November 30, 1976 agreement it was assumed that the last of the preference shares would have been redeemed in 1979 pursuant to the original 1958 financing agreement between the Company, the holders of the preference shares and others.

The determination of the amount, if any, to be paid to the Company by the former holders of the preference shares is to be made at the time that the bank indebtedness, which as of January 30, 1980 had been reduced to $4,500,000, is repaid by the Company. As at December 31, 1979, the amount that would have been owing to the Company would have been $285,000 subject to reduction or elimination if the 1979 loss is utilized to reduce or eliminate future taxes. As there is no virtual certainty as to the amount owing to the Company as at December 31, 1979, no amount has been recorded on the books.

12. SUBSEQUENT EVENT

Subsequent to December 31, 1979, the Company entered into financing arrangements whereby: –

a) Certain shareholders and customers of the Company have loaned $10,000,000 to Advocate by way of notes due December 31, 1985 subordinated to the Company's bank indebtedness with interest at bank prime. Subject to the prior consent of the Company's bankers, the Company may prepay the notes in whole or in part prior to maturity without notice, penalty or bonus.

and

b) Advocate's asbestos customers have agreed to a surcharge on the price of fibre sold to them.

13. DEPRECIATION AND AMORTIZATION

The Company has re-examined the geological information in light of current economic conditions and has revised the ore reserves downward at December 31, 1979 to 28.9 million tonnes. As a result, additional depreciation of $2,369,000 and amortization of $74,000 on account of prior years has been recorded in the statement of loss as a special allowance in 1979.

Five Year Financial Summary

	1979	1978	1977	1976	1975
FOR THE YEAR (in thousands)					
Value of fibre produced	$ 30,958	$ 21,357	$ 34,475	$ 31,790	$ 21,389
Operating costs	37,119	24,351	27,036	22,410	18,136
Amortization and depreciation	3,743	870	1,275	1,085	965
Exploration	—	—	—	76	66
Interest	2,409	1,557	940	57	295
Gifts to school board	—	—	—	251	286
Provision for (recovery of) income and mining taxes	(2,012)	(1,989)	1,815	3,482	932
	$ 41,259	$ 24,789	$ 31,066	$ 27,361	$ 20,680
Net income (loss)	$ (10,301)	$ (3,432)	$ 3,409	$ 4,429	$ 709
Provision for cumulative preference dividend	—	—	—	563	624
Net income (loss)	$ (10,301)	$ (3,432)	$ 3,409	$ 3,866	$ 85
Per share	$ (1.72)	$ (.57)	$ .57	.64	$ .01
Working capital generated	(8,561)	(4,125)	5,839	7,803	2,700
Per share	(1.43)	(.69)	.97	1.30	.45
Working capital from long-term loan	2,400	1,284	—	10,000	—
Working capital used for					
Preference dividend	$ —	$ —	$ —	$ 563	$ 624
Common dividend	—	—	1,110	486	450
Redemption of preference shares	—	—	—	12,506	1,350
Fixed assets	2,613	2,629	1,715	1,269	666
Current portion of long-term debt	1,162	662	2,500	2,500	—
AT THE YEAR END (in thousands)					
Working capital (deficiency)	$ (11,786)	$ (1,902)	$ 4,221	$ 3,707	$ 3,228
Fixed assets	16,842	17,785	15,946	15,423	15,432
Preproduction and mine development costs	2,009	2,198	2,278	2,393	2,508
Other assets at cost	75	75	75	75	476
	$ 7,140	$ 18,156	$ 22,520	$ 21,598	$ 21,644
Less: Long-term debt	5,900	4,500	5,000	7,500	—
Less: deferred taxes*	1,953	3,907	5,461	4,338	2,758
Less: Conditional Sales Contract	960	1,121	—	—	—
Total shareholders' equity	$ (1,673)	$ 8,628	$ 12,059	$ 9,760	$ 18,886
Preference shares, par value	—	—	—	—	12,506
Common shares, book value	$ (1,673)	$ 8,628	$ 12,059	$ 9,760	$ 6,380
Common shares book value per share*	$ (.28)	$ 1.44	$ 2.01	$ 1.63	$ 1.06
PRODUCTION					
Fibre production (tonnes) A-25	48,127	35,311	59,886	66,118	50,894
A-35	11,279	4,527	15,435	10,490	12,247
Material mined (thousands of tonnes)					
Ore	2,371	1,488	2,301	1,879	2,390
Waste and overburden	12,614	7,645	9,205	8,104	6,936
	14,985	9,133	11,506	9,983	9,326
Waste to ore ratio	5.32:1	5.14:1	4.0:1	4.3:1	2.9:1
Recovery from ore crushed	2.78%	2.60%	3.67%	4.06%	2.85%
Ore reserves (thousands of tonnes)	28,900**	41,439	42,339	44,155	45,443

*1975 is restated to give retroactive effect to full tax allocation accounting for mining taxes and the settlement of federal income tax reassessments for 1968 and 1969.

**After recalculation as at December 31, 1979 and reduction by 10.2 million tonnes.

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