

INCO LTD  
Form 10-K  
March 15, 2004

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**SECURITIES AND EXCHANGE COMMISSION**  
Washington, D.C. 20549

**Form 10-K**

þ **ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934**

**For the fiscal year ended: December 31, 2003**

**Commission File Number 1-1143**

**Inco Limited**

*(Name of Registrant as specified in its charter)*

**Canada**  
*(Jurisdiction of incorporation)*

**145 King Street West, Suite 1500  
Toronto, Ontario, Canada**  
*(Address of principal executive offices)*

**98-0000676**  
*(I.R.S. Employer Identification No.)*

**M5H 4B7**  
*(Postal Code)*

**(416) 361-7511**

*(Telephone number)*

Securities registered pursuant to Section 12(b) of the Securities Exchange Act of 1934 (the Act):

<b>Title of Each Class</b>	<b>Name of Each Exchange on Which Registered</b>
Common Shares	New York Stock Exchange*
Stock Purchase Rights	New York Stock Exchange
Common Share Purchase Warrants	New York Stock Exchange

The Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Act during the preceding 12 months, and (2) has been subject to such filing requirements for the past 90 days.

The Registrant is an accelerated filer (as defined in Rule 12b-2 under the Act).

As of June 30, 2003, the aggregate market value, based upon the closing sale price of the Common Shares on the New York Stock Exchange, of the Registrant's voting shares held by non-affiliates equaled \$3,951 million. §

As of February 20, 2004, 187,300,108 Common Shares (including non-voting fractional interests aggregating 5,096 Common Shares) of the Registrant were issued and outstanding.

**DOCUMENTS INCORPORATED BY REFERENCE**

## Edgar Filing: INCO LTD - Form 10-K

Portions of the Registrant's proxy circular and statement dated February 20, 2004 for the 2004 Annual and Special Meeting of Shareholders of the Registrant are incorporated by reference in Part III of this Report to the extent set forth in Items 10, 11, 12 and 14 hereof.

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\* In addition, the Common Shares are listed on the Toronto and London stock exchanges and are traded on certain other exchanges principally through independent arrangements made by securities dealers.

In addition, the Stock Purchase Rights and the Common Share Purchase Warrants are listed on the Toronto Stock Exchange.

§ Unless otherwise stated, all dollar amounts in this Report are expressed in United States currency.

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## 2003 ANNUAL REPORT ON FORM 10-K

UNLESS OTHERWISE STATED, ALL DOLLAR AMOUNTS IN THIS REPORT  
ARE EXPRESSED IN UNITED STATES CURRENCY

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**PART I**

**Items 1. and 2. *Business and Properties of Inco Limited***

**Introduction**

Inco Limited ( Inco , the Company , we or us ) was incorporated in 1916 under the laws of Canada, succeeding a business established in 1902. In 1979, the Company was continued by articles of continuance under the *Canada Business Corporations Act* and is governed by that Act. The Company's executive offices are located at 145 King Street West, Suite 1500, Toronto, Ontario, Canada M5H 4B7. Unless the context otherwise requires, all references in this Report to Inco or the Company include all of its consolidated subsidiaries, unincorporated units and divisions.

Inco is one of the world's premier mining and metals companies. The Company is a leading producer of nickel, a hard, malleable metal which, given its properties and wide range of applications, can be found in thousands of products. The Company is also an important producer of copper, precious metals and cobalt and produces sulphuric acid and liquid sulphur dioxide as by-products from its processing operations at Sudbury, Ontario. The Company's principal mines and processing operations are located in the Sudbury area of Ontario, the Thompson area of Manitoba and, through a subsidiary in which the Company has an equity interest of 61 per cent, PT International Nickel Indonesia Tbk ( PT Inco ), on the island of Sulawesi, Indonesia (reference is made to PT International Nickel Indonesia Tbk below). The Company has additional wholly-owned metals refineries at Port Colborne, Ontario and in the United Kingdom at Clydach, Wales and Acton, England. The Company also has interests in nickel refining capacity in the following Asian countries: in Japan, through contractual arrangements with Inco TNC Limited ( ITL ), in which the Company has an equity interest of 67 per cent; in Taiwan, through Taiwan Nickel Refining Corporation ( Taiwan Nickel ), in which the Company has an equity interest of 49.9 per cent; and in South Korea, through Korea Nickel Corporation ( Korea Nickel ), in which the Company has an equity interest of 25 per cent. In the People's Republic of China ( China ), the Company has a 65 per cent equity interest in Jincou Nonferrous Metals Co., Ltd. ( Jinco ), a company which produces nickel salts for plating and other applications at a plant near Shanghai. In August 2003 the Company announced that it would be forming Inco Wanzhong Advanced Technology Materials (Dalian) Ltd. ( Inco Wanzhong ), a new joint venture company in which Inco would have approximately a 62 per cent equity interest. Inco Wanzhong is being established to produce high quality nickel foam for sale to the manufacturers of nickel rechargeable batteries in the Asian market. We have been evaluating other commercial relationships in China, and in early March 2004 started up a shearing and packaging operation for certain nickel products to service the specific needs of this market.

Inco is currently developing or plans to develop two major new or greenfield projects, its wholly-owned Voisey's Bay nickel-copper-cobalt project in the Province of Newfoundland and Labrador and its approximately 85 per cent-owned Goro nickel-cobalt project in the French overseas territorial community (*collectivité territoriale*) of New Caledonia ( New Caledonia ).

Inco owns approximately an 85 per cent equity interest in Goro Nickel S.A. ( Goro Nickel ), the project company which holds a number of concessions covering nickel-cobalt properties in New Caledonia. In April 2001, the Company announced that it planned to proceed with the construction of a commercial nickel-cobalt project in the south province of New Caledonia to supply nickel products to stainless steel customers in South Korea, Taiwan and eventually China and cobalt products to certain markets. This project encompassed a fully integrated mining and processing facility with a planned annual production capacity of approximately 55,000 tonnes of nickel and 4,500 tonnes of cobalt. In September 2002, the Company initiated a review process covering a number of key aspects of the Goro project, including the project's capital cost estimate and construction schedule, and in December 2002 it suspended construction and initiated a significantly more comprehensive review of the project following the receipt of information from the engineering firms that had been providing engineering, procurement and construction management services to the project which indicated an unacceptable increase in the capital cost estimate for the project of 30 to 45 per cent above the project's then current capital cost estimate of \$1,450 million. This review evolved into two phases during 2003. The first phase of this review focused on an orderly suspension of work and identification of opportunities for capital cost reduction. On

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August 13, 2003, the Company announced the key results of the first phase of the review process and that it was moving to the second phase of the review process which would involve a structured process to further develop the capital cost reduction opportunities identified in the first phase and establish a capital cost control estimate, an updated project schedule and an optimized and clearly defined scope and execution plan for the project. The Company currently plans to report on the status of the second phase in August 2004 and to reach a decision on whether or not to proceed, and if the decision is to proceed, the terms and conditions on how, we would proceed with this project. As a result of the actions taken by December 31, 2002, the Company recorded a pre-tax charge of \$25 million in the fourth quarter of 2002 relating to the Goro project. This charge included \$62 million (i) relating to the cancellation or termination of certain outstanding contractual obligations, (ii) to accrue for certain demobilization costs and (iii) to reduce the carrying value of certain assets relating to the project. This charge was partially offset by currency hedging gains of \$37 million on certain forward currency contracts which became ineffective for hedge accounting purposes because of the suspension of this project. For further information on this review and other aspects of the Goro project, see "Goro Nickel S.A." below.

Inco holds a 100 per cent equity interest in the Voisey's Bay nickel-copper-cobalt deposits in Labrador in the Province of Newfoundland and Labrador through its wholly-owned subsidiary, Voisey's Bay Nickel Company Limited ("VBNC"). In 2002 the Company reached agreements with the other key stakeholders in the project, the Province of Newfoundland and Labrador, the Labrador Inuit Association ("LIA") and Innu Nation, to enable the commercial development of the Voisey's Bay deposits to proceed. The Company made significant progress on the initial or phase 1 of the Voisey's Bay project in 2003. In 2003, the Company spent approximately \$138 million on the initial phase of this project, which phase consists of an open pit mine, concentrator and related facilities and a research and development program on hydrometallurgical processing technologies and certain other programs, and currently expects to spend approximately \$430 million on this initial phase in 2004. Approximately 70 per cent of the project engineering and 75 per cent of the procurement for the open pit mine and the concentrator and related facilities had been completed by early March 2004. During 2003, an airstrip and construction camp, and nearly one-third of the concentrator construction were completed, and work began on the project's port facility. During 2003, the Company, as part of the hydrometallurgical process research and development program, continued testing pressure oxidative leaching processes for Voisey's Bay at its mini-pilot plant in Mississauga, Ontario which began operation in the second quarter of 2003. As a result of a review of the net carrying value of the Voisey's Bay project which was announced in June 2002, the Company recorded a non-cash charge of \$1,552 million, net of deferred income and mining taxes of \$770 million, in the second quarter of 2002, to reduce the \$3,753 million net carrying value of the Voisey's Bay project to \$2,201 million. For further information on the Voisey's Bay project and related matters, see "Voisey's Bay Nickel Company Limited" below.

Inco's properties are described under "Description of Business" and "Ore Reserves and Mining Rights" below.

The information in this Report is as of December 31, 2003 except where an earlier or later date is expressly indicated. Nothing included herein should be considered as implying that any information is correct as of any date other than December 31, 2003, except as otherwise expressly stated.

In this report, certain data and estimates which had been previously limited to the Western World or the Western World plus China because of limited available data from certain countries or regions has been reported on a global or worldwide basis for 2003.

## **Availability of Documents**

Inco files Annual Reports on Form 10-K, Quarterly Reports on Form 10-Q and Current Reports on Form 8-K with the Securities and Exchange Commission. You may read and copy any materials we file with the Securities and Exchange Commission at the Commission's Public Reference Room at 450 Fifth Street, NW, Washington, DC 20549. You may obtain information on the hours of operation of the Securities and Exchange Commission's Public Reference Room by calling the Commission at 1-800-SEC-0330. The Securities and Exchange Commission maintains an Internet site (<http://www.sec.gov>) that contains reports, proxy and information statements, and other information regarding issuers that file electronically with the Commission. Such reports and all amendments to such reports regarding the Company are available free of charge on the Company's

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website, [www.inco.com](http://www.inco.com), as soon as reasonably practicable after such reports are electronically filed with the Securities and Exchange Commission. Information contained in or otherwise accessed through the Company's website does not form part of this Report. All such references to the Company's website are inactive textual references only.

### **Cautionary Statement Regarding Forward-Looking Statements**

Certain statements contained in this Report are forward-looking statements (as defined in the U.S. Securities Exchange Act of 1934, as amended). Examples of such statements include, but are not limited to, statements concerning: (1) the price volatility for nickel and other primary metal products produced by the Company; (2) the long-term demand for and supply of nickel, copper and other metals as well as the availability of, and prices for, intermediates containing nickel purchased by the Company, and nickel-containing stainless steel scrap and other substitutes for primary nickel; (3) the premiums realized by the Company over London Metal Exchange (LME) cash prices and the sensitivity of the Company's results of operations to changes in metals prices, prices of commodities used in its operations and interest and exchange rates; (4) the Company's strategies and plans; (5) the Company's interest and other expenses; (6) the Company's energy and other costs, and pension contributions and expenses and assumptions relating thereto; (7) the Company's position as a low-cost producer of nickel; (8) the Company's debt-equity ratio and tangible net worth; (9) the political unrest or instability in countries such as Indonesia and its impact on the Company's Indonesian subsidiary, PT Inco, and political developments in other countries in which the Company operates and elsewhere; (10) the completion and results of a comprehensive review of the capital cost, scope, schedule and other key aspects of the Goro project; (11) the timing of reaching a decision on whether to proceed with, and the necessary financing plans and arrangements for, and partner or similar investment and other agreements or arrangements associated with, the Goro project, and the timing of the start of production and the costs of construction with respect to, the issuance of the necessary permits and other authorizations required for, and engineering and construction timetables for, the Goro and Voisey's Bay projects; (12) the Company's estimates of the quantity and quality of its ore reserves; (13) planned capital expenditures; (14) the Company's costs of production and production levels, including the costs and potential impact of complying with existing and proposed environmental laws and regulations and net reductions in environmental emissions; (15) the impact of changes in Canadian dollar-U.S. dollar and other exchange rates on the Company's costs and the results of its operations; (16) the Company's sales of specialty nickel products; (17) the Company's cost reduction and other financial and operating objectives and planned maintenance shutdowns; (18) the commercial viability of new production processes and process changes and processing recoveries for its development projects; (19) the Company's productivity, exploration and research and development initiatives as well as environmental, health and safety initiatives; (20) the negotiation of collective agreements with its unionized employees; (21) the Company's sales organization and personnel requirements; (22) business and economic conditions; and (23) the enforceability of certain liabilities. Inherent in forward-looking statements are risks and uncertainties well beyond the Company's ability to predict or control. Actual results and developments are likely to differ, and may differ materially, from those expressed or implied by the forward-looking statements contained in this Report. Such statements are based on a number of assumptions which may prove to be incorrect, including, but not limited to, assumptions about: (a) business and economic conditions, including exchange rates and energy, and other anticipated and unanticipated costs and pension contributions and expenses; (b) the supply and demand for, deliveries of, and the level and volatility of prices of, nickel, copper, cobalt and the Company's other primary metals products, purchased intermediates and nickel-containing stainless steel scrap and other substitutes and competing products for the primary nickel and other metal products the Company produces; (c) the timing of the receipt of regulatory and governmental approvals for the Goro and Voisey's Bay projects and other operations; (d) the availability of financing, including through partner or other participation arrangements in the case of the Goro project, for the Company's development projects on reasonable terms; (e) the Company's costs of production and production and productivity levels, as well as those of the Company's competitors; (f) engineering and construction timetables and capital and operating costs for the Goro and Voisey's Bay projects; (g) market competition; (h) mining, processing, exploration and research and development activities; (i) the accuracy of ore reserve estimates; (j) premiums realized over LME cash and other benchmark prices; (k) tax benefits; (l) the resolution of environmental and other proceedings and the impact on the Company of various environmental regulations and initiatives;

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(m) political instability in Indonesia and other countries or locations in which the Company operates or otherwise; and (n) the Company's ongoing relations with its employees at its operations throughout the world. The forward-looking statements included in this Report represent the Company's views as of the date of this Report. While the Company anticipates that subsequent events and developments may cause the Company's views to change, the Company specifically disclaims any obligation to update these forward-looking statements. These forward-looking statements should not be relied upon as representing the Company's views as of any date subsequent to the date of this Report.

**Description of Business***Sales*

The following table shows the Company's net sales to customers for the three years ended December 31, 2003:

	<u>2003</u>	<u>2002</u>	<u>2001</u>
	(in millions)		
Primary nickel	\$2,109	\$1,654	\$1,488
Copper	171	184	195
Precious metals <sup>(1)</sup>	114	238	292
Cobalt	17	24	34
Other <sup>(2)</sup>	63	61	57
	<u>          </u>	<u>          </u>	<u>          </u>
Net sales to customers	\$2,474	\$2,161	\$2,066
	<u>          </u>	<u>          </u>	<u>          </u>

(1) Excludes toll-refined materials.

(2) Representing principally sales of sulphuric acid, liquid sulphur dioxide, miscellaneous primary metals products and reprocessed waste materials.

*Deliveries*

The following table shows deliveries of the Company's principal primary metals and related products for the three years ended December 31, 2003:

	<u>2003</u>	<u>2002</u>	<u>2001</u>
Nickel, including intermediates <sup>(1)</sup> (tonnes) <sup>(2)</sup>	213,890	231,590	230,049
Copper <sup>(3)</sup> (tonnes)	93,335	113,116	116,751
Cobalt (tonnes)	903	1,582	1,454
Platinum <sup>(4)</sup> (troy ounces, in thousands)	83	189	177
Palladium <sup>(4)</sup> (troy ounces, in thousands)	101	225	206
Rhodium <sup>(4)</sup> (troy ounces, in thousands)	17	13	13
Ruthenium <sup>(4)</sup> (troy ounces, in thousands)	2	1	4
Iridium <sup>(4)</sup> (troy ounces, in thousands)	6	3	5
Gold <sup>(4)</sup> (troy ounces, in thousands)	50	71	76
Silver <sup>(4)</sup> (troy ounces, in thousands)	1,435	1,570	1,540
Sulphuric acid and liquid sulphur dioxide (tonnes)	548,000	732,000	696,000

(1) Includes 29,780 tonnes in 2003, 19,343 tonnes in 2002 and 22,978 tonnes in 2001 purchased by the Company.

(2) A tonne is a metric unit equal to approximately 2,204.6 pounds.

(3) Includes 1,133 tonnes in 2003 and 3,097 tonnes in 2002 purchased by the Company.

(4) Excludes toll-refined materials.



**Table of Contents***Prices**Nickel*

Inco's nickel price realizations tend to lag LME cash nickel price movements due primarily to the terms of the Company's contractual sales arrangements with certain of its customers. The LME, a physical market where various metals, including nickel, can be bought or sold for prompt or future delivery, represents the principal terminal market in the world for nickel meeting certain specifications. The Company realizes a premium over prevailing LME cash prices for its nickel powders and other value-added products, as discussed under Inco Special Products below.

The Company's average realized price for its primary nickel products, including intermediates and purchased products, was \$9,860 per tonne (\$4.47 per pound) in 2003, representing an increase of 38 per cent from the average price of \$7,143 per tonne (\$3.24 per pound) realized in 2002. The 2002 average price was 10 per cent higher than the average price of \$6,468 per tonne (\$2.93 per pound) realized in 2001.

The Company's price realizations for its nickel and other primary metals products generally reflect LME or other metal market prices and, over the longer term, depend principally upon the balance between demand for its products in the marketplace relative to the supply available from the Company and its competitors, including for this purpose similar primary metals materials in various producer, merchant and consumer inventories, inventories of secondary or scrap materials containing nickel and other metals in usable or recyclable form, and supplies of other materials which may compete as substitutes. Of particular importance is the availability of nickel-containing stainless steel scrap, which competes directly with primary nickel as a source of nickel for use in the production of stainless steel. The scrap ratio, or that portion of total nickel units consumed in the form of nickel-containing stainless steel scrap by stainless steel producers in the world, was 44 per cent in 2003, compared with 45 per cent in 2002 and 47 per cent in 2001. The applications for nickel and variations in demand for and supply of nickel are discussed under Nickel below.

For information on the Company's hedging transactions relating to nickel, see Item 7A of this Report and Notes 1, 20 and 23(h) to the financial statements under Item 8 of this Report.

The average prices, per tonne and per pound, realized by Inco for its primary nickel products, including intermediates and purchased products, for the five years ended December 31, 2003, are shown in the following table:

<b>Year</b>	<b>Nickel</b>	
	<b>(\$ per tonne)</b>	<b>(\$ per pound)</b>
1999	6,415	2.91
2000	9,007	4.09
2001	6,468	2.93
2002	7,143	3.24
<b>2003</b>		
First Quarter	8,582	3.89
Second Quarter	8,652	3.92
Third Quarter	9,614	4.36
Fourth Quarter	12,403	5.63
Year	9,860	4.47

*Copper*

The Company's average realized price for copper was \$1,832 per tonne (\$0.83 per pound) in 2003, representing an increase of 12 per cent from the average price of \$1,629 per tonne (\$0.74 per pound) realized in 2002. The 2002 average realized price was two per cent lower than the average price of \$1,668 per tonne (\$0.76 per pound) realized in 2001.





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The average prices, per tonne and per pound, realized by the Company for copper, including purchased products, for the five years ended December 31, 2003, are shown in the following table:

Year	Copper	
	(\$ per tonne)	(\$ per pound)
1999	1,631	0.74
2000	1,908	0.87
2001	1,668	0.76
2002	1,629	0.74
<b>2003</b>		
First Quarter	1,714	0.78
Second Quarter	1,641	0.74
Third Quarter	1,329	0.60
Fourth Quarter	2,087	0.95
Year	1,832	0.83

*Other Metals*

The average prices, per tonne or per troy ounce, realized by the Company for cobalt, the principal platinum-group metals (platinum, palladium and rhodium), gold and silver, all of which are produced primarily from the Company's Ontario ores, for the five years ended December 31, 2003, are shown in the following table:

Year	Cobalt	Platinum	Palladium	Rhodium	Gold	Silver
	(\$ per tonne)			(\$ per troy ounce)		
1999	30,556	377.59	359.80	888.33	280.69	5.29
2000	29,475	541.55	670.04	1,930.63	278.91	4.99
2001	23,216	541.27	711.32	1,475.85	270.50	4.40
2002	15,124	545.92	419.70	804.59	309.17	4.58
2003	18,846	653.87	202.69	530.67	366.15	4.86

For information on the Company's hedging transactions relating to these metals, see Item 7A of this Report and Notes 1, 20 and 23 to the financial statements under Item 8 of this Report.

*Operating Results*

The Company's operating results comprise earnings or loss before income and mining taxes, interest expense, other income or expenses, and minority interest. All financial statement information in this Report is based on the Company's financial statements prepared in accordance with Canadian generally accepted accounting principles (GAAP). A reconciliation of the Company's financial statements to U.S. GAAP is presented in Note 23 to the financial statements under Item 8 of this Report.

*Customers*

As in recent years, sales of the Company's primary metals products in 2003 were concentrated in the United States, Europe, Japan, other countries in Asia, and Canada, with sales of nickel to customers in Asia representing about 66 per cent of the Company's total nickel sales revenues for 2003. For further information, see Inco's Position in the Nickel Industry below.

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For 2003, the Company had no non-affiliated customer which accounted for more than five per cent of Inco's total nickel deliveries. In 2002, Special Metals Corporation ( SMC ), which purchased Inco's alloys business in 1998, was the only non-affiliated customer whose purchases accounted for more than five per cent of Inco's total deliveries. Such purchases by SMC accounted for approximately six per cent of Inco's total nickel deliveries for 2002, compared with approximately eight per cent in 2001. As discussed under *Management's*

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*Discussion and Analysis of Financial Condition and Results of Operations* under Item 7 of this Report, the Company recorded certain non-cash asset impairment charges in 2002 associated with certain receivables and other assets relating to this customer given SMC's filing for bankruptcy protection in the U.S. in late March 2002. See *Nickel*, *Copper* and *Other Primary Metals and Related Products* below for additional information on the Company's customers.

**Competitors**

A discussion of the competitive conditions in the nickel industry appears under *Nickel* below. Competitive conditions with respect to the Company's other primary metals and related products are discussed under *Copper* and *Other Primary Metals and Related Products* below.

**Inventories**

The Company's general practice is to sell its principal primary metals products at the time of production and not to hold inventories except as necessary to meet its current sales requirements. Inco's finished nickel inventories at the end of each of the five years ended December 31, 2003 are shown in the following table:

Year-end	Inco's Finished Nickel
	(in tonnes)
1999	24,333
2000	26,582
2001	26,517
2002	23,126
2003	25,604

In recent years the minimum finished nickel inventories we generally need to run our business and meet customers' requirements have been about 26,000 tonnes, depending upon the required product mix.

**Nickel Unit Cash Cost of Sales**

Since this measure captures our key costs of production and the impact of the prices for our by-products, nickel unit cash cost of sales represents a key performance measurement that management uses to manage our costs and operations. Nickel unit cash cost of sales before by-product credits, representing a calculation equal to the total of all cash costs incurred to produce a unit of nickel before the deduction of contributions from by-products sold divided by Inco-source nickel deliveries, increased to \$4,453 per tonne (\$2.02 per pound) in 2003 from \$3,483 per tonne (\$1.58 per pound) in 2002. Nickel unit cash cost of sales after by-product credits increased to \$4,740 per tonne (\$2.15 per pound) in 2003 from \$3,197 per tonne (\$1.45 per pound) in 2002.

The increase in nickel unit cash cost of sales both before and after by-product credits in 2003 was due to the unfavourable effect of the strengthening of the Canadian dollar relative to the U.S. dollar on our costs incurred in Canadian dollars, higher energy costs at PT Inco and our Ontario operations, higher employment and pension costs, higher costs for purchasing and processing larger volumes of purchased intermediates, the ramp-up problems experienced at our Ontario operations after the three-month strike discussed below and, in the case of nickel unit cash cost of sales after by-product credits, lower contributions from by-products, primarily resulting from lower deliveries of platinum-group metals due to that strike.

A reconciliation of our nickel unit cash cost of sales before and after by-product credits to cost of sales under Canadian GAAP is shown in the table *Reconciliation of Nickel Unit Cash Cost of Sales Before and After By-Product Credits to Canadian GAAP Cost of Sales* in the Company's *Management's Discussion and Analysis of Financial Conditions and Results of Operations* set forth as Item 7 of this Report.

It is currently expected that at least some of the principal factors which have caused increases in nickel unit cash cost of sales before and after by-product credits for 2003 will continue to adversely affect such nickel unit cash costs of sales into 2004. As a result of changes in certain assumptions and actual experience of plan assets as



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well as certain legislative and regulatory requirements referred to under "Cash Flows, Liquidity and Capital Resources" in the Company's *Management's Discussion and Analysis of Financial Conditions and Results of Operations* set forth as Item 7 of this Report, we currently expect that pension expense will increase slightly from the 2003 level of \$107 million to approximately \$112 million in 2004 and, depending upon the future performance of our pension plan assets and other related factors, including changes in certain exchange rates, in particular the Canadian dollar, this expense is currently expected to remain at least at that level until at least 2005.

The Company experienced a three-month strike at our Ontario operations which began June 1, 2003. Prior to the strike, all of the Company's principal operations were operating above planned production levels for 2003. When operations resumed at the Ontario operations after the end of the three-month strike in late August 2003, we experienced a series of unanticipated problems principally at those operations' smelter and related facilities. These problems were associated with the ramp-up of those facilities after the strike and included outages or curtailments of operations at the oxygen plants and acid plant. These problems resulted in lower than planned production of in-process and finished material. Due to these problems, an expense of \$25 million was incurred during the third quarter of 2003 based upon the resulting production shortfall we experienced at those operations.

Operating costs continued to represent a major challenge for us in 2003 due to a stronger Canadian dollar, higher energy costs, increased pension expense, higher costs for purchased intermediates and lower by-product credits. Many of these cost pressures are expected to continue in 2004. We faced three key production challenges in 2003 in addition to the strike in Ontario and the ramp-up problems experienced when production resumed after the strike in September 2003; lower ore grades in Canada, in particular at the Company's Manitoba operations; adverse smelter performance at our Manitoba operations due to the processing of ores with higher magnesium oxide content, and reaching or exceeding PT Inco's expanded production design capacity. Two of these challenges were successfully met. At the Company's Manitoba operations, we modified certain facilities to address the higher magnesium oxide content of this operations' Birchtree mine ore, resulting in improved concentrate grade with no loss in recoveries. At PT Inco, we produced a record 70,200 tonnes (155 million pounds) of nickel-in-matte in 2003, exceeding PT Inco's production design capacity of 68,000 tonnes (150 million pounds) despite completion of a planned furnace rebuild in the first six weeks of the year. In 2003, improved mining and blending practices raised the ore grades at PT Inco as shown in the tables under "Ore Reserves and Mining Rights" below. Furnace throughput at PT Inco also improved based on these better ore blending practices and higher grades. At PT Inco, we also increased power available to improve throughput by enabling all five hydroelectric generators to feed all furnaces. We were able to resolve the ramp-up issues encountered at the Company's Ontario operations following the three-month strike and operations were on track in the fourth quarter of 2003.

The Company's nickel unit cash cost of sales, both before and after by-product credits, for the five years ended December 31, 2003, are shown in the following table:

Year	Nickel Unit Cash Cost of Sales Before By- Product Credits	Nickel Unit Cash Cost of Sales After By- Product Credits
	(\$ per pound)	
1999	1.29	1.26
2000	1.48	1.23
2001	1.56	1.35
2002	1.58	1.45
2003	2.02	2.15

Based upon the average exchange rate for the year, the Canadian dollar, the currency in which a substantial portion of the Company's operating costs are incurred, increased by 12 per cent relative to the U.S. dollar in 2003. In 2002, the Canadian dollar declined by one per cent relative to the U.S. dollar. At December 31, 2003, the value of the Canadian dollar, relative to the U.S. dollar, was \$0.774, compared with \$0.633 at December 31, 2002 and \$0.628 at December 31, 2001, and was \$0.748 at March 12, 2004. At December 31, 2003, the Company had outstanding forward currency contracts to purchase Cdn.\$85 million in 2004 at an average price of \$0.717. These contracts are to hedge a portion of the Company's Canadian production costs and the construction costs for the

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Voisey's Bay project and were the only Canadian dollar currency hedges that the Company had outstanding at December 31, 2003. For further information on these contracts and contracts entered into after December 31, 2003 and a discussion of the sensitivity of foreign currency exchange rates on the Company's earnings, see Voisey's Bay Nickel Company Limited Project Phases below and *Management's Discussion and Analysis of Financial Condition and Results of Operations* under Item 7 of this Report.

For information regarding the Company's profit sharing and incentive arrangements and the Company's collective agreements with its unionized employees, see Employees below.

### ***Business Segment Information***

Inco's business operations consist of two segments, its (i) finished products segment, representing the Company's mining and processing operations in Ontario and Manitoba, the refining operations in the United Kingdom and its interests in refining operations in Japan and other Asian countries referred to on page 1 of this Report, and (ii) intermediates segment, which represents PT Inco's mining and processing operations in Indonesia, where nickel-in-matte, an intermediate product, is produced and sold primarily into the Japanese market. For further information on the Company's business segments by operating segment and geographic location, see Note 19 to the financial statements under Item 8 of this Report.

### ***Nickel***

#### ***Applications for Nickel*** <sup>(1)</sup>

Nickel is a hard, malleable metal with a wide range of uses. Its principal characteristics include imparting strength and corrosion resistance in alloys. The following five general categories constitute the principal applications of nickel: the production of nickel-bearing or austenitic stainless steels, low-alloy steels, non-ferrous alloys, foundry industry castings and non-alloying uses. The Company's nickel products represent what is known in the industry as primary nickel, a designation given to nickel produced principally from nickel ores. It is estimated that approximately 81 per cent of global primary nickel consumption relates to its end use in austenitic stainless steel production and as an alloy with other metals. The other type of nickel used in industrial applications is known as secondary nickel, which is also referred to as recycled or scrap nickel. Secondary nickel units are recovered largely from austenitic stainless steel manufacturing and fabricating operations and nickel-containing scrap from obsolete plant and equipment. In the recent past, secondary nickel has represented between 43 and 48 per cent of the total nickel used for austenitic stainless steels, with primary nickel accounting for between 52 and 57 per cent of such nickel use. These percentages can vary based upon relative prices, the availability of scrap and other factors.

The nickel industry generally divides its primary nickel products into three categories: charge nickel products (products of various nickel purities produced in special forms for the stainless and low-alloy steel industries), melting nickel products (relatively pure metallic products for the non-ferrous metals and foundry industries) and plating nickel products (relatively pure metallic products in special shapes or cut to special sizes for the plating industry).

The dominant use of primary nickel in the world has continued to be in the production of nickel-bearing or austenitic stainless steels. Stainless steels, defined as iron-based alloys containing 10.5 per cent or more chromium, are typically identified by their metallurgical structure austenitic, ferritic, martensitic, precipitation-hardening and duplex. Approximately 75 to 77 per cent of global stainless steel production in recent years consists of austenitic, or nickel-bearing, grades. On average, austenitic stainless steels contain approximately eight to 10 per cent nickel. Nickel-bearing stainless steels are used throughout the industrialized world in a wide variety of applications ranging from consumer products to industrial process equipment, as well as for power generation and transportation equipment, kitchen appliances and hundreds of other applications where strength

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<sup>(1)</sup> Unless otherwise indicated, data in this Report on applications for nickel are on a global basis. Previous reports from the Company included data on a Western-World-plus-China basis. Western World is defined as the world excluding the former East Bloc countries (Russia and other members of the former Commonwealth of Independent States, China, Cuba, Bulgaria, the Czech Republic, Slovakia, Hungary, Poland and Romania).

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and corrosion resistance are required. Nickel use in nickel-bearing or austenitic stainless steels currently accounts for about 65 per cent of annual global primary nickel consumption.

A second, closely related, use of primary nickel is in low-alloy steels for construction and in structural, tool, high-strength and electrical steels. These steels are produced in greater volume than stainless steels but with a much lower nickel content, averaging less than one per cent nickel by weight. They account for about five per cent of annual global primary nickel demand.

The third category of nickel use is in non-ferrous alloys which, unlike the two categories of steel alloys noted above, contain little or no iron. These alloys, which are used in industrial process plants, marine engineering, coinage, electronics, and gas turbine engine components, as well as in other diverse products, account for approximately eight per cent of annual global primary nickel demand.

A fourth category is comprised of foundry industry castings, which consist of either iron alloys, steel alloys or non-ferrous alloys. These uses account for about three per cent of annual global primary nickel demand and represent the balance of the approximately 81 per cent of primary nickel used to make stainless steels and nickel-containing alloys.

The fifth category consists of various non-alloying uses of primary nickel. These uses account for the remaining 19 per cent of annual global primary nickel demand, and include electroplating (representing about seven per cent of primary nickel demand) and numerous applications of nickel powders, including Inco's specialty nickel powder products described under Inco Special Products below. Many consumer durable goods, such as metal furniture, are nickel-chrome electroplated. Nickel powder applications are a relatively small but important nickel-consuming sector. Given the properties of nickel powders, applications include dissolving nickel into salts for plating and catalysts for the petrochemical industry, and use in nickel-cadmium and nickel-hydride rechargeable batteries, welding electrodes, metal sprays and specialized parts made by powder metallurgy.

As indicated above, nickel used in stainless and low-alloy steel sectors account for approximately 70 per cent of annual global primary nickel demand. In choosing primary nickel, these two sectors can generally use either charge nickel products or melting nickel products to satisfy their nickel requirements; however, they may also use secondary nickel units such as nickel-containing stainless steel scrap or other recycled nickel-containing material, with the selection being based largely on relative prices and availability of these materials. See Prices Nickel above for a discussion of the percentages of nickel consumed as stainless steel scrap by stainless steel producers.

Inco has been a member of the Nickel Development Institute ( NiDI ), a non-profit association which promotes applications for nickel, since NiDI was founded in 1984. NiDI sponsors numerous research and development projects, including projects aimed at promoting the use of nickel-containing stainless steels, broadening markets for nickel-containing alloys resistant to high and low temperatures, high pressures and corrosion, and seeking to ensure that sound science is used as the basis for regulatory developments relating to the production and use of nickel and nickel-containing products and the recycling or disposal of nickel-containing waste materials. In early 2004, NiDI and the Nickel Producers Environmental Research Association ( NiPERA ), an organization that we and other nickel producers had formed in the 1980s to fund scientific studies relating to, and focus on, environmental, health and other issues with respect to various forms of nickel, merged to form the Nickel Institute.

### *Historical Review of the Nickel Industry; Recent Industry Conditions<sup>(2)</sup>*

The nickel market has been cyclical in nature over the past half-century given the positive correlation of nickel demand to industrial production.

Primary nickel demand in the Western World grew significantly during the 1946-1974 period in response to postwar reconstruction, increased per capita incomes and the rapid growth of the stainless steel industry. Annual

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<sup>(2)</sup> Data and estimates included in this historical review through 2002 are limited to the Western World because of limited available data for certain countries. See Note 1 above with respect to our definition of Western World.

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demand increased from approximately 136,100 tonnes in 1950 to a then record level of approximately 620,000 tonnes in 1974. The compound rate of annual growth in nickel demand over the 1946-1974 period was about six per cent.

With the oil crisis in 1973, the substantial rise in energy costs resulted in a reduction in industrial production and a consequent reduction in primary nickel demand. These negative trends were repeated in the early 1980s following a second round of significant oil price increases in 1979-1980, but were reversed in the second half of the 1980s, when a period of strong industrial growth resulted in an increase in the demand for nickel.

Record growth in stainless steel production, accompanied by a shortage of nickel production, placed significant upward pressure on LME cash nickel prices in 1988 and 1989, with these prices averaging \$13,823 per tonne (\$6.27 per pound) and \$13,338 per tonne (\$6.05 per pound), respectively, for 1988 and 1989.

During the early 1990s, significant increases in primary and secondary nickel deliveries to the world from the Russian Federation ( Russia ) and other members of the former Commonwealth of Independent States ( CIS ), combined with economic downturns in North America, Western Europe and Japan, led to a surplus in primary nickel supply, resulting in a weakening of nickel prices. This situation was exacerbated in 1992 and 1993 by negative economic growth in Western Europe and Japan and continued exports of nickel from the CIS. From 1990 to 1993, annual average LME cash nickel prices fell from \$8,885 per tonne (\$4.03 per pound) to \$5,291 per tonne (\$2.40 per pound).

In 1994 and 1995, a worldwide economic recovery led to strong growth in stainless steel production and nickel demand, resulting in primary nickel demand exceeding supply and a recovery in nickel prices, with the LME cash nickel price rising to an average of \$8,231 per tonne (\$3.73 per pound) for 1995.

In the latter half of the 1990s, strong economic growth led to significant increases in stainless steel production and nickel demand, except that the Asian economic crisis in 1998 caused overall nickel demand to decrease slightly that year. The decrease in the demand for nickel during 1998, combined with the market's anticipation of large supplies of low-cost nickel from the three new Australian laterite projects, Murrin Murrin, Bulong and Cawse, resulted in the LME cash nickel price reaching a low for the decade of \$3,725 per tonne (\$1.69 per pound) in December 1998. Nickel prices recovered during 1999, supported by the resumption of strong economic and nickel demand growth, with the LME cash nickel price reaching \$8,450 per tonne (\$3.83 per pound) at the end of 1999.

The LME cash nickel price continued to increase into 2000, reaching a peak of \$10,660 per tonne (\$4.84 per pound) in March 2000 but, subject to some variability, over the balance of 2000 declined to \$7,190 per tonne (\$3.26 per pound) by the end of the year. Solid market conditions contributed to the increase in the average LME cash nickel price to \$8,642 per tonne (\$3.92 per pound) in 2000, as did the anticipation of possible labour disruptions at certain producers which did not materialize. The world economic recovery that commenced in 1999 continued in 2000, resulting in increased demand for nickel-containing products, especially stainless steel where world production of this material on a world basis increased in 2000 by 8.8 per cent to a record level of 19.5 million tonnes. However, the use of primary nickel in this segment registered no growth in 2000 due to the increased supply of nickel-containing stainless steel scrap, which led to an increase in the scrap ratio to 48 per cent in 2000 from 44 per cent in 1999. Overall world demand for primary nickel grew by 5.8 per cent in 2000 to a record level of 1,109,000 tonnes, reflecting both stock building by consumers, who were replenishing their inventories from the relatively low levels at the end of 1999, and an estimated 12 per cent growth in consumption for primary nickel in applications other than stainless steel.

In 2000, world primary nickel supply production increased by an estimated 78,000 tonnes to 1,105,000 tonnes, due mainly to a rise in primary nickel production in the Western World of approximately 52,000 tonnes, reflecting the return to more normal levels of production by several producers who either had experienced unexpected production disruptions or reduced output in 1999, and production from new nickel capacity and the continued commissioning of the three new laterite projects in Australia referred to above. Demand for nickel in 2000 exceeded supply by approximately 4,000 tonnes, but we believe that additional material was withheld from the market by one leading nickel producer, thereby reducing apparent stocks to critically low levels, as reflected in nickel inventories held in LME warehouses, which fell by over 37,000 tonnes during the year.



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The nickel market in 2001 was a challenging one compared with 2000 when total world demand for primary nickel achieved a record level. Market fundamentals weakened during 2001 as the world's major economies experienced softness and recessionary conditions intensified in the manufacturing sectors of virtually all of the major countries that are members of the Organization for Economic Cooperation and Development (OECD). This overall weakness in demand was primarily concentrated within the Western World where nickel demand declined significantly. While there was continued strength in nickel demand in China in 2001, the Company estimates that there was an overall decline in world nickel demand in 2001 of 2.2 per cent to approximately 1,085,000 tonnes. Growth in world primary nickel production continued in 2001, reflected in a net increase of 40,000 tonnes to 1,145,000 tonnes. The largest sources of this increase in supply were the continued ramping up of certain laterite projects in Australia and the commissioning of new capacity in Venezuela and Colombia. With the decline in demand and increase in supply, the world nickel market in 2001 shifted to a surplus position of approximately 60,000 tonnes following the deficit positions in the previous two years. Over 2001, nickel inventories held by consumers are estimated to have fallen by 13,000 tonnes and despite the slowdown LME inventories increased by only 9,510 tonnes, with such inventories ending 2001 at 19,188 tonnes.

The cash nickel price on the LME opened 2001 at \$6,995 per tonne (\$3.17 per pound) but, subject to some variability, declined to the year's low of \$4,420 per tonne (\$2.00 per pound) in late October 2001. With the aggressive reduction of interest rates in the United States and renewed prospects for an economic recovery, prices for nickel and other non-ferrous metals improved in the fourth quarter of 2001 and the LME cash nickel price had increased to \$5,680 per tonne (\$2.58 per pound) as of December 31, 2001.

The nickel market strengthened in 2002 as demand, on a world basis, grew by approximately eight per cent during the year to 1,168,000 tonnes despite continued weakness in certain large segments of the global economy. During 2002, growth in industrial production continued in China and rebounded in most major Asian economies, excluding Japan, while economic recovery in the United States, Europe and Japan struggled to take hold.

The growth in nickel demand in 2002 was primarily concentrated in the stainless steel sector. Nickel demand growth in this sector increased by almost 10 per cent, driven by an increase in stainless steel production and a decline in the percentage of nickel-containing stainless steel scrap relative to primary nickel consumed by stainless steel producers. World stainless steel production increased by 7.9 per cent to approximately 20.3 million tonnes with growth experienced in all major industrial countries of the world except Japan where production declined slightly. This production growth was particularly strong in the United States, up 20 per cent, driven by the opening of a new 800,000 tonne-per-year stainless steel production facility in Kentucky and higher production at existing facilities elsewhere in the United States, and in Taiwan, where production increased by 20 per cent as existing facilities operated at near-capacity levels.

Growth in primary nickel supply continued in 2002 as several relatively new or greenfield projects located in South America and Australia continued to increase production to their expected design capacities. The overall increase in nickel supply in 2002 came principally from (1) Colombia and Venezuela, where new or greenfield projects were completing their ramp-up to their design capacities, (2) Australia, where production increased from the continued ramp-up of one project and higher production from certain existing producers, and (3) Japan, where production in the form of ferronickel rebounded to near-capacity levels.

The LME cash nickel price opened 2002 at \$5,680 per tonne (\$2.58 per pound) and increased during the first half of 2002 as the economies of certain industrialized countries began to recover from their relatively low fourth quarter 2001 levels, ending the first half of the year at \$7,080 per tonne (\$3.21 per pound). Prices declined through the third quarter, reaching a low of \$6,305 per tonne (\$2.86 per pound) in September 2002 as concern over the pace of economic recovery and uncertainty about a potential war with Iraq adversely affected the nickel markets. The LME cash nickel price recovered in the fourth quarter, underpinned by improving fundamentals for nickel, ending 2002 at \$7,100 per tonne (\$3.22 per pound).

The strong growth in nickel demand during 2002, largely offset the growth in nickel production, resulting in an essentially balanced market for 2002 as it is estimated by Inco that the world market reflected a small surplus of approximately 3,000 tonnes. Inventories of nickel on the LME increased slightly during 2002 by 2,784 tonnes, remaining at a relatively low level of 21,972 tonnes at December 31, 2002.

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The global nickel market reflected favourable fundamentals for nickel producers such as ourselves in 2003 as world demand grew by approximately seven per cent from 2002 levels to 1,251,000 tonnes despite continued economic weakness in Europe and a delayed economic recovery in the United States. Industrial production in Asia grew during 2003, led by continued significant growth in China, as well as growth in South Korea, Taiwan and Japan. The global nickel market was essentially in balance for 2003 as a result of the release into the market of approximately 60,000 tonnes (132 million pounds) of nickel or about five per cent of total global nickel supply that we understand one leading nickel producer had initially pledged as collateral for a loan.

The growth in nickel demand in 2003 was concentrated in the stainless steel sector, the largest end user of primary nickel. Nickel demand growth in this sector increased by almost eight per cent in 2003, driven by a significant increase in stainless steel production and a decline in the stainless steel scrap-ratio. The world production of stainless steel increased by nine per cent to approximately 22 million tonnes in 2003. This growth was due, in part, to increases in production capacity and the start-up of several new large-scale stainless steel manufacturing facilities around the world. Stainless steel production expanded in all major industrial regions and was particularly strong in China and South Korea where new production facilities were commissioned during the year. Nickel demand growth in non-stainless steel applications was relatively weak in 2003, as one important end-use market, high nickel alloys for the aerospace industry, continued to struggle with new aircraft orders remaining at relatively depressed levels. However, demand for nickel in plating applications was relatively strong, led by growth in these applications in China, slightly offset by reduced demand for these applications in Europe and the United States.

The growth in world supply of primary nickel in 2003 could not keep pace with the demand growth experienced in 2003. Supply of primary nickel in 2003 was adversely affected by a strike at the Company's Ontario operations during a three-month period beginning June 1, 2003 which resulted in effectively no production from these operations which would normally produce about 20 million pounds of primary nickel per month. We believe that several other major producers failed to reach their 2003 projected production targets due to unexpected maintenance or operational problems. The shortfall in supply was partially offset by the gradual release of approximately 60,000 tonnes into the market during 2003 by one leading nickel producer, as discussed above. In addition, production of ferronickel in Australia, New Caledonia, Colombia and the Dominican Republic increased in 2003. As a result, world primary nickel production increased by 21,500 tonnes to 1,192,000 tonnes in 2003. World primary nickel supply increased to 1,192,000 tonnes taking into account the release of the 60,000 tonne loan collateral mentioned above.

The significant growth in nickel demand during 2003, coupled with the limited supply growth, created an underlying deficit between supply and demand in 2003 of approximately 59,000 tonnes. With the release of the 60,000 tonne loan collateral referred to above, we believe there was a small surplus in the global nickel market of approximately 1,000 tonnes in 2003. Inventories of nickel on the LME, a physical market (i) where various metals, including nickel, can be bought or sold for prompt or future delivery and (ii) representing the principal terminal market for primary nickel in the world, increased slightly during 2003 by 2,100 tonnes, remaining at a relatively low level of 24,072 tonnes at December 31, 2003. As of March 12, 2004, given the significant drawdown in these reported inventories during the first nearly two and one-half months of 2004, LME inventories totalled 14,316 tonnes.

An uncertain global economic environment would be expected to have a significant adverse effect on Inco's business and financial results given the historical positive correlation between industrial production and demand for primary nickel and the Company's other products. There can be no assurance that the over supply situations which have existed historically in the nickel markets could not reoccur in the future. Any such conditions would have an adverse effect on the prices realized by Inco for its nickel products. Other international economic trends, expectations of inflation and political events in major nickel producing and consuming countries can also adversely affect nickel prices and the prices of other metals produced by the Company. These factors are beyond the Company's control and have resulted, and are expected to continue to result, in a high degree of price volatility for nickel and other primary metals produced by Inco. There can be no assurance that the price for nickel or other metals produced by Inco will not decline. A return to the relatively low price of nickel reflected by the LME cash nickel price which prevailed through most of 1998 and into the first half of 1999 and during a

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portion of the second half of 2001 would have a material adverse effect on the Company's results of operations, financial condition, cash flows and liquidity.

World primary nickel demand has increased at an average compound annual rate of approximately six per cent over the last ten years. As noted under "Applications for Nickel" above, about two-thirds of world primary nickel demand is associated with the production of austenitic stainless steels. The following table shows the relationship between Inco's most recent estimates of world primary nickel demand and stainless steel production for the five years ended December 31, 2003:

Year	World Primary Nickel Demand <sup>(1)</sup>	World Stainless Steel Production
	(in tonnes)	(in millions of tonnes)
1999	1,048,000	17.9
2000	1,109,000	19.5
2001	1,085,000	18.8
2002	1,168,000	20.3
2003 <sup>(2)</sup>	1,251,000	22.0

(1) Previously disclosed figures were provided on a Western World-plus-China basis.

(2) Preliminary estimates.

The following table shows Inco's most recent estimates of world primary nickel demand, world primary nickel supply, year-end combined Western World producers and LME inventories of primary nickel year-end LME nickel inventories and the average annual LME cash nickel prices for the five years ended December 31, 2003:

Year	World Primary Nickel Demand	World Primary Nickel Supply	Year-End Combined Western World Producers and LME Inventories <sup>(2)</sup>	Year-End LME Inventories	Average Annual LME Cash Nickel Prices
	(in tonnes)				(\$ per tonne)
1999	1,048,000	1,027,000	120,000	46,962	\$ 6,015
2000	1,109,000	1,105,000	90,000	9,678	8,642
2001	1,085,000	1,145,000	106,000	19,188	5,948
2002	1,168,000	1,171,000	100,000	21,972	6,775
2003	1,251,000(1)	1,192,000(1)	104,000(1)	24,072	9,633

(1) Preliminary estimates.

(2) Excludes Russia, other members of the former CIS, China, Cuba and Eastern Europe.

Future nickel consumption and nickel prices could be adversely affected by a number of factors, including the development of new nickel capacity, such as the new capacity described below under "Participants in the Nickel Industry"; new processing technologies which have made, and are expected to continue to make, the development of relatively low-grade lateritic nickel deposits economically viable; decreases in the general level of economic and business activity in industrial economies which, in turn, could lead to reduced production of stainless steel; levels of nickel-containing stainless steel scrap and other sources of secondary nickel; increased environmental restrictions affecting the production and use of nickel and nickel-containing products; recommissioning of any currently remaining shutdown nickel capacity; and, in the longer term, increased use of substitutes, including plastics and ceramics, for nickel-containing materials. In addition, the future levels of production and consumption of nickel in Russia are expected to continue to have significant, but unpredictable, effects on world nickel prices.

*Participants in the Nickel Industry*

The six largest suppliers in the nickel industry, each having its own integrated facilities, including nickel mining, processing, refining and marketing operations, are MMC Norilsk Nickel (Norilsk), Inco, Falconbridge



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Limited ( Falconbridge ), BHP Billiton plc ( BHP Billiton ), Eramet and its subsidiary, Le Nickel-SLN (collectively, Eramet ), and WMC Resources Ltd. ( WMC ). The Company estimates that these six producers accounted for about 60 per cent of the total world primary nickel production in 2003. In addition to these six principal participants, there are approximately 30 other producers in numerous other countries around the world that participate in the nickel industry. Operations of the six largest producers are located in several countries. Inco, as noted on page 1 of this Report, has operations in Canada, the United Kingdom, Indonesia, Japan and China and in other parts of Asia through two companies, Taiwan Nickel and Korea Nickel, in whose refining capacity Inco has interests, but less than majority ownership. Norilsk has operations in Russia; WMC has operations in Australia; Falconbridge has operations in Canada, Norway and the Dominican Republic; Eramet has operations in France and New Caledonia; and BHP Billiton has operations in Australia and Colombia.

Norilsk has integrated facilities at Norilsk in Siberia and at Pechenga and Severonickel on the Kola Peninsula of Russia. For 2003, Norilsk reported production of approximately 238,000 tonnes of nickel from all of its facilities, compared with 218,000 tonnes in 2002 and 228,000 tonnes in 2001, and exports of 239,000 tonnes in 2003, compared with 208,000 tonnes in 2002 and 182,000 tonnes in 2001.

World primary nickel supply is estimated by Inco to have been approximately 1,192,000 tonnes in 2003, up 1.8 per cent from approximately 1,171,000 tonnes in 2002 and 1,145,000 tonnes in 2001. Production increases during 2003 were mainly from Norilsk in Russia, Jinchuan Group Limited in China, BHP Billiton's Cerro Matoso operation in Colombia, Falconbridge's operations in Canada and Norway and its Falcondo subsidiary's ferronickel operations in the Dominican Republic. However, these increases were largely offset by lost production due to the three-month strike at our Ontario operations.

*Inco's Position in the Nickel Industry*

Inco is a leading producer of nickel. The Company's nickel deliveries in 2003 represented an estimated 17 per cent of the total world demand for primary nickel, compared with 20 per cent in 2002 and 21 per cent in 2001.

Inco's total deliveries of nickel in 2003 were 213,890 tonnes, representing a decrease of eight per cent from total deliveries of 231,590 tonnes in 2002. Deliveries by Inco in 2003 of nickel produced at its own facilities were 184,110 tonnes, representing a decrease of 13 per cent from deliveries of 212,247 tonnes in 2002. The decrease in deliveries was primarily due to lower production at the Company's Ontario operations as a result of the three-month strike referred to above which was partially offset by higher nickel deliveries from PT Inco and the Company's Manitoba operations and an increase in the deliveries of purchased finished nickel. The Company's Ontario operations normally produce about 9,000 tonnes (20 million pounds) of nickel products per month. Deliveries of finished nickel purchased from external sources, used by the Company to supplement Inco-source production as required, increased by 54 per cent in 2003 as a result of the three-month strike referred to above.

In 2002, Inco's total deliveries of nickel increased slightly to 231,590 tonnes from total deliveries of 230,049 tonnes in 2001. Deliveries by Inco in 2002 of nickel produced at its own facilities were 212,247 tonnes, representing an increase of two per cent from deliveries of 207,071 in 2001, due to increased production of finished nickel and sales from finished nickel inventories. Deliveries of finished nickel purchased from external sources, used by the Company to supplement Inco-source production as required, declined in 2002 as a result of higher Inco production in 2002.

The Company believes that one of the key strengths of its position in the highly-competitive global nickel industry is the broad geographic distribution of its customers. In 2003, the Company continued to supply its customers worldwide from its operations in Canada, the United Kingdom and Asia. In 2003, reflecting the Company's global market presence, 21 per cent of the Company's total primary nickel deliveries were to customers in the United States and Canada, 25 per cent to customers in Japan, 12 per cent to customers in Europe, and 42 per cent to customers in other countries, primarily in Asia, compared with 26 per cent to customers in the United States and Canada, 24 per cent to customers in Japan, 12 per cent to customers in Europe, and 38 per cent to customers in other countries, primarily in Asia, in 2002. In 2003, sales to customers in Asia, including Japan, represented 66 per cent of the Company's total nickel deliveries for the year, compared with 60 per cent in 2002.

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In 2003, the Company continued to implement marketing strategies aimed at providing consistent long-term demand for its products. At year-end 2003, the Company had fixed-volume contracts with customers for a substantial portion of its expected annual nickel sales. These contracts, combined with the requirements of the Company's affiliated refineries in Asia and its sales of proprietary nickel products, have continued to provide stable demand for a significant portion of the Company's annual production.

The three-month strike at the Company's Ontario operations and the ramp-up problems experienced when those operations were restarted after the end of the strike, as discussed above, significantly and adversely affected the Company's production of primary nickel products, copper, platinum-group metals and its other products.

The following table shows, for the five years ended December 31, 2003, Inco's most recent estimates of total world primary nickel demand, Inco's total nickel deliveries, Inco's deliveries of purchased nickel, Inco's estimated share of world demand based on its total nickel deliveries, the LME average cash and three-month nickel prices and Inco's average realized price for its primary nickel products:

Year	World Primary Nickel Demand	Total Inco Deliveries <sup>(1)</sup>	Inco Deliveries of Purchased Nickel	Inco Share of World Demand	LME Average Cash Nickel Price	LME Average 3-Month Nickel Price	Inco Average Realized Nickel Price <sup>(1)</sup>
		(in tonnes)		(%)			(\$ per tonne)
1999	1,048,000	258,088	77,038	25	6,015	6,073	6,415
2000	1,109,000	259,374	60,277	23	8,642	8,453	9,007
2001	1,085,000	230,049	22,978	21	5,948	5,877	6,468
2002	1,168,000	231,590	19,343	20	6,775	6,755	7,143
2003	1,251,000(2)	213,890	29,780	17(2)	9,633	9,610	9,860

(1) Includes intermediates and purchased nickel.

(2) Preliminary estimates.

*Inco Special Products*

The Company is a world leader in the development, production and sale of value-added or specialty nickel products, including powders, foams, flakes, oxides and nickel-coated graphite. These products are used for such applications as consumer electronics, rechargeable batteries for consumer and hybrid vehicle use, fuel cells, powder metallurgy, automotive parts, electromagnetic interference shielding for computers and cellular telephones, special catalysts and salts, metal injection moulding, and hard metal binders.

Inco Special Products, an unincorporated business unit, has responsibility for all business activities related to the Company's value-added or specialty nickel products. Inco's value-added or specialty nickel products are developed at the Company's research laboratory at Mississauga, Ontario and are manufactured, using the Company's gas decomposition technology, at the Company's refineries in Sudbury, Ontario and Clydach, Wales; and certain value-added or specialty products are also manufactured at Novamet<sup>(3)</sup> Specialty Products Corporation (Novamet), a wholly-owned subsidiary of the Company located in Wyckoff, New Jersey. Inco Special Products expects to continue to work closely with customers to develop advanced nickel products to meet their needs. Accounting for approximately nine per cent of the Company's nickel sales revenue in 2003, compared with 12 per cent in 2002 and 2001, value-added or specialty nickel products sold at premium prices. These premiums are affected by fluctuations in the LME cash nickel price and how the Company prices certain of its value-added or specialty nickel products.

*Copper*

Inco produces copper at its Ontario operations which it recovers, in conjunction with nickel, principally from the sulphide ores mined in the Sudbury area of Ontario. In 2003, the Company's copper production was 91,134 tonnes, representing a decrease of 18 per cent from 111,787 tonnes in 2002. Copper production in 2003 was

(3) Inco trademark.

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below the Company's planned target of 113,000 tonnes due to the three-month strike and ramp-up problems associated with the restart of operations after the three-month strike at the Company's Ontario operations. In 2002, the Company's copper production was down four percent from 116,255 tonnes in 2001, due to production and mechanical difficulties experienced during the year at the Company's Ontario operations.

The Company's copper is sold to industrial users under the trademark ORC<sup>(4)</sup>. In 2003, all of the Company's copper production was sold in North America at prices based on quotations on the COMEX Division of the New York Mercantile Exchange. Copper accounted for \$171 million, or seven per cent, of the Company's total net sales to customers in 2003, compared with \$184 million, or nine per cent, in 2002 and \$195 million, or nine per cent, in 2001.

The Company's sales and deliveries (including purchased copper) for the past three years and the Company's average realized prices for copper for the past five years are shown in the tables under Sales, Deliveries and Prices - Copper above, respectively.

World refined copper production is estimated to have been approximately 15.2 million tonnes in 2003, compared with 15.5 million tonnes in 2002 and 15.3 million tonnes in 2001.

Like nickel prices, copper prices have been in recent years, and are expected to continue to be, subject to significant price volatility. In 2002, LME and COMEX inventories continued to increase until they peaked in the second quarter as a result of production cutbacks announced during the fourth quarter of 2001 and higher demand, particularly from China, which began to have a positive impact on the overall copper market supply-demand balance. Prices also peaked in the second quarter and declined during the remainder of the year as economic uncertainty and a lack of demand growth negatively affected overall copper market sentiment. Total LME and COMEX inventories ended the year at 1,255,000 tonnes, an increase of 25 per cent from these combined inventory levels at the end of 2001, but lower than the peak of 1,306,000 tonnes for 2002 reached in the second quarter. In 2003, the combination of strong economic growth in Asia, in particular China, combined with a number of production cutbacks and the actions of one leading copper producer which we understand stockpiled material, led to accelerating declines in reported stocks throughout 2003. By the end of 2003, reported copper stocks on the COMEX and the LME declined by over 40 per cent to 711,100 tonnes. The COMEX first position price averaged \$1,787 per tonne (\$0.81 per pound) in 2003, a 13 per cent increase from \$1,580 per tonne (\$0.72 per pound) in 2002, and was \$2,886 per tonne (\$1.31 per pound) on March 12, 2004.

***Other Primary Metals and Related Products***

Sales of Inco's primary metals and related products other than nickel and copper accounted for eight per cent of its total net sales to customers in 2003, compared with 15 per cent in 2002 and 19 per cent in 2001. These products include cobalt, platinum-group metals (platinum, palladium, rhodium, ruthenium and iridium), gold, silver, sulphuric acid and liquid sulphur dioxide and some modest quantities of selenium and tellurium. For 2003, Inco, based upon production principally from its Ontario ores, accounted for approximately two per cent of the world's supply of platinum-group metals. Platinum-group metals are utilized primarily for catalysts, electronic components and jewelry. In addition to refining its own ores to obtain platinum-group metals, the Company processes substantial volumes of spent automotive catalytic converters and other material containing these metals at its Sudbury, Ontario and Acton, England refineries. In 2003, due principally to the post-strike ramp-up problems discussed above at the Company's Ontario operations, such other material, which was principally toll-refined, accounted for about 76 per cent of all platinum-group metals refined by the Company, compared with 60 per cent in 2002 and 69 per cent in 2001. Deliveries of toll-refined material, however, are not included in the Company's deliveries of precious metals shown in the table under Deliveries above since Inco does not take ownership of these materials. As a result primarily of the reduced quantities of platinum-group metals produced by the Company given the three-month strike, sales of platinum-group metals accounted for approximately four per cent of the Company's net sales to customers in 2003, compared with 11 per cent in 2002 and 13 per cent in 2001. The platinum-group metals sold in 2003 were derived principally from the Company's Ontario ores.

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(4) Inco trademark.

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Approximately 80 per cent of Inco's cobalt production, which is derived from the Company's Canadian ores and purchased feedstock material, is sold as metal, with the balance being sold as cobalt oxide. Cobalt oxide, which normally commands a price premium over cobalt metal, is used primarily in the chemical industry. Cobalt metal is used in the production of various alloys, particularly for aerospace applications.

Copper and nickel producers supply a majority of the world's cobalt production as a by-product of their copper and nickel operations, which has resulted in the supply of cobalt being largely driven by the demand for copper and nickel rather than the demand for cobalt. As a result, there has been a significant increase in the supply of cobalt in the last decade. Demand for cobalt from the aerospace and land-based gas turbine sectors, which together currently represent about 23 per cent of world cobalt consumption, continued to be weak in 2003. However, in 2003 the total demand for cobalt increased as a result of the growth of applications for cobalt in the battery and catalyst market sectors. The increases in cobalt demand as a result of these applications, together with supply disruptions, resulted in a more balanced market. With supply and demand moving closer into balance during 2003, the Metal Bulletin 99.8 per cent average reference price for cobalt, the most commonly used benchmark price for cobalt pricing, averaged \$19,330 per tonne (\$8.77 per pound) in the first half of the year and \$26,570 per tonne (\$12.05 per pound) in the second half of the year, compared with \$15,700 per tonne (\$7.10 per pound) in 2002 and \$23,300 per tonne (\$10.60 per pound) in 2001. On March 11, 2004, the Metal Bulletin 99.8 per cent average reference price for cobalt was \$60,627 per tonne (\$27.50 per pound).

As indicated in the table of the Company's price realizations under Prices - Other Metals above, Inco's average realized price for its cobalt deliveries was \$18,846 per tonne (\$8.55 per pound) in 2003, compared with \$15,124 per tonne (\$6.86 per pound) in 2002 and \$23,216 per tonne (\$10.53 per pound) in 2001. The Company's Goro and Voisey's Bay projects, in addition to the quantities of nickel projected to be produced by them, are also expected to produce significant quantities of cobalt given the currently estimated quantities of cobalt in the mineral deposits to be mined as part of these projects. With significant increases in the global supply of cobalt and changes in demand, the price of cobalt has fluctuated significantly over the past several years. The financial analyses undertaken by the Company in support of the substantial investment to be made with respect to these projects have been based upon a long-term price of cobalt of \$15,400 per tonne (\$7.00 per pound). If realized cobalt prices, as well as realized prices for the other metals to be produced by these projects, were to be below the long-term prices assumed by the Company, the expected financial returns from, and expected cash and other unit costs of production after by-product credits for, these projects would be adversely affected.

The Company also produces sulphuric acid and liquid sulphur dioxide from the sulphur dioxide gases captured as part of its sulphur dioxide (SO<sub>2</sub>) abatement program at the Company's Ontario operations. A total of 473,805 tonnes of sulphuric acid and liquid sulphur dioxide were produced by the Company in 2003, compared with 673,995 tonnes in 2002 and 650,651 tonnes in 2001. Most of the Company's sulphuric acid production and all of its liquid sulphur dioxide production are sold to Chemtrade Logistics Inc., an unaffiliated customer, under long-term contractual arrangements at prices based on prevailing market prices for these products. These products are included in the table of product deliveries under Deliveries above.

Tables showing the Company's sales, deliveries and average net realized prices of these other primary metals and related products are shown under Sales, Deliveries and Prices - Other Metals above.

***Mining and Production******General***

Based on publicly available information and its own studies and analysis, the Company believes that, relative to other nickel producers, it is a low-cost producer of nickel. Since low-cost operations are essential in the highly competitive global nickel business, one of Inco's key strategic objectives is to become the world's lowest-cost and most profitable producer of nickel. A number of favourable factors, as described below, generally contribute to the Company's current cost structure, with the contribution of each factor varying from year to year. A number of other nickel producers experienced some of the same cost pressures we did in 2003, including higher energy costs and the impact of the strengthening in the currency which some or all of their costs of production are incurred relative to the U.S. dollar, the currency in which most or at least some of their revenue is received.



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The Company's estimated ore reserves include both sulphide and laterite nickel deposits, the two main types of nickel deposits found in the world. Sulphide deposits currently account for about 30 per cent of the world's nickel resources and are found in bedrock, often deep below the surface which generally make them more costly to mine than laterite deposits. Sulphide deposits commonly contain copper, precious metals and cobalt in addition to nickel. Laterite deposits, which currently account for the remaining 70 per cent of the world's nickel resources, occur as either wet laterites or dry laterites. Wet laterites are found in tropical areas where heavy rainfall combined with suitable landforms have resulted in the concentration of nickel through a process of surface weathering and leaching action. Currently, wet laterites may be processed by using either smelting or acid leaching technology, depending on the characteristics of the particular deposit. Dry laterites, such as those found in Australia, may be processed only by using acid leaching technology due to their mineralogy and their generally lower nickel content compared with wet laterites. Laterite deposits are found at or near the surface and are therefore usually amenable to low-cost surface mining. Cobalt is also usually present in these deposits.

The Company has large sulphide orebodies with satisfactory ore grades and metallurgical properties principally at its operations at Sudbury, Ontario and certain sulfide orebodies with generally declining ore grades at its Thompson, Manitoba operations, and large lateritic orebodies with satisfactory ore grades and metallurgical properties at its operations in Indonesia. In addition to nickel, Inco recovers significant quantities of copper, precious metals and cobalt from its Ontario ores. The relative economic advantages of Inco's Canadian sulphide ores are offset, to some degree, by the higher mining costs for sulphide ores relative to lateritic ores and by higher costs of doing business in Canada relative to some other nickel-producing countries. The Company's unit costs of production also benefit from economies of scale attributable to its large, integrated mining and processing facilities and from the use of bulk mining methods and automated mining equipment and other productivity improvements implemented in recent years in all areas of the Company's business.

Energy costs are a significant component of production costs in the nickel industry since nickel production is highly energy intensive, especially in respect of the pyrometallurgical processing of lateritic ores. Inco enjoys relatively low energy costs because of substantial production from its Canadian sulphide ores, which consume only about one-fifth the energy required to process lateritic ores. In addition, low-cost energy is available from the Company's hydroelectric facilities in Ontario and at PT Inco's lateritic mining operation in Indonesia, and from purchased hydroelectric power at the Company's Manitoba operations.

In 2003, our hydroelectric facilities in Ontario generated approximately 22 per cent of the Company's Ontario operations' electricity requirements, and PT Inco's 165-megawatt hydroelectric-generating facility at its Larona dam together with its 93-megawatt hydroelectric generating facility at its Balambano dam generated virtually all of PT Inco's 2003 electrical requirements. The Balambano facility has been able to generate power consistently above its design capacity due to improved water management practices and higher reservoir levels and other related factors than were assumed in developing its original design capacity. In 2003, energy costs at the Company's Ontario and Manitoba operations were approximately 14 per cent of total cash production costs, compared with 36 per cent for PT Inco. The availability of captive hydroelectric power decreased cash energy costs at PT Inco by about 51 per cent in 2003, 47 per cent in 2002 and 50 per cent in 2001 relative to the energy costs that would have been incurred by PT Inco if fuel oil had been the sole source to meet its energy requirements.

Inco's Ontario operations benefit significantly, and its Company's Manitoba operations benefit to a minor extent, from the copper, precious metals and cobalt produced in association with nickel. In 2003, Ontario ores accounted for approximately 96 per cent of the Company's copper production, 94 per cent of its by-product platinum-group metals production and 48 per cent of its by-product cobalt production, with one per cent of the Company's copper production, six per cent of its by-product platinum-group metals production and 34 per cent of its cobalt by-product production derived from the Company's Manitoba ores. The Company also produces nickel, copper, cobalt and precious metals from purchased materials. Precious metals have relatively high selling values compared with the Company's processing costs for these metals. Inco's accounting and financial reporting practice is to include revenues from deliveries of copper, precious metals and cobalt in net sales and to include costs of recovering such metals in cost of sales. Copper is considered to be a joint product with nickel and, as such, its production costs include an allocation of mining costs plus its identifiable concentrating, smelting and refining costs; precious metals and cobalt are considered to be by-products and, as such, their production costs

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include no allocation of mining, concentrating and smelting costs, but do include their identifiable upgrading and refining costs.

The Company's nickel production decreased by 11 per cent to 187,173 tonnes in 2003, compared with 209,728 tonnes in 2002, reflecting lower production at the Company's Ontario operations due to the three-month strike by production workers, ramp-up problems following the strike, and completion of a planned furnace rebuild at PT Inco in the first quarter, partially offset by higher production at the Company's Manitoba operations, the processing of higher volumes of purchased intermediates, and higher ore grades and higher production at PT Inco. In 2002, the Company's nickel production increased by one per cent to 209,728 tonnes from 207,077 tonnes in 2001. The increase was primarily due to the decision to operate the Company's Ontario operations in 2002 without any planned maintenance shutdown. Nickel production in 2002 was, however, below the Company's planned production of 213,000 tonnes that it had announced in February 2002. Our Manitoba operations in 2002 and early 2003 were adversely affected by start-up problems concerning the 1-B orebody of the Thompson mine and the adverse effect on processing operations of the higher magnesium oxide ( MgO ) content in the ores mined from the Manitoba operations' Birchtree mine. These issues were resolved in 2003. Production of finished nickel from Canadian ores and purchased material processed in Canada totalled 120,479 tonnes in 2003, compared with 146,620 tonnes in 2002 and 145,221 tonnes in 2001. Additional nickel and copper production statistics for the Company's primary metals operations are shown in the tables under Concentrating, Smelting and Refining below. For a discussion of PT Inco's operating rates and estimated ore reserves, see PT International Nickel Indonesia Tbk Operations below.

The Company's 2004 nickel production is currently expected to be in the range of 227,000 to 231,000 tonnes, up substantially from the 187,173 tonne level in 2003. Nickel production in 2003 was negatively impacted by the strike at our Ontario operations. The Company expects purchased nickel intermediates to increase by over 45 per cent from 2003 levels to approximately 33,570 tonnes in 2004. This external feed source is expected to represent the source of 15 per cent of planned 2004 finished nickel production, up from 23,130 tonnes in 2003 as discussed above. We continue to utilize purchased nickel intermediates to increase the processing capacity utilization of the Company's Ontario and Manitoba operations and to maintain nickel production at the Company's Manitoba operations at or near its 45,000 tonne annual capacity. While such use is profitable, it does increase our costs, particularly at higher nickel prices since the cost of purchased nickel feeds is based on prevailing LME prices. Copper production is currently expected to be approximately 118,000 tonnes in 2004, up 29 per cent from 91,134 tonnes in 2003. Total production of platinum-group metals is expected to increase to 400,000 troy ounces in 2004 from the 2003 strike-affected level of 207,000 troy ounces.

While the Company has certain potential new mine development projects at its existing operations in Canada, if sufficient new low-cost sources of nickel such as the Voisey's Bay and Goro projects are not developed on a timely basis, the Company's overall nickel production, particularly at its Manitoba operations, could decline beginning as early as 2005, and the Company's unit costs of production could increase significantly with any material decline in mine production from its Canadian operations if such operations were not significantly restructured. These developments could materially adversely impact the Company's results of operations, financial condition, profitability and cash flows.

During 2002, as mine production at the Company's Manitoba operations transitioned from the Thompson mine to the lower grade Birchtree mine, the Company experienced lower mine production. The Company continued to experience such lower mine production in 2003 and, as this transition continues to move forward, the Company currently expects to see a continuing decline in mine production in Manitoba in 2004 and expects to see further declines in future years. The Company has recently been relying, and expects that it will continue to rely on an increasing basis, upon the availability of purchased intermediates to maintain its Manitoba's nickel production at around the 45,000 tonne annual level in 2004. While the Company has entered into agreements and other arrangements to purchase intermediates to maintain its Manitoba's production levels at or near the 45,000 tonne annual level for the next few years, until the Company is able to produce intermediate products from its Voisey's Bay project for further processing at its Canadian operations, in particular, the Company's Manitoba operations, it will remain increasingly dependant, in order to continue to produce nickel products at, or close to, their capacity, on purchases of intermediate products principally from two Australian companies. The Company has entered into arrangements for the purchase of nickel-containing concentrates from those two Australian

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producers. Under these arrangements, these producers are currently expected to provide an aggregate of 85,000 tonnes of nickel in concentrate form between 2004 and 2009 for further processing by the Company's Ontario and Manitoba operations. If these suppliers experienced problems in producing or shipping to Canada their intermediate products, these events would have an adverse effect on the Company's ability to produce and sell the nickel products it plans to produce at least in 2004 and 2005 and it would adversely affect the Company's results of operations, financial condition, profitability and cash flows. Extended strikes, such as the one the Company experienced at its Ontario operations in 2003, other labour disruptions and unforeseen events could also adversely affect the Company's production plans and costs and these developments could also adversely affect the Company's results of operations, financial condition, profitability and cash flows.

The Company continues to explore its options to fully utilize its existing Canadian facilities, including the purchase of intermediates and additional external feedstocks from existing or new suppliers and additional mine development. In addition, Inco is seeking to develop new mines principally at its Ontario operations to help sustain its production capacity and reduce costs. Further information on these projects is set out under "Exploration and Project Development" below.

The Company's copper production is currently planned to increase to approximately 118,000 tonnes in 2004 from its 2003 strike-affected level and its total production of platinum-group metals is planned to increase from its 2003 strike-affected level to 400,000 troy ounces in 2004.

*Capital Expenditures*

The primary focus of Inco's capital expenditures is to provide the Company's operations with appropriate production capacity for its nickel and other primary metals products and to develop new projects, including the Voisey's Bay and Goro projects. Capital expenditures totalled \$591 million in 2003, compared with \$600 million in 2002 and \$263 million in 2001. The decrease in 2003, compared with 2002, was primarily due to lower capital spending mainly in respect of our Goro project which was partially offset by higher capital spending in respect of the Voisey's Bay project.

Capital expenditures for the Goro project, including capitalized interest, totalled \$249 million in 2003, compared with \$353 million in 2002 and \$84 million in 2001, and for the Voisey's Bay project totalled \$138 million in 2003, compared with \$73 million in 2002 and \$9 million in 2001. The balance of capital expenditures in each of the three years was directed primarily to the development, maintenance and improvement of new and existing mining operations in Canada and productivity improvements and to meet environmental regulations and similar requirements. The Company currently estimates that its existing operations require, on an annual basis, capital expenditures of approximately \$255 million to sustain their operations, including to meet existing environmental requirements, at currently planned production and/or utilization levels for these operations.

The Company's 2004 capital expenditures are currently expected to total \$1,040 million, including approximately \$430 million for the Voisey's Bay project, approximately \$220 million for the Goro project and approximately \$390 million in sustaining capital expenditures for existing operations, of which about \$60 million will be required for environmental measures and about \$135 million will be used to help maximize or increase production at existing operations, in particular at PT Inco. Depreciation expense is projected to be \$305 million in 2004. The total capital expenditures for the Voisey's Bay and Goro projects will depend on a number of factors, including receipt of all necessary construction and other permits and, in the case of the Goro project, the results of the second phase of that project's review process, the availability of certain tax-advantaged financing from the French government and the acquisition of a minority interest in the Goro project by one or more parties. For a discussion of the results of the bankable feasibility study for the Voisey's Bay project, see "Voisey's Bay Nickel Company Limited - Project Phases" below.

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*Mining*

At December 31, 2003, the Company had the following mines in operation in Canada:

<b>Ontario</b>	<b>Manitoba</b>
Copper Cliff North	Birchtree
Copper Cliff South	Thompson
Creighton <sup>(1)</sup>	
Garson	
Gertrude	
McCreedy/Coleman	
Stobie	

(1) Excludes Creighton 3 located near the main Creighton mine and accessible by a separate shaft and ramp.

All of the mines listed above are underground mines except for the Gertrude mine which is an open pit mine. In addition to these operating mines, the Company's Ontario operations include several non-operating mines or mines on standby which contain estimated ore reserves as indicated in the tables for the Total Estimated Ore Reserves as of Year-End 2002 and 2003 under Ore Reserves and Mining Rights below.

The following maps show the location of the operating mines, non-operating mines, currently undeveloped properties and processing and other facilities at the Company's Ontario and Manitoba operations.

**Ontario Operations**

**Location of Operating Mines, Non-Operating Mines, Undeveloped Properties and Processing and Other Facilities**

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**Manitoba Operations**

**Location of Operating Mines, Non-Operating Mines and Processing and other Facilities**

For further information on the development projects or undeveloped properties at the Company's Ontario and Manitoba operations, see Exploration and Project Development below.

The tables below set forth the Company's annual mine production in thousands of tonnes by operating mine or for PT Inco on an aggregate basis since it has mining areas, and the average grades (in %) of certain metals (nickel (Ni); copper (Cu)), for the Company's Ontario operations, the Company's Manitoba operations and PT Inco for 2001, 2002 and 2003. For the Company's Manitoba and Ontario operations, the production and average grades represent the mine product delivered to those operations' respective process plants and do not include adjustments due to beneficiation, smelting or refining. The mine production at PT Inco represents the product from PT Inco's dryer kilns and delivered to PT Inco's smelting operations ( Dry Kiln Product or DKP ) and does not include nickel losses due to smelting.

**Table of Contents****ANNUAL MINE PRODUCTION**

Tonnes in 000

		2001	2002	2003
<b>Ontario Operations Operating Mines</b>				
Copper Cliff North	Tonnes	889	986	701
	Cu%	1.98	1.29	1.16
	Ni%	1.55	1.18	1.21
Copper Cliff South	Tonnes	964	1,035	769
	Cu%	1.94	2.27	2.50
	Ni%	1.82	1.89	1.80
Crean Hill <sup>(1)</sup>	Tonnes	268	261	
	Cu%	1.46	1.29	
	Ni%	1.91	1.75	
Creighton	Tonnes	1,019	912	713
	Cu%	1.55	1.53	1.53
	Ni%	2.08	2.14	2.10
Stobie	Tonnes	2,582	2,792	2,222
	Cu%	1.00	0.91	0.83
	Ni%	1.10	0.98	0.90
Garson	Tonnes	631	584	434
	Cu%	1.14	1.15	1.10
	Ni%	1.82	1.92	1.87
McCreedy East/ Coleman	Tonnes	1,173	1,084	870
	Cu%	3.19	3.19	3.57
	Ni%	1.73	1.69	1.78
Gertrude <sup>(2)</sup>	Tonnes		156	453
	Cu%		0.37	0.36
	Ni%		1.09	1.01
<b>Total Ontario Operations</b>	Tonnes	<b>7,527</b>	<b>7,810</b>	<b>6,162</b>
	Cu%	<b>1.68</b>	<b>1.57</b>	<b>1.53</b>
	Ni%	<b>1.57</b>	<b>1.45</b>	<b>1.39</b>
<b>Manitoba Operations Operating Mines</b>				
Thompson	Tonnes	1,520	1,433	1,393
	Ni%	2.7	2.58	2.21
Birchtree	Tonnes	431	425	640
	Ni%	1.61	1.78	1.83
<b>Total Manitoba Operations</b>	Tonnes	<b>1,951</b>	<b>1,858</b>	<b>2,033</b>
	%Ni	<b>2.46</b>	<b>2.40</b>	<b>2.09</b>
<b>PT Inco Operations</b>	Tonnes	<b>4,187</b>	<b>3,137</b>	<b>3,891</b>
	%Ni	<b>1.70</b>	<b>1.71</b>	<b>1.91</b>

(1) Crean Hill Mine was closed in 2002.

(2) The Gertrude open pit mine did not operate in 2001. This open pit mine is operated as required based on market conditions and plant capacities.

**Table of Contents***Concentrating, Smelting and Refining*

The conversion of nickel ore mined from the Company's sulphide deposits in Canada into commercially marketable products requires various processing and refining steps undertaken at concentrators, smelters and refineries. The ore is first crushed and ground, the sulphides are separated into concentrates, and the concentrates are then smelted to produce nickel matte, an intermediate product containing approximately 75 per cent nickel plus copper. The matte is then refined to produce primary nickel and copper products.

The Company's processing facilities in operation during 2003 in the Sudbury area included a concentrator, a combined nickel and copper smelter, matte processing facilities, a nickel refinery, a copper refinery, a silver refinery, a sulphuric acid plant and a sulphur dioxide liquefaction plant. Nickel matte produced in Sudbury is refined in Sudbury and other locations into nickel pellets, nickel powders, UTILITY<sup>(5)</sup> nickel, nickel discs and Nickel Oxide Sinter 75<sup>(6)</sup>, a product containing approximately 75 per cent nickel. In Thompson, Manitoba, the Company has a concentrator, a nickel smelter and an electrolytic nickel refinery. Certain nickel products produced in Sudbury and Thompson are finished at Port Colborne.

Finished nickel is also produced at our refinery at Clydach, Wales. The Clydach refinery processes material supplied from Inco's operations in Canada. At Port Colborne, the Company also operates an electrocobalt refinery and a precious metals upgrading facility. The majority of the Company's silver production is refined at Copper Cliff, Ontario and its gold production is refined under a tolling arrangement with the Royal Canadian Mint. This by-product production is reflected in the tables under Sales and Deliveries above. A refinery at Acton, England produces platinum-group metals from upgraded concentrates from Inco's operations in Canada and from the recovery, through toll-refining, of materials containing platinum-group metals supplied by unaffiliated customers.

In November 2001, the Company announced that it was consolidating its Ontario Division, its Manitoba Division and its United Kingdom operations into a new business unit to be known as its Canadian and UK Operations. This new organization has facilitated the sharing of knowledge and has helped to optimize the use of certain of the Company's facilities and resources.

The following table shows Inco's total production of finished nickel and copper from its primary metals facilities for the five years ended December 31, 2003:

	<b>Finished Nickel and Copper Production</b>				
	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>	<b>1999</b>
			(in tonnes)		
Nickel	187,173	209,728	207,077	202,806	177,253
Copper	91,134	111,787	116,255	114,397	116,260

See Mining and Production General above for information regarding the Company's expected nickel production for 2004.

Of the amounts reported in the table above as finished nickel production, the following table shows the amounts of such total finished nickel production from nickel-in-matte produced by PT Inco for the five years ended December 31, 2003:

	<b>Finished Nickel from PT Inco Matte</b>				
	<b>2003</b>	<b>2002</b>	<b>2001</b>	<b>2000</b>	<b>1999</b>
			(in tonnes)		
Nickel	65,704	61,692	61,856	58,356	43,615

The Company's worldwide nickel processing capacity, including capacity at its majority-owned subsidiaries, is adequate to refine the production from its mines at current rates of mine production. The Company also has contractual nickel refining arrangements with nickel refiners in Asia in which the Company has minority equity

- (5) Inco trademark.
- (6) Inco trademark.



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interests. These include an arrangement with Taiwan Nickel for the supply of intermediate products produced by Inco for Taiwan Nickel's refining operations, and a joint venture, also involving the supply of intermediate products produced by Inco, with Korea Nickel which, in turn, produces UTILITY nickel. The other shareholders of Taiwan Nickel are a number of Taiwanese investors and the other shareholders of Korea Nickel are Korea Zinc Company, Ltd. ( Korea Zinc ), a number of individuals associated with Korea Zinc and entities associated with Pohang Iron and Steel Co., Ltd.

All production facilities at the Company's operations in Ontario, Manitoba, Clydach and Acton are owned by the Company and are located on property which Inco owns or with respect to which it has contractual rights to acquire ownership.

Permission from the Ontario government is required for the export of intermediate products derived from Ontario ores. The Company's practice is to meet with government officials prior to the expiration of each of the required export licences to discuss relevant aspects of the export procedure. In December 1995, the Ontario government granted permission for the Company to export nickel oxide sinter and nickel sulphide matte, as well as nickel sulphate residue, to Clydach until December 31, 2005. During 2003, the Company refined about 14 per cent of its primary nickel production at its refinery in Clydach from intermediate products derived from the Company's Ontario ores. The Ontario government also granted permission for the Company to export its semi-refined platinum-group metals concentrate to its Acton refinery until December 31, 2005. The Company anticipates that it will be granted permission to continue to export these materials for additional years after the expiry of these current permits. There is currently no restriction on the export of the products of the Company's Thompson mines for treatment or refining outside Canada. As discussed under *Ore Reserves and Mining Rights* and *Voisey's Bay Nickel Company Limited Negotiations with the Provincial Government* below, there will be certain restrictions or limitations relating to the export of intermediate products from the Province of Newfoundland and Labrador.

***Ore Reserves and Mining Rights***

***Ore Reserves***

The following tables show, as of the end of the periods indicated, the Company's estimates of its (i) proven ore reserves, (ii) probable ore reserves and (iii) aggregate of proven and probable ore reserves at its operating mines, non-operating mines or mines on standby, undeveloped properties, development projects and mining areas at its Ontario operations, Manitoba operations, Voisey's Bay project in the Province of Newfoundland and Labrador, PT Inco in Indonesia and at its Goro project in New Caledonia and the estimated respective average nickel (Ni), copper (Cu), cobalt (Co), platinum (Pt), palladium (Pd) and gold (Au) metal grades, where significant, of each such total amount expressed as a percentage of such total amount as of the end of the periods

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indicated. Ore reserve estimates referred to under Exploration and Project Development below or elsewhere in this Report are included in these tables.

**Total Estimated Ore Reserves As of Year-End 2002**

(in millions of tonnes (Mt) except as indicated)<sup>(1)(2)(3)(7)</sup>

	<b>Class</b>	<b>Mt</b>	<b>%Ni</b>	<b>%Cu</b>	<b>%Co</b>	<b>Pt (g/mt)*</b>	<b>Pd (g/mt)*</b>	<b>Au (g/mt)*</b>
<b>ONTARIO OPERATIONS</b>								
Operating Mines	Proven	112	1.36	1.52		0.65	0.73	0.28
	Probable	36	1.21	1.58		1.26	1.49	0.63
	Total	148	1.32	1.54		0.80	0.92	0.37
Non-Operating Mines	Proven	1	1.60	0.69		0.10	0.10	0.03
	Probable	38	1.07	0.92		0.55	0.55	0.21
	Total	39	1.08	0.92		0.54	0.54	0.21
Undeveloped Properties	Proven	0.3	1.39	0.84		0.10	0.10	0.03
	Probable	5.7	1.47	0.57		0.22	0.52	0.12
	Total	6.0	1.47	0.58		0.22	0.50	0.11
Total	Proven	113	1.36	1.51		0.64	0.72	0.27
	Probable	80	1.16	1.20		0.85	0.96	0.38
	Total	193	1.28	1.38		0.72	0.83	0.31
<b>MANITOBA OPERATIONS</b>								
Operating Mines	Proven	22	2.14	0.14				
	Probable	15	2.21	0.14				
	Total	37	2.17	0.14				
<b>VOISEY S BAY PROJECT</b>								
Development Property	Proven	28	3.02	1.77	0.15			
	Probable	2	0.77	0.55	0.04			
	Total	30	2.85	1.68	0.14			
<b>PT INCO</b>								
Mining Areas	Proven	51	1.71					
	Probable	40	1.76					
	Total	91	1.73					
<b>GORO PROJECT</b>								
Development Property	Proven	44	1.41		0.13			
	Probable	13	1.92		0.08			
	Total	57	1.52		0.12			

\* in grams per tonne (g/mt)

**Table of Contents****Total Estimated Ore Reserves As of Year-End 2003****(in millions of tonnes (Mt) except as indicated)<sup>(1)(2)(3)(7)</sup>**

	<b>Class</b>	<b>Mt</b>	<b>%Ni</b>	<b>%Cu</b>	<b>%Co</b>	<b>Pt (g/mt)*</b>	<b>Pd (g/mt)*</b>	<b>Au (g/mt)*</b>
<b>ONTARIO OPERATIONS<sup>(4)(6)</sup></b>								
Operating Mines	Proven	90	1.42	166		0.75	0.83	0.29
	Probable	52	1.16	1.42		1.08	1.18	0.45
	Total	142	1.33	1.57		0.87	0.96	0.35
Non-Operating Mines	Proven	1	1.60	0.69		0.10	0.10	0.03
	Probable	38	1.04	0.92		0.55	0.56	0.21
	Total	39	1.06	0.91		0.54	0.55	0.21
Undeveloped Properties	Proven	1	1.09	0.50		0.10	0.10	0.03
	Probable	5	0.50	0.60		0.25	0.59	0.14
	Total	6	0.47	0.60		0.24	0.56	0.13
Total	Proven	92	1.42	1.64		0.75	0.82	0.31
	Probable	95	1.13	1.18		0.82	0.89	0.34
	Total	187	1.27	1.41		0.79	0.86	0.31
<b>MANITOBA OPERATIONS<sup>(4)(6)</sup></b>								
Operating Mines	Proven	20	2.25	0.15				
	Probable	14	2.11	0.15				
	Total	34	2.19	0.15				
<b>VOISEY S BAY PROJECT<sup>(4)(6)</sup></b>								
Development Property	Proven	28	3.02	1.77	0.15			
	Probable	2	0.77	0.55	0.04			
	Total	30	2.85	1.68	0.14			
<b>PT INCO<sup>(5)(6)</sup></b>								
Mining Areas	Proven	62	1.81					
	Probable	45	1.80					
	Total	107	1.81					
<b>GORO PROJECTS<sup>(5)(6)</sup></b>								
Development Property	Proven	44	1.41		0.13			
	Probable	13	1.92		0.08			
	Total	57	1.52		0.12			

\* In grams per tonne (g/mt)

- (1) Reserves represent, in accordance with applicable rules and regulations of the U.S. Securities and Exchange Commission (the "SEC"), including the definitions thereunder, that part of a mineral deposit which could be economically and legally extracted or produced at the time of the reserve determination. Proven reserves are reserves for which (i) the quantity is computed from dimensions revealed in outcrops, trenches, workings or drill holes; grade and/or quality are computed from the results of detailed sampling and (ii) the sites for inspection, sampling and measurement are spaced so closely and the geologic character is so well defined that size, shape, depth and mineral content of reserves are well-established. Probable reserves are reserves for which the quantity and grade and/or quality are computed from information similar to that used for proven reserves, but the sites for inspection, sampling, and measurement are farther apart or are otherwise less adequately spaced. The degree of assurance, although lower than that for proven reserves, is high enough to assume continuity between points of observation.
- (2) The Company, in accordance with applicable Canadian securities regulatory requirements, also estimates its mineral reserves (as well as mineral resources) in compliance with the definitions under the CIM Standards on Mineral Resources and Reserves Definitions and Guidelines adopted by the CIM Council of the Canadian Institute of Mining, Metallurgy and Petroleum in August 2000 (the "CIM Guidelines"). If the reserve numbers above estimated as of year-end 2003 and 2002 were prepared in accordance with such definitions for mineral reserve, probable mineral reserve and proven mineral reserve in the CIM Guidelines, there would be no substantive differences in such numbers from the total numbers for proven and probable ore reserves in the tables above or as noted in the paragraphs immediately following the tables or with respect to the other reserve estimates set forth elsewhere in this Report. For the purposes of such



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Guidelines, the Ontario and Manitoba operations' ore reserves at their operating mines are estimated based on, among other factors, operating costs, and the ore reserves estimates at such operations' non-operating mines are based on, among other factors, mining costs derived from certain mining studies. Total reserve estimates are based on a number of assumptions such as mining methods, production and other costs, metal recovery rates and dilution factors. Such costs also include amortization and depreciation; selling, general and administration charges; marketing costs; and charges for non-operating or stand-by mines. Projections of metal prices and certain exchange rates are also used in preparing reserve estimates. For 2003, revenue assumptions were based upon certain metal prices used in preparing these estimates as follows: nickel at \$3.20 per pound (London Metal Exchange (LME) cash nickel price) with adjustments made for a volatility premium (where the volatility premium represents an estimate of the net price change taking into account the nickel price volatility and probability of exploiting additional ore reserves contained in our various orebodies) and for special product premiums or discounts; copper at \$0.90 per pound; cobalt at \$7.00 per pound; platinum at \$420 per troy ounce; palladium at \$250 per troy ounce; and gold at \$275 per troy ounce; the U.S. dollar-Canadian dollar exchange rate used was \$1.00 to Cdn.\$1.52 and an exchange rate for the Indonesian rupiah (Rp) of \$1.00 to Rp 9,500. In 2002, revenue assumptions were based upon the following metals prices: for nickel: \$3.30 per pound LME cash nickel price for the Ontario and Manitoba operations and, based upon the timing of these estimates, a \$3.20 LME cash nickel price was used for the Goro and Voisey's Bay projects, with adjustments made for special product premiums realized by the Ontario and Manitoba operations; copper: \$0.90 per pound; cobalt: \$7.00 per pound; platinum: \$420 per troy ounce; palladium: \$250 per troy ounce; and gold: \$275 per troy ounce; and a U.S. dollar-Canadian dollar exchange rate of \$1.00 = \$1.52; the revenue assumptions utilized for 2002 varied for PT Inco due to the timing of the assessments and the evaluations. For PT Inco, the breakeven cut-off grade was based on a metal price of \$3.20 (LME cash nickel price) for its nickel in matte, a U.S. dollar-Canadian dollar exchange rate of \$1.00 = \$1.43 and a U.S. dollar-Indonesian rupiah exchange rate of \$1.00 = 9,500 Rp, taking into account when this cut-off grade was developed. The Company, in preparing its ore reserve estimates, takes into account recent trends in metal prices and exchange rates in developing the metal prices and exchange rates it uses for these purposes.

- (3) In accordance with applicable Canadian securities regulatory requirements, including National Instrument 43-101, Standards of Disclosure for Mineral Projects, Mr. Robert A. Horn, who served as Vice-President, Exploration from 1995 until mid-November 2003 and continued as a full-time employee until the end of January 2004 and currently as a part-time employee serves as an executive advisor to the Company's Executive Vice-President, Technical Services, has as a qualified person within the meaning of such National Instrument (which means generally an individual with relevant experience as an engineer or geoscientist who is also a member in good standing of a recognized engineering or similar professional association) indirectly supervised the preparation of the ore reserves estimates and other information set forth in the tables and notes thereto for the Goro project. Dr. Lawrence B. Cochrane, Director of Mines Exploration with the Company, has as a qualified person within the meaning of such National Instrument indirectly supervised the preparation of the ore reserve estimates for the Ontario and Manitoba operations, the Voisey's Bay project and PT Inco, and Mr. Robert C. Osborne, Consulting Geologist, Laterites with the Company, has as such a qualified person also indirectly supervised the preparation of the ore reserve estimates for PT Inco. Mr. Horn, Dr. Cochrane and Mr. Osborne have, in accordance with the requirements of such National Instrument, conducted either directly by themselves or indirectly through employees of the Company reporting directly or indirectly to them a comprehensive review and confirmation of the application of the detailed procedures, systems and processes the Company has developed and implemented for the purpose of verifying such data. Mr. Horn, Dr. Cochrane, Mr. Osborne and the staff of the Company involved in this process also periodically check the adequacy of such procedures, systems and processes which are intended to provide sufficient verification of such data based upon recognized sampling, analytical testing, modeling and other procedures in the mining industry.
- (4) The ore reserve estimates for the Ontario and Manitoba operations are of in-place material after adjustments for mining dilution and mining recovery. No adjustments to these estimates have been made for metal losses due to processing (beneficiation, smelting and refining). For the Company's Ontario operations, the average metal recoveries after processing in 2003 are as follows: nickel (Ni) 74.5%, copper (Cu) 89.4%, platinum (Pt) 69.5%, palladium (Pd) 69.7% and gold (Au) 62.9%. For the Company's Manitoba operations, the average metal recoveries after processing in 2003 are as follows: nickel 86.1%, copper 79.5% and cobalt 34.6%. The metal recoveries for each operating mine, non-operating mine, and undeveloped property vary depending on the metal grades and mineralogy for each mine or undeveloped property. The estimated ore reserves include factors for dilution and ore losses due to mining. The ore reserve estimates for the Voisey's Bay project are of in-place material after adjustments for mining dilution and losses due to mining recovery. No adjustments have been made to the ore reserve estimates for metal losses due to processing (beneficiation, smelting and refining). Overall processing recoveries for the Voisey's Bay project are expected to be 82% for nickel, 94% for copper, and 39% for cobalt. The metal recoveries from beneficiation were determined from extensive pilot plant tests. Smelting and refinery recoveries are based on actual recoveries at the Company's Ontario and Manitoba operations given that the Voisey's Bay nickel-containing concentrates planned to be produced over the 2006-2011 period are to be processed at these operations. The realized metal recoveries in each zone may vary depending on the metal grades and the mineralogy of the ore in each zone.
- (5) The ore reserve estimates for PT Inco represent the product from PT Inco's dryer kilns (Dry Kiln Product). The estimated ore reserves at PT Inco include factors for dilution and ore losses due to mining and screening recovery during ore preparation. The estimated ore reserves do not include nickel losses due to smelting. The average nickel recovery after processing used for PT Inco's 2003 ore reserve estimate is 90.0%. For the Goro project, the ore reserve estimates include factors for dilution due to mining and for ore losses due to mining recovery and screening recovery during feed preparation. The ore reserve is estimated using a screened fraction recovered of -50mm. The ore reserve estimates do not include the nickel or cobalt losses due to processing. The planned processing recoveries are anticipated to be 92.2% for nickel and 90.8% for cobalt.
- (6)

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At the Company's Ontario operations, the drill-spacing for the estimated ore reserves classified as proven ranges from 30 meters by 46 meters to 15 meters by 23 meters, averaging 23 meters by 34 meters. The drill-spacing for the estimated ore reserves classified as probable ranges from 61 meters by 91 meters to 30 meters by 61 meters, averaging 46 meters by 76 meters. The classifications are also dependent on the mining method and mining selectivity.

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At the Company's Manitoba operations, the drill-spacing for the estimated ore reserves classified as proven ranges from 15 meters by 18 meters to 12 meters by 12 meters, averaging 14 meters by 15 meters. The drill-spacing for the estimated ore reserves classified as probable ranges from 30 meters by 30 meters to 61 meters by 61 meters, averaging 45 meters by 45 meters. The classifications are also dependent on the mining method and mining selectivity.

For the Voisey's Bay project, the drill-spacing for the ore estimated reserves classified as proven averages 50 meters by 25 meters. The drill-spacing for the estimated ore reserves classified as probable averages 50 meters by 50 meters.

For PT Inco, the drill-spacing for the estimated ore reserves classified as proven ranges from 100 meters by 100 meters to 50 meters by 50 meters, averaging 75 meters by 75 meters whereas the drill-spacing for the estimated ore reserves classified as probable ranges from 200 meters by 200 meters to 100 meters by 100 meters, averaging 150 meters by 150 meters.

For the Goro project, the average drill-spacing for the estimated ore reserves classified as proven is 100 meters by 100 meters and 100 by 200 meters for the estimated ore reserves classified as probable.

- (7) All estimated proven and probable ore reserves referred to in this Report, including the estimates referred to under Exploration and Project Development below, are included in the tables above.

The estimated ore reserves at the Company's Ontario operations for 2003 decreased by 5.0 million tonnes primarily due to mining removal of 6.2 million tonnes grading 1.39 per cent nickel and 1.53 per cent copper. The estimated ore reserves at one of the Ontario operations undeveloped properties, the WD 16 property (0.5 million tonnes grading 1.23 per cent nickel and 0.16 per cent copper), was removed from the Ontario operations estimated ore reserves in 2003 due to the extended time required to obtain the necessary mining permits for this property. These decreases were partially offset by an increase in estimated ore reserves for the Ontario operations for 2003 of 2.5 million tonnes grading 1.48 per cent nickel and 2.75 per cent copper from exploration.

In 2003, estimated proven and probable ore reserves at the Manitoba operations were reduced by 3 million tonnes from year-end 2002 estimates. In addition to mining removal (2.0 million tonnes grading 2.09 per cent nickel and 0.13 per cent copper), the re-evaluation of mining plans at the Manitoba operations due to an increase in mining costs resulted in a decrease of 2.8 million tonnes from year-end 2002 estimates. These reductions were partially offset by an increase of 1.9 million tonnes of estimated proven and probable ore reserves from exploration at the Thompson and Birchtree mines.

At PT Inco, estimated probable ore reserves were increased by 16 million tonnes as a result of ongoing exploration at the Petea mining area. The nickel grade of the estimated ore reserves at PT Inco increased from 1.73 per cent at year-end 2002 to 1.81 per cent at year-end 2003 as a result of reductions in mining dilution and the application of more selective mining methods. In 2003, mining removal at PT Inco totaled 3.9 million tonnes grading 1.9 per cent nickel.

At the Company's Ontario and Manitoba operations, ore reserves are estimated based on a breakeven calculation where the estimated value of the ore in the ground must be equal to, or greater than, the mining costs (or cut-off value). The ore value is determined by deducting from the calculation of gross revenues certain expenses and processing costs. All costs are based upon Inco's applicable annual operating plan. Processing costs include operating, depreciation and sustaining capital costs and are updated annually to reflect the assumptions for such costs included in Inco's current annual or longer term (usually five-year) operating plans. Plant overhead costs are also updated annually with plant throughput assumed to remain constant. Corporate costs include selling, general and administration costs, charges for stand-by mines and demolition expenses. Mining costs include operating and mine overhead, capital, transportation and amortization and depreciation. For the Company's Ontario and Manitoba operations, metal recoveries are calculated based on process plant recoveries developed as part of our annual operating plans and are updated annually. Cut-off values for operating purposes may be adjusted depending on a number of factors, principally plant performance, profitability targets and/or short-term metal prices.

Block modeling and geostatistical interpolation methods are used to derive the ore reserve estimates for over 90 per cent of the ore reserves at Ontario. Conventional (polygonal) methods are used primarily to estimate the ore reserves remaining in pillars for secondary mining assessments. At the Company's Manitoba operations, block models are used and geostatistical interpolation methods are used at the Manitoba Operations Birchtree mine and portions of the Thompson mine. Conventional estimation methods are used for about 50 per cent of the ore reserve estimates at the Manitoba operations. The mining methods used are generally non-selective and the internal dilution is included in the mining blocks evaluated in developing the estimates.

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For the block models, an estimation method, which we believe represents an appropriate geostatistical approach for the data, is selected and technical checks are incorporated into the modeling process. Back analysis studies of mined out areas are completed to verify the appropriateness of polygonal and geostatistical estimation methods and the block models are verified internally. External auditors have been used to critique our geostatistical techniques utilized. Standard procedures are used for the polygonal estimation techniques. Sections and plans employing standardized grading and interpretation procedures are used to select the mining method and assign mining lines. Mineral tonnages and metal grades are then determined and appropriate mineability and dilution rates are applied. As noted above, mining costs represent the cut-off values used to selectively report what mining blocks would be included in our ore reserve estimates.

For the Voisey's Bay project, the geological interpretation of the Voisey's Bay Ovoid zone has been based on the modelling of the troctolite unit hosting the mineral. Within this model, two domains of massive sulphide and disseminated mineralization were further defined. The block dimensions used in the block model are 10m x 10m x 5m vertical. Geotechnical data derived from core holes drilled in the pit walls were used to design the open pit to mine this zone. Economic evaluations are based on metal recoveries determined from extensive metallurgical testing and operating costs estimated in the Voisey's Bay project's March 2003 feasibility study.

Due to the different economic contributions from each metal, block net smelter royalty (BNSR) values have been used instead of a single metal cut-off grade for the open pit definition, production planning and ore reserve determination. The BNSR calculations assume constant concentrate grades with which to calculate smelting, refining and freight charges. Charges in the BNSR calculation, in addition to smelting, refining, and concentrate shipping charges, include a 3 per cent royalty payment to Archean Resources Ltd., which in 2003 transferred this royalty to a limited partnership it created to hold such royalty interest as discussed under Mining and Other Rights below, and an assumed technical/management fee payable to Inco Limited. A life-of-mine schedule using a variable BNSR cut-off approach was also developed. Blocks valued greater than the BNSR cut-off in the production schedule were tabulated as ore. The cutoff value corresponds to the expected milling costs plus site general and administration costs. All blocks with BNSR values less than the cut-off were considered as waste. There are no plans for a low-grade stockpile for the Voisey's Bay project, and, accordingly, no part of the estimated ore reserve is considered stockpile ore. The BNSR cut-off used in the last six years in the project's estimated mine life corresponds to the mill breakeven cut-off.

For the Goro project, the ore reserves were estimated using block modelling based on a 30m by 30m by 1m block size. The nickel and cobalt grades, the chemical components and screen recoveries were interpolated for each block for each of the laterite layers using recognized mining industry methods. The specific gravity, moisture content and screen size recoveries of the laterite layers were determined based on data collected during geological and geotechnical drilling campaigns. Grade simulation models, developed from close-spaced drilling, were used to simulate variability in the layers' thickness and chemistry, that are expected to be encountered during mining, to estimate the ore loss due to mining and mining dilution. A 1.20 per cent nickel cut-off grade was used to estimate the ore reserves. The cut-off grade provides a plant feed that meets the required chemistry of the blended material delivered to the process plant to provide the planned nickel and cobalt production. The 1.20 per cent nickel cut-off grade was applied in the limonitic layer only and all material located below that cut-off horizon are planned to be mined in bulk, without mining selectivity applied, until bedrock is reached.

The cut-off grades used to estimate ore reserves at PT Inco are also based on a break-even calculation. A break-even grade is used rather than a break-even value since nickel is the only metal produced by PT Inco. The estimation of the break-even grade is based on a certain assumed nickel prices less the discount for the nickel in matte product produced by PT Inco (representing the selling price received by PT Inco for its nickel in matte product equivalent to a percentage of the London Metal Exchange (LME) cash nickel price). Costs are based on annual plan operating costs (including selling, general and administration costs), and current depreciation and amortisation expenses (adjusted for any future changes). In the computation of the break-even grades for 2003, operating and fixed costs are based on PT Inco's 2004 annual budget plan, after normalising certain costs for long-term usage and removing certain unusual costs for one-time events (additional pre-stripping, delineation drilling and equipment rentals) and an adjustment for oil prices to a ten-year average. PT Inco's process plant nickel recovery factor is also based on its annual operating plan and is adjusted each year. For the estimation of ore reserves for PT Inco's three mining areas, the Sorowako East Block, Sorowako West Block and the Petea



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areas, the break-even grades take into consideration the operating costs at each location. The cut-off grade used for the Sorowako East Block is 1.45 per cent nickel, the Petea area is 1.50 per cent nickel and for the Sorowako West Block is 1.55 per cent nickel. Given the nature of PT Inco's laterite deposits and how they are mined, PT Inco does not have specific operating mines but rather has mining areas. PT Inco from time to time has, however, referred to the Sorowako West Block and East Block areas (shown on the map below under P.T. International Nickel Indonesia Tbk ) collectively as its Sorowako mine.

PT Inco may use different cut-off grades for purposes of its short-term operations. Cut-off grades for short-term operating purposes are adjusted depending on a number of factors, principally plant performance, profitability targets and/or short-term nickel prices.

The ore reserves for PT Inco are estimated using block modelling techniques and geostatistical interpolation methods. Standard block sizes are used with different parameters applied to each deposit and in each of the limonite and saprolite layers. Mining volumes were estimated using a minimum ore thickness of two meters and material below cut-off grade was classified as internal waste if it was equal to or less than two meters thick. A minimum of 25 meters by 25 meters lateral extent criteria was used to classify the ore. The mineral volumes were converted to tonnages using appropriate wet tonnage factors. Screening recovery factors based on actual production are applied to convert the run of mine product to equivalent DKP. Mining recovery and dilution was included in the estimation of the reportable reserves.

Over the past three years, the key processes for developing the Company's ore reserve estimates have been enhanced to include more formalized senior management review and approval of such processes and the preparation of such estimates. These processes involve key technical personnel at each of the principal operating units or locations, the Company's corporate technical group, including the Company's corporate exploration personnel, as well as senior management's involvement and have been enhanced as part of the objective of recognizing ore reserve estimating as a core business process. In addition to internal audits of the processes utilized and the estimates themselves, we have also retained external auditing firms to review such processes and estimates, including the ore reserve estimates for the Voisey's Bay project.

### *Mining and Other Rights*

The following discussion reflects a summary of the property rights, mining rights, licences, leases or other concessionary rights to mine for or extract metals and other associated minerals from the areas that the Company currently mines or expects to mine as part of its long-term mine plans in Canada, Indonesia and New Caledonia. With respect to those properties which are not currently owned but are subject to leases or licenses with finite terms that are not perpetual or cannot be automatically renewed or extended and on which estimated ore reserves are located and/or are covered by the Company's current long-term mine plans, the Company currently believes that it will be able to obtain renewals or extensions of such leases or licenses, if required as part of its long-term mine plans on a timely basis.

#### Ontario Operations

All operating mines, non-operating mines and undeveloped properties which contain estimated proven and probable ore reserves for the Company's Ontario operations are on lands owned by Inco, with the exception of a portion of the Copper Cliff South mine (known as Kelly Lake) and a portion of the Victor non-operating mine. These portions of the Copper Cliff South and Victor mines are located on lands with respect to which Inco currently holds a license of occupation. Inco has applied for a 21-year lease for each of these two areas and believes that renewals of these leases will be obtained on a timely basis.

In Ontario, the Company also holds mining rights, surface rights, licenses of occupation and mining claims granted to it by the Province of Ontario. Mining rights are rights to exploit and extract minerals on, in or under the land, and surface rights are rights to use the surface of the land. These rights remain in effect so long as Inco owns the land to which these rights apply. Inco also owns a combination of mining and surface rights covering land leased from the Province of Ontario. These leased lands, which include a combination of mining and surface rights, are leased for either 10 or 21 years. Annual rentals are paid to the Province to keep the leases in good standing. One of the 21-year leases expired in November 2003 and the Company applied for a 21-year renewal

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term and currently expects to receive the renewal in late March 2004. Three of the 10-year leases held are up for renewal in late March 2004. The next lease that comes up for renewal is in 2008. Inco currently holds 165 licenses of occupation for mining, hydro electric installations and various other industrial purposes in Ontario. These licenses of occupation allow Inco to use the land in the manner specified in each license, including the right to dig, excavate and remove ores and minerals from and under the land. Inco currently also has a number of mining claims in Ontario. Mining claims represent rights to explore the land covered by the claim. In early March 2001, a party purported to stake mining claims and then initiated an administrative appeal in the Province of Ontario effectively contesting the validity of a licence of occupation originally granted to the Company more than 50 years ago covering a portion of the Company's Kelly Lake deposit which was identified in 1997. The actions taken by this party alleged that the Company's rights under the licence had been lost because the Company had not made timely payments in accordance with the then applicable requirements for the periodic payment of the rent required to be paid to the province to maintain the licence. All of the appeals initiated by this party contesting the license were dismissed during 2001 and 2002. As a result of the dismissal of the appeals and the enactment of new legislation in Ontario in 2002, the Company does not anticipate any future challenges to the validity of such licences on the grounds alleged by this party.

**Manitoba Operations**

Inco's landholdings or mining rights in Manitoba consist of order-in-council leases ( OIC Leases ), mineral leases and mining claims. OIC Leases were negotiated as part of an agreement between Inco and the Province of Manitoba entered into in 1956 covering the development of the Thompson, Manitoba nickel deposits by the Company. OIC Leases entitle Inco to explore for, and mine, all minerals in the subsurface (except hydrocarbons, industrial minerals and surficial deposits that are not incidental to the mining, milling, smelting and refining processes). OIC Leases also provide Inco with the right to erect buildings and structures necessary for its operations and provide for a right of access over and upon the lands. OIC Leases provide for an initial 21-year term and two subsequent guaranteed renewals of 21 years each, for a total guaranteed lease period of 63 years. Subsequent lease renewals beyond the three 21 year terms can be granted at the discretion of the Province of Manitoba. OIC Leases were initially surveyed and made effective over a six year period over the 1957 to 1962 period. All of the current OIC Leases remain in effect through the 2020 - 2024 period except certain leases where the current second guaranteed 21-year term expires in September 2004. All third 21-year guaranteed renewals of the OIC Leases have been granted except for one set of OIC Leases that, as indicated above, are due for the third 21-year guaranteed term renewal once the second 21-year guaranteed renewal term expires in September 2004. All of the OIC Leases that cover the current area of the Thompson mine were renewed in 2001 for 21-year terms. The eastern and depth extensions of the Thompson mine are covered by OIC Leases that are subject to a guaranteed 21-year renewal of such leases in September 2004. Mineral leases are 21-year leases that are renewable at the discretion of the Province. Inco holds seven mineral leases in the Thompson, Manitoba nickel belt. The mineral leases, which conveys to the lessee the exclusive right to the minerals (other than quarry minerals) that occur on or under the land covered by the lease and access rights to erect buildings and structures (including shafts) to mine within the limits of the lease, remain in effect until April 1, 2013. Inco also holds mining claims, a right issued by the Province of Manitoba under provincial legislation which conveys to the holder the exclusive right to the minerals (other than quarry minerals) that occur on or under the land covered by the claim and access rights to explore for and develop minerals owned by the Province. A mining claim does not, however, entitle the holder to extract minerals from the land covered by the claim. In order to extract minerals from the land covered by a mining claim, the holder must obtain a mineral lease from the Province of Manitoba.

All of the Manitoba operations' operating mines and all the mineral rights for all mines which contain estimated proven and probable ore reserves are on properties covered by OIC Leases. The Manitoba operations' Thompson mine is located on land covered by an OIC Lease that is due for renewal in 2022. Since this renewal would be beyond the three 21-year guaranteed renewals, the renewal can be obtained prior to this Lease's current expiration date. The eastern and depth extensions of the Thompson mine are covered by OIC Leases that are due for renewal in September 2004. As discussed above, under the provisions of the original agreement with the Manitoba Government, the renewal of these OIC Leases is guaranteed for a third 21 year term. The Manitoba operations' Birchtree mine is located on land covered by both OIC Leases and three mineral leases. The mineral

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leases are in good standing until April 1, 2013. We currently believe that the renewals of these leases will be granted when they expire.

Voisey's Bay Project

The Voisey's Bay project company, VBNC, holds mineral claims (which have been grouped into mineral licences), a mining lease and surface rights in the Province of Newfoundland and Labrador. A mineral claim (generally covering a 500 meter by 500 meter parcel of land), issued by the Province of Newfoundland and Labrador under provincial legislation, entitles its holder the exclusive right to explore for minerals in, on or under the area of land described in the licence, and obligates its holder to conduct a minimum amount of assessment work (measured by the amount of money spent) on the land covered by the license. Up to 256 mineral claims can be grouped together into one mineral licence. Grouping mineral claims into a single mineral license allows the holder to better manage the assessment work required to be done on the land that is the subject of the claims. Mineral claims and mineral licences are issued for a period of five years and may be extended for three additional five-year renewal periods, for a total of twenty years. A mineral licence does not entitle its holder to extract any minerals from the land described in the licence. None of the Voisey's Bay project's current estimated ore reserves are located on lands covered by a mineral claim or licence.

In order to extract minerals from the land covered by a mineral licence, the holder of a mineral licence must obtain a mining lease issued by the province under provincial legislation for the land covered by such mineral licence. VBNC obtained a mining lease, effective September 30, 2002, for a period of 25 years which gives VBNC the exclusive right to extract minerals and carry out mineral exploration, mining operations or mining processing and development in, on or under the lands, or part of the lands so long as VBNC and Inco continue to meet the terms and conditions of a development agreement made as of September 30, 2002 between VBNC, Inco and Her Majesty the Queen in right of Newfoundland and Labrador. This mining lease can be renewed for further 10-year terms so long as VBNC has been in compliance with the terms of the lease and has applied for such renewal at least three months prior to the expiration of the then current lease. Under the terms of the mining lease, production is not to exceed on average 2.2 million tonnes of ore annually for the first 10 years of mining operations and on average 5.5 million tonnes of ore annually thereafter. The current areas to be mined as part of the Voisey's Bay project and all of the estimated proven and probable ore reserves for the Voisey's Bay project are held under this mining lease. We are not aware of any information or other factors at this time which would indicate that we could not reach agreement with the Province on a new mining lease or an extension when the current mining lease expires in September 2027. In addition, as a corollary to the mining lease, VBNC received a surface lease entitling it to use certain lands necessary for its mining operations. Like the mining lease, the surface lease was effective September 30, 2002 for a period of 25 years, and may be renewed for further 10-year terms.

VBNC also holds nine mineral licences, all of which expire over the March – November 2014 period, covering the main claim block of the Voisey's Bay project. These mineral licences have not been legally surveyed. Geographic coordinates define their locations. To date, sufficient assessment work has been completed to maintain these mineral licences at least until 2008 so long as the required renewal fees (currently being approximately Cdn. \$100,000 and payable every five years, subject to increases in such fees based on subsequent renewals) are paid. Additional assessment work will be required to hold the mineral licences in good standing through 2014.

Pursuant to the terms of an option agreement originally entered into in 1993 (the Option Agreement), Diamond Fields Resources Inc. (Diamond Fields) acquired, upon the exercise of the option thereunder, all of the mineral claims of Archean Resources Ltd. (Archean) in Labrador and Archean was granted a royalty, payable quarterly, equal to three per cent of net smelter returns from mining production from VBNC's Labrador properties, including the Voisey's Bay deposit, (the Royalty) and a three per cent gross royalty (also payable quarterly) on the gross value of raw diamonds and/or gemstones recovered from these properties. The Option Agreement was assigned to VBNC by Diamond Fields in 1995. The royalty is secured by a mortgage on VBNC's Labrador properties in the maximum aggregate principal amount of \$100 million. The mortgage is expressly subordinated to any mine development financing that might be obtained in the future. In 2003 Archean transferred this royalty to a limited partnership currently controlled by Archean's principal shareholders.

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The Voisey's Bay deposit is within a geographical area that has been the subject of land claims negotiations between certain aboriginal groups and the Governments of Canada and the Province of Newfoundland and Labrador. Aboriginal groups asserting land claims in the area include the Labrador Inuit Association (the LIA) and Innu Nation. For further information, see Voisey's Bay Nickel Company Limited Negotiations with Aboriginal Groups below.

Goro Project

The Goro project company, Goro Nickel, currently holds 69 nickel, cobalt and certain other mining concessions and approximately 26 surface rights covering 19,500 hectares, all in the south province (*Province Sud*) of New Caledonia. Goro Nickel also holds an additional 12 mining concessions outside the Goro project area in New Caledonia in a region called Tiebaghi. Of the 69 concessions held by Goro Nickel, the Goro project covers 6,042 hectares within seven mining concessions, of which four are perpetual in term and three are renewable prior to their expiry dates (in 2016 and 2051). Goro Nickel has the right to renew these three renewable concessions for an additional 25-year period when their initial terms expire. Concessions generally represent long term permits (having a term up to perpetuity) granted for mining large deposits which entitle the holder the exclusive right to exploit, extract and mine. A concession applies to one or several minerals defined by the granting decision along with its geographical location. The granting of a concession is based on the delineation of an exploitable orebody made during exploration activities conducted pursuant to permits called *permis de recherches* or *permis d exploitation*. Surface rights can be granted independently of mineral rights. Goro Nickel holds surface rights, known as *occupation des sols*, which are rights to use surfaces on or outside mining permits for mining-related activities. All of the estimated proven and probable ore reserves for the Goro project are within the mining and surface rights held as concessions. As discussed above, four of the concessions are perpetual and the other three concessions have expiry dates between 2016 and 2051.

PT Inco

Under the original Contract of Work or concessionary agreement between the Republic of Indonesia and Inco entered into in 1968, and the agreement on modifying and extending that Contract of Work entered into in January 1996 which sets forth certain provisions which will apply once the terms of the original Contract of Work expires on March 1, 2008 and through December 28, 2025, PT Inco, as the sole contractor of the Government of Indonesia in the areas covered by the Contract of Work, has been granted exclusive rights in these specified areas on the Island of Sulawesi to mine, process, store, transport and sell all nickel and nickel-containing minerals in any form and all minerals, except for radioactive materials) found in association with nickel in the areas. The Contract of Work also grants PT Inco all necessary licenses and permits to conduct its operations, including certain expansions of its operations, as provided for in the Contract of Work. All of PT Inco's mining areas currently containing estimated proven and probable ore reserves are within PT Inco's Contract of Work. Under the terms of the agreement of modification and extension of PT Inco's original Contract of Work entered into in 1996, the Government of Indonesia has agreed to give sympathetic consideration to a further renewal or extension of the Contract of Work, upon the request of PT Inco based upon one or more developments, including a proposal to make a substantial new investment in PT Inco, or the demonstration by PT Inco of the positive economic and other benefits to Indonesia provided by PT Inco. We are not aware of any information or other factors at this time that would indicate that we would not be able to reach agreement on a further extension of PT Inco's Contract of Work before it expires at the end of 2025.

***PT International Nickel Indonesia Tbk***

*General*

In early March 2004, Inco acquired from an existing shareholder in PT Inco approximately 5.2 million shares in PT Inco held by this shareholder. As a result of this acquisition, Inco's ownership of the equity of PT Inco increased from 59 per cent to 61 per cent. Sumitomo Metal Mining Co., Ltd. (SMM) holds slightly more than 20 per cent and public shareholders hold a total equity interest of slightly more than 18 per cent. PT Inco's shares are traded on the Jakarta Stock Exchange. The Company's investment at book value of PT Inco was approximately \$364 million at December 31, 2003, the same as at December 31, 2002 and 2001. At

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December 31, 2003 PT Inco had outstanding indebtedness to third party lenders totaling \$192 million, compared with \$269 million at year-end 2002 and \$292 million at year-end 2001. This indebtedness was incurred primarily to finance the expansion project referred to below under Contract of Work Extension and Expansion of Facilities .

In view of its remote location, PT Inco's production facilities are almost completely self-contained. They consist of an open-cast laterite mine, a processing plant with four electric furnace smelting lines (including a fourth line constructed as part of the PT Inco expansion project referred to below), thermal and hydroelectric power generating facilities and ancillary infrastructure, including a townsite, roads, an airport and port facilities.

Since 1998, Indonesia has been experiencing economic and political turmoil, some of which have been compounded by a downturn in the global economy. Indonesia's return to economic and political stability will be dependent to a large extent on the effectiveness of measures taken by the democratically elected Government of Indonesia to restore business and popular confidence, decisions of international financial institutions, including the World Bank and the International Monetary Fund, regarding the availability of financing to Indonesia and companies operating in Indonesia, global economic conditions, and a number of other factors, including regulatory and political developments within Indonesia, which are beyond the Company's control or ability to predict.

In the Indonesian mining sector, mining companies have been facing several challenges stemming from the problems being experienced by Indonesia. These challenges include regulatory uncertainty under regional autonomy legislation which has sought to transfer governmental power in a number of areas, including taxation and mining regulations, from the central government to regional governments; overlapping and unclear tax and environmental legislation enacted by central, provincial and local government authorities; weakness in the banking sector; illegal mining activities; increasingly militant actions of non-governmental organizations and labour unions; and continued disputes between mining companies and local communities who are making increasing demands on mining companies operating in their communities. These challenges may, in time, affect the Company's operations and have, to the extent possible, been taken into account by PT Inco's management in evaluating PT Inco's current and future activities in Indonesia.

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The map below indicates the mining areas, the East Block, the West Block and the Petea areas, where PT Inco's estimated proven and probable ore reserves were located for 2002 and 2003 as well as the location of PT Inco's process plant, hydroelectric facilities and the boundary of the other properties (referred to as "Other Concessions" in the map) contained within PT Inco's Contract of Work containing additional mineralized nickel laterite.

*Contract of Work Extension and Expansion of Facilities Completed in 1999*

As discussed under "Ore Resources and Mining Rights" above, PT Inco's operations are conducted pursuant to a Contract of Work with the Government of Indonesia under which PT Inco is the sole contractor of the Indonesian government for the production and marketing of nickel and associated minerals (other than radioactive materials) mined in specified areas on the island of Sulawesi. The original Contract of Work was signed in 1968 and in January 1996 PT Inco signed an agreement with the Government of Indonesia to modify and extend the Contract of Work to the year 2025, subject to further extensions with the consent of the Government of Indonesia, from its original expiry date in 2008. The Contract of Work confers upon PT Inco all authorizations necessary for the development and operation of its nickel project.

In late 1999, PT Inco completed a major expansion project that increased its production capacity by 50 per cent to 68,000 tonnes of nickel-in-matte per year. The expansion involved improvements to the three existing smelting lines and the construction of a fourth electric furnace smelting line together with the construction of 93 megawatts of additional low-cost hydroelectric generating capacity at Balambano, approximately 25 kilometres from PT Inco's production facilities at Sorowako. The Balambano facility has been able to generate power consistently above its design capacity due to improved water management practices and higher reservoir levels and other related factors than were assumed in developing its original design capacity.

Financing for the expansion project was provided by a group of international lenders in the total principal amount of \$340 million for the expansion project and an additional \$81 million to refinance then existing PT Inco debt. The remainder of the original estimated cost of \$580 million for the project had been expected to be provided by PT Inco's available cash balances plus cash generated by existing operations during the construction

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period. However, as a result of lower production levels caused by limited rainfall and its adverse effect on hydroelectric power generation in 1998 and 1997, low nickel prices and increased costs due to construction delays associated with its new hydroelectric facilities, PT Inco's ability to generate cash was significantly reduced and, as a result, Inco Limited agreed in May 1999 to provide PT Inco with a loan facility under which \$88 million was advanced. These advances have since been repaid.

PT Inco's existing hydroelectric facilities were constructed and are currently operated pursuant to a 1975 decree of the Indonesian government. This decree, which effectively also covers the Balambano generating capacity which was part of the expansion project, vests an Indonesian ministry with the right, upon two years' prior written notice to PT Inco, to acquire the hydroelectric facilities. No such notice has been given. If such right were exercised, the decree also provides that the hydroelectric facilities would be acquired at their depreciated value subject to the ministry providing PT Inco with sufficient power to meet its operating requirements, at a rate based on costs plus a normal profit margin, for the remaining term of the Contract of Work.

PT Inco's estimated ore reserves and other deposits at Sorowako on the island of Sulawesi are sufficient to support its operations for more than 20 years, and have the potential to continue to supply PT Inco's operations for a number of additional years. Future expansions are possible, as warranted by market conditions, by developing the extensive laterite nickel deposits within PT Inco's Contract of Work area in the Sorowako outer area and at Bahodopi and Pomalaa, located approximately 80 kilometres and 200 kilometres, respectively, from PT Inco's operations at Sorowako.

When PT Inco's Contract of Work was extended in 1996, PT Inco agreed to several undertakings with regard to future expansions of its operations. Under one such undertaking, PT Inco agreed, subject to economic and technical feasibility, to construct production plants at Pomalaa in Southeast Sulawesi and Bahodopi in Central Sulawesi. The Contract of Work indicated that the first plant could be in operation by 2005 and the second by 2010, but did not specify which plant was to be constructed first.

In February 2003, PT Inco signed a Cooperative Resources Agreement (the CRA) with PT Aneka Tambang Tbk (PT Antam), an Indonesian government-controlled diversified mining company and producer of ferronickel whose nickel operations are located near where PT Inco has certain deposits which we have referred to as the Pomalaa area within its Contract of Work. Under the CRA, PT Inco agreed to supply saprolite, a relatively high grade of lateritic ore, to PT Antam from PT Inco's contract area in Pomalaa at prices based on an agreed upon pricing formula. The initial term of the CRA is 36 months starting from the initial delivery of ore by PT Inco to PT Antam. Initial ore deliveries are currently expected to be made to PT Antam by the end of the second quarter of 2004. The CRA can be extended for one or more additional terms of 12 months each provided PT Antam has fulfilled its obligations under the CRA. PT Inco has certain unilateral termination rights under the CRA.

In conjunction with the CRA, PT Inco obtained the approval of the Indonesian Minister of Energy and Mineral Resources with respect to PT Inco meeting certain of its undertakings covering future mining and processing activities under its Contract of Work by virtue of entering into the CRA. That approval indicated that PT Inco will be deemed to have satisfied its obligation to build a commercial plant at Pomalaa until the later of December 31, 2008 or the termination of the CRA, following which PT Inco will be obligated to deliver a report evaluating the technical and economic feasibility of constructing such a plant to the Government of Indonesia. PT Inco's obligation under its Contract of Work concerning the construction of a commercial plant at Bahodopi by 2010, subject to economic and technical feasibility, remains in effect.

PT Inco believes that the CRA provides a number of benefits to PT Inco, including (i) enabling PT Inco's saprolite mineral deposits at Pomalaa to be developed on a basis that should provide PT Inco with a reasonable return, (ii) satisfying certain of PT Inco's undertakings under its Contract of Work, (iii) evidencing, in addition to Inco's Sorowako expansion in 1999, Inco's continuing commitment to the Indonesian mining sector at a time of economic and political uncertainty in that country, and (iv) satisfying certain concerns relating to regional development expressed by the provincial and regional governments in Southeast Sulawesi which have assumed a greater role in the development of regional natural resources under Indonesia's regional autonomy program.

**Table of Contents***Operations*

Production of nickel-in-matte at PT Inco increased by 18 per cent to 70,200 tonnes in 2003 from 59,500 tonnes in 2002, reflecting the processing of higher grade ore and higher overall production levels in 2003 compared with 2002. Production in 2002 decreased by five per cent to 59,500 tonnes from 62,600 tonnes in 2001, reflecting the planned rebuild of one of PT Inco's furnaces and related facilities during 2002. Nickel-in-matte, an intermediate product, is sold by PT Inco primarily into the Japanese market. Approximately 95 per cent of PT Inco's electric power requirements are supplied by its 165 megawatt hydroelectric generating facilities on the Larona River and its newer 93 megawatt facilities at Balambano which began operation in 2000. The Balambano facility has been able to generate power consistently above its design capacity due to improved water management practices and higher reservoir levels and other related factors than were assumed in developing its original design capacity. PT Inco still required approximately 443,282 tonnes of fuel oil to operate its dryers, kilns and other oil-fired facilities in 2003.

Largely as a result of improved nickel prices, PT Inco's net earnings, as reported to its shareholders, were \$104 million in 2003, compared with \$30 million in 2002 and \$9 million in 2001. PT Inco's net realized price for nickel-in-matte in 2003 averaged \$7,117 per tonne (\$3.23 per pound), compared with \$5,114 per tonne (\$2.32 per pound) in 2002 and \$4,836 per tonne (\$2.19 per pound) in 2001. The selling price of PT Inco's nickel-in-matte is determined by a formula which is based upon the LME cash price for nickel.

The following table shows PT Inco's production, together with deliveries by the Company of finished nickel refined from PT Inco's matte, for the five years ended December 31, 2003:

Year	Production of Nickel in Matte	Deliveries of Finished Nickel to Customers <sup>(1)</sup>
		(in tonnes)
1999	45,400	42,285
2000	59,200	60,192
2001	62,600	60,480
2002	59,500	61,997
2003	70,200	70,534

(1) Includes 9,638 tonnes in 1999, 12,064 tonnes in 2000, 12,283 tonnes in 2001, 12,557 tonnes in 2002 and 14,307 tonnes in 2003 of nickel-in-matte delivered to SMM as a final product.

As indicated in the tables on estimated ore reserves on a Company-wide basis above under *Ore Reserves and Mining Rights*, PT Inco's estimated ore reserves at the end of 2003 were 62 million tonnes of proven reserves grading 1.81 per cent nickel and 45 million tonnes of probable reserves grading 1.80 per cent nickel, compared with 51 million tonnes of proven reserves grading 1.71 per cent nickel and 40 million tonnes of probable reserves grading 1.76 per cent nickel at the end of 2002<sup>(6)</sup>.

The Indonesian government has indicated that it intends to exempt those companies operating under Contracts of Work similar to the one which PT Inco had entered into prior to 1999 from the scope of legislation originally enacted in 1999 covering protected forests in Indonesia and limiting the activities which could be conducted in areas covered by this law. In early March 2004, the Indonesian government indicated publicly that it intended to put into effect this exemption for PT Inco and a number of other mining companies in 2004.

<sup>(6)</sup> In accordance with applicable Canadian securities regulatory requirements, including National Instrument 43-101, *Standards of Disclosure for Mineral Projects*, as indicated in Note (3) to the tables entitled *Total Estimated Ore Reserves as of Year-End 2003 and 2002* above, Dr. Lawrence B. Cochrane and Mr. Robert C. Osborne, each as a qualified person within the meaning of such National Instrument, either indirectly supervised or has been involved in the supervision of the preparation of the estimates of such proven and probable ore reserves as of year-end 2003 and 2002 in accordance with the CIM Guidelines. These estimates would be identical under the applicable rules and regulations of the SEC and such definitions are substantially the same as the corresponding definitions under the SEC rules and regulations. Reference is made to such Note (3) to such tables for additional information on how PT Inco's reserve estimates for the 2002-2003 period were prepared.



**Table of Contents***Sales*

All of PT Inco's production is sold in U.S. dollars under long-term contracts to Inco and SMM which, by their terms, continue until the expiration of the Contract of Work. These contracts provide that if the Contract of Work is extended or renewed the contracts will be extended for the period of such extension or renewal. Under these contracts, about 20 per cent of PT Inco's production is sold to SMM and the balance to Inco.

PT Inco's deliveries of nickel-in-matte totalled 70,500 tonnes in 2003, compared with 61,900 tonnes in 2002 and 60,500 tonnes in 2001. The Japanese nickel market continues to be particularly important to PT Inco since PT Inco's operations were conceived, in part, as a stable source of feed material to Japanese nickel refiners in the form of a processed intermediate nickel product which could be imported free of existing Japanese tariffs levied on refined nickel metal and other finished forms of nickel.

Inco owns a 67 per cent interest in ITL which processes nickel-in-matte from PT Inco to produce finished products for the stainless steel industry in Japan.

*Goro Nickel S.A.*

Inco owns an approximately 85 per cent interest in Goro Nickel, with a French government agency, Bureau de Recherches Géologiques et Minières ( BRGM ), currently holding the other approximately 15 per cent. Goro Nickel holds a number of claims covering nickel-cobalt properties in New Caledonia, located about 1,500 kilometres east of Australia. These properties have an extensive laterite resource base, including, as reflected in the tables above for estimated ore reserves on a Company-wide basis under Ore Reserves and Mining Rights, an initial mining zone with, as of year-end 2003 and an estimated 44 million tonnes of estimated proven ore reserves grading 1.41 per cent nickel and 0.13 per cent cobalt and 13 million tonnes of estimated probable ore reserves grading 1.92 per cent nickel and 0.08 per cent cobalt which has been outlined as an initial source of feed for a commercial plant.<sup>(7)</sup> Given the status of the comprehensive review of the Goro project referred to below, the capital cost estimate used for this estimate of ore reserves as at year-end 2003 reflected an increase of approximately 30 per cent above the capital cost estimate of \$1,450 million which had been based upon the Goro project's March 2001 bankable feasibility study. This estimated ore reserve base can be mined using low-cost open pit methods, which, when combined with Inco's proprietary pressure-acid leaching and solvent extraction (PAL-SX) technology, gives the project the potential to have one of the lowest cash costs of nickel production in the world.

In 1999, the Company completed the construction of an integrated pilot plant in New Caledonia capable of processing 12 tonnes of ore per day to continue with the development of the PAL-SX technology required for commercialization. The pilot plant operated successfully for over two years, both in further proving the PAL-SX technology and in training the core workforce for a future commercial plant.

In April 2001, following completion of a bankable feasibility study, the Company announced that it planned to proceed with the construction of a commercial nickel-cobalt project at Goro. The project consists of a fully integrated mining and processing facility with a planned annual capacity of approximately 55,000 tonnes of nickel and 4,500 tonnes of cobalt. The Goro project is currently expected to produce a nickel oxide product containing 78 per cent nickel and a cobalt carbonate product. The operation is expected to supply nickel to stainless steel customers in South Korea, Taiwan and eventually China. In June 2001, the Company announced that Goro Nickel had reached an agreement in principle with a joint venture of Bechtel Overseas Corporation of the United States and Technip France S.A. of France, in association with Hatch Associates Ltd. of Canada as subcontractor, to act as the prime contractors for the construction of the Goro project, and the definitive contracts with the joint venture companies were signed in April 2002.

<sup>(7)</sup> In accordance with applicable Canadian securities regulatory requirements, including National Instrument 43-101, Standards of Disclosure for Mineral Projects, as indicated in Note (3) to the tables entitled Total Estimated Ore Reserves as of Year-End 2003 and 2002 above, Mr. Robert A. Horn has, as a qualified person within the meaning of such National Instrument, indirectly supervised the preparation of the estimates of such proven and probable ore reserves as of year-end 2003 in accordance with the CIM Guidelines. These estimates would be identical under the applicable rules and regulations of the SEC and such definitions are substantially the same as the corresponding definitions under the SEC rules and regulations. Reference is made to Note (3) to such tables for additional information on how the reserve estimates for the 2002-2003 period were prepared.

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During 2002, Inco proceeded with the commercial development of the Goro project. In early September 2002, the project experienced labour disruptions by personnel associated with certain project construction subcontractors. As a result of these disruptions, a decision was made to curtail certain activities at the project site to enable Goro Nickel, contractors, subcontractors and other interested parties to develop procedures to avoid future disruptions. Over the September to November 2002 period, a number of procedures were put in place as part of a phased resumption of certain of the project activities that had been curtailed. At the same time that the labour disruptions referred to above occurred, Inco began updating the status of certain key aspects of the project, including the necessary permitting, capital cost estimate, project schedule and organization. Work on certain critical parts of the project, including engineering, continued during this update process.

On December 5, 2002, the Company announced that it would be undertaking a comprehensive review of all key aspects of the Goro project. This action was based upon information received by the Company from the joint venture companies referred to above acting as the prime construction contractors that, if confirmed, would indicate an increase in the capital cost estimate for the project in the range of 30 to 45 per cent above the then current capital cost estimate of \$1,450 million. The objective of the comprehensive review was to assess all information on the Goro project, including the various cost estimates and trends, and determine what changes in the capital cost estimate and the project could be made to maintain the project's economic feasibility. As a result of the temporary suspension of certain development activities and other actions which had been taken by year-end 2002 during this review process, the Company recorded a pre-tax charge of \$25 million in the fourth quarter of 2002. This charge was comprised of pre-tax expenses of \$62 million relating to the cancellation or termination of certain outstanding contractual obligations, to accrue for demobilization costs and to reduce the carrying value of certain assets relating to the project, partially offset by currency gains of \$37 million as a result of the ineffectiveness of certain forward currency contracts that had been entered into for hedging purposes. As part of the comprehensive review, we also evaluated various contractual and other arrangements covering construction and other work relating to the Goro project and implemented certain actions to suspend or terminate certain of those contractual arrangements.

As the comprehensive review of the Goro project that began in December 2002 moved forward during 2003, it evolved into two phases. The first or initial phase, which was completed in July 2003, focused on the identification of issues that had resulted in, or created, actual or potential increases in capital costs and how those issues could be addressed and other actions that could be taken to reduce these costs. On August 13, 2003, we announced the results of the initial phase of the review. The second phase, or Phase Two, which began essentially in August 2003, is intended to evaluate further opportunities to reduce costs and develop, among other key deliverables, a new capital cost control estimate, project scope and schedule and execution plan for the project. While one of the Company's objectives of Phase Two of our review is to have a capital cost estimate for the project of \$1.8 billion, the conclusion of that review could result in a capital cost estimate higher than this objective.

As of December 31, 2003, the Company had spent approximately \$600 million on the Goro project since July 1, 2001 when this project was formally launched. This amount excludes a current estimate of approximately \$58 million that would still have to be spent for equipment, services and other requirements under existing contracts and commitments, and accruals of approximately \$31 million relating to such requirements as of December 31, 2003, most of which expenditures are expected to have value for the project. The Company currently believes that, based upon the focus on certain potential new approaches to construction as part of, and the expected results of, the Phase Two review as it moves to completion, it will be required to take additional non-cash charges beyond those taken in the fourth quarter of 2002 but we cannot predict at this time the amount of such non-cash charges and whether they will have a material effect on our results of operations, financial condition or profitability.

While the key objective of Phase Two of the review is to have a project that will produce an acceptable rate of return on the investment to be made in this project, if, upon completion of this phase of the review, the Company were to conclude that the Goro project could not proceed or be restructured to meet our rate of return on investment requirements, the Company currently expects that it would undertake a further evaluation to determine how the project could be restructured to provide an acceptable return on the investment to be made. Depending upon the timing of the completion of such further evaluation, or if that further evaluation did not occur

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or did not result in achieving an acceptable return, the Company would have to consider writing off all or a substantial portion of the carrying value of the Goro project, approximately \$802 million at December 31, 2003, and the Company would also lose the expected future production from Goro. Such a result would have a material adverse effect on our business, results of operations, financial condition, profitability and cash flows.

The New Caledonian authorities enacted a fiscal regime in 2001 which provides a nominal 15-year tax holiday plus an additional five years at tax rates that are 50 per cent of the prevailing tax rates for qualifying metallurgical companies. If the project achieves an internal rate of return in excess of a cumulative threshold rate during this 20-year period, the applicable tax rates or levels for the project would then be adjusted prospectively to be equivalent to the general rates or levels then in effect for mining and processing companies.

New Caledonia is currently an overseas territorial community (*collectivité territoriale*) of France having special legal status under the French constitution, including significant autonomy except in foreign relations, defence, justice, currency and certain other related areas. As part of the objective of increasing New Caledonia's autonomy from France and to implement arrangements to address political and other issues that New Caledonia had experienced, in 1998 the French government, the New Caledonian government and two New Caledonian political movements representing the native population entered into the Noumea accord. This accord sets forth a process and timetable for increasing the autonomy of New Caledonia over the next 14 years, culminating in a referendum to be held by 2018 on whether New Caledonia would become fully independent from France. As part of the initial phase of the accord, steps have been taken, and will be taken over the next few years, to develop the form of provincial governments to be part of the New Caledonian government structure and to pass local legislation, including the enactment of a new mining law, that will provide for the transfer of certain authority in a number of areas still maintained by France to the New Caledonian government. The Company does not believe that these developments will have an adverse effect on the Goro project but there can be no assurances in this regard. Provincial elections are currently planned for early May 2004 for the election of members of the three provincial assemblies in New Caledonia. Each assembly will select its president and who will be part of the province's executive board. The members of the newly elected provincial assemblies will also select the persons who will serve as members of the Congress of New Caledonia. This Congress is responsible for the selection of the President of New Caledonia.

In September 2001, Goro Nickel S.A. (then known as Compagnie des Mines de Xere) applied for an exploration permit for an area next to the Goro deposit known as Prony West. Several other companies applied for the same exploration permit. After an assessment of the various applications, the government of the South Province of New Caledonia determined that Goro Nickel's application as being the best technically and offering the greatest financial commitment. As such, the South Province's recommendation to accept Goro Nickel's application was discussed at the mining committee (*Comité Consultatif des Mines*) in April 2002 and the recommendation to accept Goro Nickel's application was subsequently approved by the mining council (*Conseil des Mines*) the same day. In July 2002, after a public debate on the awarding of this exploration permit, the legislative assembly of the South Province voted to award the Prony West exploration permit to Goro Nickel. As soon as this decision was made, several companies challenged the South Province's decision. The administrative tribunal which considered this challenge released its decision on December 24, 2003. The administrative tribunal decided that the legislative assembly of the South Province did not have the authority to make the award as this authority had been previously delegated to the Executive Committee of the South Province and that the delegation had not been withdrawn. As a result of this decision, the exploration permit previously awarded to Goro Nickel was cancelled. However, after the cancellation of this permit, on December 27, 2003 the Executive Committee of the South Province met and reawarded the exploration permit to Goro Nickel. This decision to reaward the permit to Goro Nickel is open to challenges until April 20, 2004. As of March 12, 2004 no such challenges have been made.

***Voisey's Bay Nickel Company Limited******Voisey's Bay Deposit***

The Voisey's Bay deposit consists of three main bodies of mineralization, the Ovoid, the Eastern Deeps and related deposits and the Western Extension, including the Reid Brook and Discovery Hill zones and other small

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zones. As of year-end 2003, as reflected in the tables entitled "Total Estimated Ore Reserves as of Year-End 2003 and 2002" under "Ore Reserve and Mining Rights" above, proven and probable ore reserves of 30 million tonnes grading 2.85 per cent nickel, 1.68 per cent copper and 0.14 per cent cobalt were estimated for the Ovoid, based on a mill throughput of 6,000 tonnes per day. Reference is made to the notes to these tables for information on how these reserves were estimated and how the Company meets certain Canadian securities regulatory requirements for the purpose of any ore reserve estimates it might prepare.

While the Ovoid deposit is accessible by open-pit mining, most of the mineralization discovered to date in the remaining bodies is not amenable to open-pit mining. Preliminary mining assessments were carried out on the Eastern Deeps, Discovery Hill and the upper portion of the Reid Brook deposits in 2002 and early 2003. The results of these assessments were used to plan the 2003 advanced exploration program. The results of this ongoing surface exploration program, which is continuing as part of the 2004 exploration program, will be used to delineate these deposits sufficiently to carry out preliminary feasibility studies for these deposits. Several additional target areas have been identified on the Voisey's Bay main block of claims. These are geophysical targets well to the east of the known deposits and are planned to be assessed as part of the 2004 exploration program.

VBNC's exploration expenditures in Labrador totalled \$1 million in 2003, compared with \$180,000 in 2002 and \$4 million in 2001. Although definition drilling was carried out on the Discovery Hill and Reid Brook Zones as part of the first phase of the 2003 advanced exploration program, no exploration drilling was carried out in 2003 and only a limited amount is planned for 2004. Most of the 2003 exploration work was concentrated on further evaluation of the Ryan's Pond prospect which is located on the main block of claims approximately three kilometres to the east of the known deposits. The program consisted of geophysical surveys, including borehole and surface electromagnetic surveys. Evaluations of the exploration claims held by VBNC in Labrador continued in 2003 and by the end of the year none of the regional claims, outside of the main block of claims which contains all the currently known ore reserves, were considered to have any further exploration potential and these claims were relinquished to Archean under the terms of the Option Agreement referred to above.

*Environmental Review Process*

The scope of the environmental review and approval process for the Voisey's Bay project was established under a January 1997 memorandum of understanding among the Governments of Canada and the Province of Newfoundland and Labrador (the "Province"), the LIA and Innu Nation on a harmonized environmental review process for the mine, concentrator and related facilities and infrastructure in the Voisey's Bay area (the "Mine/Concentrator Project").

The Mine/Concentrator Project was the first major mining project to be subject to full review under the *Canadian Environmental Assessment Act* since this legislation came into effect in January 1995. In early 1997, a five-person environmental assessment panel was selected pursuant to the January 1997 memorandum of understanding to conduct the environmental assessment of the Mine/Concentrator Project. The environmental assessment process, including public hearings, were held over the 1998 to 1999 period and the panel issued its report and recommendations in April 1999. The panel recommended that the Mine/Concentrator Project proceed subject to a number of other separate recommendations. In August 1999, the federal and provincial governments announced their respective detailed responses to the environmental assessment panel's recommendations. Both governments released the Mine/Concentrator Project from the environmental assessment process subject to certain terms and conditions, including measures intended to mitigate potential environmental effects relating to the Mine/Concentrator Project, and accepted a number of the panel's recommendations. The Company does not believe that those recommendations or the terms and conditions of the releases stipulated by the governments will create any unduly burdensome financial or other restrictions on the Mine/Concentrator Project.

In 1999, the federal and provincial governments entered into negotiations with the LIA and Innu Nation to develop a project-specific environmental management agreement for the issuance of the necessary governmental licences and permits for the Mine/Concentrator Project. With the agreement on the commercial development of the Voisey's Bay project which having been reached in mid-2002, as discussed below, these discussions restarted and in July 2002 the governments entered into an environmental management agreement with the LIA and Innu

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Nation which created an environmental management board in order to provide for participation by these aboriginal groups in the process leading to the issuance of the necessary licences and permits for the Mine/Concentrator Project. The environmental management board has been meeting since it was created in July 2002 to address the issuance of the necessary permits and licences for the Mine/Concentrator Project, including the mining and surface leases issued to VBNC pursuant to the definitive agreements entered into with the Province of Newfoundland and Labrador, as discussed below. In 2003, over 100 permits were issued for the construction and operation of the Voisey's Bay project.

In early September 1999, separate court actions were filed in the Canadian federal courts by the LIA and Innu Nation asserting that the federal government should have imposed additional conditions to, and did not meet certain consultative and other requirements in arriving at, its decision to release the Mine/Concentrator Project from the environmental assessment process. These actions were stayed pending the outcome of the ongoing negotiations of separate impacts and benefits agreements ( IBAs ) with the LIA and Innu Nation and in the summer of 2002 both of these court actions were discontinued as conditions to the effectiveness of the IBAs that VBNC entered into with the two aboriginal groups, as discussed below. In addition, in mid-October 1999 another aboriginal group, the Nunavik Inuit, filed an action against a federal minister in the Canadian federal courts, asserting that its rights had not been properly considered or protected in land claims negotiations and the agreement in principle on land claims reached in May 1999 between the federal government and the LIA. This dispute was settled and the action was discontinued by the Nunavik Inuit.

*Negotiations with Aboriginal Groups*

In June 2001, when confidential negotiations with the Province restarted on the terms that would enable the project to proceed, VBNC also resumed separate IBA negotiations with the LIA and Innu Nation. VBNC reached agreement on IBAs with both the LIA and Innu Nation in May 2002. These IBAs were subsequently ratified by the respective memberships of the two aboriginal groups and were signed by the parties effective July 29, 2002. The IBAs set forth (i) certain payments to be made to the LIA and Innu Nation by Inco and VBNC over the life of the Voisey's Bay project, (ii) programs relating to training, employment and business opportunities for the LIA and Innu Nation and (iii) the participation of the LIA and Innu Nation in environmental and certain other programs and procedures relating to the operation of the Mine/Concentrator Project, among other things.

The Company understands that, following separate confidential negotiations between each of the LIA and Innu Nation and the Governments of Canada and the Province of Newfoundland and Labrador, interim agreements were reached to resolve the respective land claims of the LIA and Innu Nation in July 2002. Neither VBNC nor the Company was a party to these agreements nor to the negotiations leading to those agreements. The LIA has since reached agreement with the federal and provincial governments on how their claims relating to Voisey's Bay would be addressed in its final land claims agreement, as well as an interim measures agreement to allow the Mine/Concentrator Project to proceed. The Company understands that the federal and provincial governments and the LIA during 2003 continued their negotiations towards the conclusion of a final comprehensive land claims agreement among those parties. The Company also understands that the LIA in early 2004 commenced a community-based ratification process to ratify the final comprehensive land claims agreement among those parties.

Innu Nation had indicated in January 1999 that it was evaluating the alternatives available to it in pursuing its land claims. In the fall of 2000, Innu Nation and the federal government began negotiating the registration of the Innu people of Labrador to become eligible for benefits under the *Indian Act* (Canada). Innu Nation has also reached agreement with the federal and provincial governments on how their claims relating to Voisey's Bay would be addressed in its final land claims agreement, and entered into a memorandum of agreement under which Innu Nation agreed, among other things, not to assert any aboriginal land claims in the Voisey's Bay area, thereby allowing the Mine/ Concentrator Project to proceed. The Company has been advised that the Innu of Labrador were registered for eligibility under the *Indian Act* in November 2002, and that work continues on the creation of Indian reserves for Innu communities in Labrador. The Company also understands that the federal and provincial governments and Innu Nation in 2003 continued negotiations towards the conclusion of a final comprehensive land claims agreement, but no such agreement has as yet been reached.

**Table of Contents***Negotiations with the Provincial Government*

In mid-1998, following confidential discussions with the Government of Newfoundland and Labrador, the Company and VBNC proposed to provincial officials an initial Mine/ Concentrator Project to produce intermediate concentrate from the Voisey's Bay deposit, with the concentrate to be further processed at the Company's existing processing facilities in Ontario and Manitoba, where there will be excess capacity. As part of this initial phase of the project, the Company proposed to carry out an extensive underground exploration program to determine the economic feasibility of the underground deposits at Voisey's Bay. The Company's proposal also included the development, if and when economic, of additional processing facilities in the Province. This approach is similar to the approach used successfully in Sudbury and other nickel locations where facilities have been developed in stages as additional ore reserves have been proved. In July 1998, the Province turned down this proposal and suspended negotiations with the Company.

Over the last half of 1999, the Company engaged in discussions with the provincial government on a revised project framework for development of the Voisey's Bay deposit. These negotiations did not result in an agreement as the Province insisted that the Company provide an unconditional guarantee that processing facilities would be built in the Province, even if they were not economic. No further negotiations were held until June 2001, when the Company resumed confidential negotiations with representatives of the Province of Newfoundland and Labrador concerning the terms of an agreement on the commercial development of the Voisey's Bay deposit. These negotiations continued in the first half of 2002 and on June 11, 2002 the Company and the Government of Newfoundland and Labrador announced their agreement on a non-binding statement of principles covering the development of the Voisey's Bay project. The statement of principles was approved by the provincial legislature in late June 2002 and on October 7, 2002 Inco and VBNC signed definitive agreements with the Government to implement the terms of the statement of principles. The definitive agreements provide for the development of a mine and concentrator processing plant at Voisey's Bay, representing the Mine/ Concentrator Project, a research and development program focusing on hydrometallurgical processing technologies, an industrial and employment benefits program for the Voisey's Bay project, a timetable for the start and completion of the principal stages of the project, and other key parts and requirements covering the overall development of the Voisey's Bay project. The definitive agreements set forth certain obligations of the Company to construct and operate (i) a demonstration plant in the Province as part of the overall research and development program to test hydrometallurgical processing technologies to treat nickel-containing ores or intermediate products from the Voisey's Bay deposits and (ii) subject to technical and economic feasibility pursuant to the terms thereof, a commercial processing facility in the Province by the end of 2011 to treat all of the Voisey's Bay ores or intermediate products to produce finished nickel and cobalt product based upon hydrometallurgical processing technologies or, if such technologies do not meet certain technical and/or economic feasibility requirements, as may be determined by one or more agreed upon experts as provided for in such agreements, a conventional refinery. Once the demonstration plant is completed and has received intermediate concentrate product from the Mine/ Concentrator Project for testing, Inco can ship quantities of intermediate concentrate products produced by the Mine/ Concentrator Project containing nickel and/or cobalt to the Company's facilities in Ontario and Manitoba for further processing into finished nickel and cobalt product. Shipments of such Voisey's Bay intermediate concentrates are limited to certain maximum aggregate quantities and will end when the construction of the hydrometallurgical or conventional matte commercial processing facility, as the case may be, is completed.

Under the definitive agreements, Inco is also required, prior to the cessation of the Voisey's Bay mining operations in the Province, subject to certain exceptions relating to the availability of such external sources, to bring into the Province for further processing at the hydrometallurgical or conventional matte processing facility to be constructed in the Province from sources outside the Province, in one or more intermediate forms, quantities of intermediate products, subject to certain annual minimum quantities, containing in total quantities of nickel and cobalt equivalent to what was shipped to the Company's Ontario and Manitoba operations. The definitive agreements also set forth (1) the Company's commitment to an underground exploration program covering the Voisey's Bay deposits with the objective of discovering sufficient nickel-containing ore reserves for processing beyond the initial phase of the Voisey's Bay project, (2) the terms under which the processing of copper intermediate in the Province would be justified, and (3) the Province's commitment to (i) the tax regime that will

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apply to the project, (ii) electric power rates for the project and (iii) the issuance of the necessary permits and authorization to enable the Voisey's Bay project to proceed. The definitive agreements also provide for programs and arrangements relating to employment and industrial benefits in connection with the construction and related aspects of the project. The definitive agreements also include specific sanctions if the Company were not to meet certain of its contractual obligations under such agreements, including the effective forfeiture of its lease to conduct mining operations in the Province. Under the terms of the definitive agreements, certain provisions became effective when these agreements were executed. The next steps which were to be met by the end of the first quarter of 2003 for these agreements to become effective overall include the securing of acceptable financing arrangements for the project and completing a bankable feasibility study for the first phase of the project, including the Mine/ Concentrator Project. As discussed under *Project Phases* below, the bankable feasibility study was completed in late March 2003. In March 2003, the Company advised the Province that it was waiving the financing condition in these agreements. The remaining conditions to the effectiveness of these agreements were met in the third quarter of 2003.

*Project Phases*

The Company announced in late March 2003 (i) the results of a bankable feasibility study for the mine and concentrator for the Ovoid and adjacent surface deposits and related facilities representing part of the initial phase of the Voisey's Bay project and (ii) that it planned to proceed with this initial phase. Based upon the results of the study, the estimated total capital cost for the Mine/ Concentrator Project was estimated to be \$582 million, including \$35 million spent since July 2002 on infrastructure and related work. The \$582 million amount represented an increase of \$77 million or about 15 per cent over the prefeasibility study estimates for the Mine/ Concentrator Project. This estimate included a \$54 million contingency. The initial phase of the Voisey's Bay project will also involve a research and development program covering hydrometallurgical processing technologies (the Hydromet R&D Program) for the treatment of the Voisey's Bay nickel and cobalt-containing concentrates to be produced into finished nickel and cobalt product, including a demonstration plant to be constructed in Argentina, Newfoundland. As of March 2003, the Hydromet R&D Program was expected to cost approximately \$134 million or about 14 per cent above the initial estimate for this program. It is possible that the cost of this program may be higher but we cannot currently predict what the increase in such cost will be. In addition to the Mine/ Concentrator Project and the Hydromet R&D Program, the initial phase will include handling facilities to be constructed at our Canadian operations for the nickel and cobalt-containing concentrates to be processed over the 2006-2011 period once the Mine/ Concentrator Project and the demonstration plant are in operation, at an estimated cost of \$47 million, and an exploration program at an estimated cost of \$13 million. The total capital cost estimate for all four parts of the initial phase of the Voisey's Bay project is \$776 million, or about 14 per cent above the original estimate of \$680 million. The engineering firm retained to complete the study indicated that it believed that the capital cost estimate was within a range of plus 15 per cent and minus 5 per cent of the \$547 million figure still to be spent for the Mine/ Concentrator Project. Given that we currently expect that a significant portion of these costs will be incurred in Canadian dollars, we have entered into Canadian dollar hedges for approximately 68 per cent of the total expected costs in Canadian dollars for the related assets, including Cdn. \$535 million of hedges at an average exchange rate of \$0.746 entered into as at March 12, 2004. The \$776 million estimate assumed a Canadian dollar-U.S. dollar exchange rate of approximately Cdn.\$1.00 to \$0.66. At exchange rates in effect at March 12, 2004, taking into consideration the forward currency contracts noted above, this estimate would be \$888 million. To the extent that this currency exposure is not hedged at exchange rates equivalent to this assumed rate, then this capital cost estimate could rise, adversely affecting the projected returns on our investment in this project.

As discussed above, the Company began infrastructure, site development and other work in July 2002 with respect to the initial phase of the project of approximately \$35 million over the July 2002 to March 2003 period. The Company currently expects initial concentrate production from the first phase of the project in 2006 for shipment to the Ontario and Manitoba operations while the hydrometallurgical process is being tested in the planned demonstration plant. Assuming technical and economic success, a commercial hydrometallurgical processing plant will be built as part of the second phase of the project between 2009 and 2011. As noted above, in the unlikely event that the hydrometallurgical process proves not to be technically and/or economically feasible, a conventional refinery will be built to produce finished nickel product. It is expected that the Voisey's

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Bay hydrometallurgical plant will produce approximately 50,000 tonnes of nickel, 2,300 tonnes of cobalt, up to 7,000 tonnes of copper intermediates, and 32,000 tonnes of copper concentrate annually. A total investment, based upon the updated capital cost estimate for the initial phase and the prefeasibility studies for the other two phases of the project, of approximately \$2,000 million would be required for all phases of the project over the 30-year life of the project, including estimated sustaining capital.

### *Asset Impairment Charge*

On June 11, 2002, Inco announced that it would be undertaking a review of the net carrying value of the Voisey's Bay project in view of the statement of principles entered into with the Government of the Province of Newfoundland and Labrador on that date and other arrangements with key stakeholders that would enable the development of the Voisey's Bay project to proceed. The Company had previously noted on a number of occasions in its public filings and other documents that such events, if and when they were to occur, might require a significant reduction in the carrying value of the Voisey's Bay project and in the related deferred income and mining tax liability and in shareholders' equity. This review, which was completed in July 2002, included an analysis of the key assumptions which the Company utilized in evaluating this net carrying value on a quarter-to-quarter basis relating to a number of important factors, including the Company's best assessment of the expected cash flows from the project, how the development of Voisey's Bay, taking into account the agreements which have been reached, fits within the Company's overall long-term development plans and updated mining and other cost assumptions. As a result of this review, the Company recorded a non-cash charge of \$1,552 million, net of deferred income and mining taxes of \$770 million, in the second quarter of 2002 to reduce the \$3,753 million net carrying value of the Voisey's Bay project to \$2,201 million. In 2000, as a result of a change in Canadian generally accepted accounting principles, the deferred income and mining tax liability associated with Voisey's Bay was increased by \$2,222 million and the carrying value of Voisey's Bay was also increased by this same amount.

### *Exmibal*

The mining and processing facilities of the Company's 70 per cent-owned Guatemalan subsidiary, Exploraciones y Explotaciones Mineras Izabal, S.A. (Exmibal), which has a design capacity of about 11,300 tonnes of nickel-in-matte annually, have been mothballed since 1982. Exmibal has a nickel deposit which could be brought back into production under appropriate market conditions. However, the recommencement of operations at these facilities would require substantial capital expenditures and start-up costs.

During 2003 Inco continued to have preliminary discussions with parties interested in developing the existing power plant facility as part of a power generating project in Guatemala and acquiring certain rights to develop the Exmibal deposits. A letter of intent was entered into in November 2003 covering the possible terms under which the Exmibal deposits could be commercialized by one of these parties. A number of terms and conditions, including obtaining satisfactory financing, would have to be met under the letter of intent to enable the party seeking to develop such deposits to obtain certain rights covering such development, subject to meeting certain milestones. The letter of intent provides that Inco would receive a minority interest in the company who would commercialize these deposits and have certain rights, including, the right market in products produced by that company and to use any proprietary technologies developed by that company.

### *Exploration and Project Development*

One of the objectives of Inco's exploration program is to provide the Company with sufficient ore reserves to sustain production at current levels for at least 20 years at its Ontario and Manitoba operations. See *Mining and Production - General* above for further information on the Company's planned production levels and *Ore Reserves and Mining Rights in Canada* above for information on the Company's proven and probable ore reserves. The Company continues to pursue exploration opportunities for platinum-group metals in Ontario.

Exploration expense totalled \$27 million in 2003, compared with \$24 million in 2002 and \$23 million in 2001. Exploration efforts continue to focus on finding additional high-grade nickel deposits in Canada near existing mine workings to expand the Company's estimated ore reserves and provide additional feed for existing



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processing facilities. Of the total exploration expenditures in 2003, \$11 million was spent on exploration in Ontario and Manitoba directed at finding additional nickel, copper and platinum-group metals estimated ore reserves near the Company's existing mines, compared with \$9 million in 2002 and \$10 million in 2001. Additions to estimated ore reserves from the evaluation of diamond drilling in 2003 totalled 2.5 million tonnes averaging 1.5 per cent nickel and 2.7 per cent copper at the Company's Ontario operations and 1.9 million tonnes averaging 1.5 per cent nickel and 0.1 per cent copper at the Company's Manitoba operations. The Company also continued to evaluate non-nickel exploration targets and joint venture opportunities that have the potential to enhance the Company's overall mining operations.

In 2003, deteriorating ground conditions at the Ontario operations' Copper Cliff North mine reduced production from that mine's 138 ore body high-grade precious metal zone. As a result, the additional production of precious metals (platinum plus palladium plus gold) that was expected to be produced from that mine in 2003 was not realized. The ground conditions problem was resolved and it is expected that the quantities of precious metals that had been planned to be produced from this mine's 138 ore body will be achieved in 2004, bringing the total expected production of precious metals from this zone to about 2,000 kilograms in 2004. Exploration drifting on the 3,400-foot level of this mine is scheduled to be completed in 2004, allowing drilling of this mine's lower 138 ore body high-grade precious metals zone. A feasibility study is currently being completed on the mineralized material that forms a halo surrounding the 138 ore body from the 1,050-foot level to the 1,400-foot level. A feasibility study on the remnants of the upper 138 ore body was completed in 2003. Work in 2004 is expected to be focused on the inclusion of this remnant ore into the production plan for the Copper Cliff North mine.

By the end of the first quarter of 2004, the physical connection between the Company's Ontario operations' Copper Cliff North and Copper Cliff South mines is expected to be complete. Some equipment and services will be shared between the mines and the connection will provide the Copper Cliff North mine with ramp access to the surface through Copper Cliff South mine. Work is then expected to begin on a drive on 3,400-foot level of the Copper Cliff North mine to that mine's 880 ore body which will provide access to explore for potential down-dip extensions to that ore body.

In 2003, exploration drilling continued on the 191 ore body of the Copper Cliff North mine with respect to a potential new zone located adjacent to the footwall of the main 191 deposit at the 4,600-foot to 4,800-foot levels. This program is planned to continue in 2004.

Underground exploration drilling continued in 2003 on the 170 footwall high-grade precious metals deposit at the Ontario operations' McCreedy/ Coleman mine. The drilling and follow-up evaluations have resulted in the addition of 0.2 million tonnes of estimated ore reserves, bringing the estimated ore reserve for this deposit to 1.8 million tonnes of probable ore reserves grading 7.0 per cent copper, 0.9 per cent nickel and 15.1 grams per tonne of combined platinum, palladium and gold. Advanced exploration is planned in 2004 to expand the estimated ore reserve and assess the detailed variation in the thickness and orientation of the sulphide veins found in this deposit. The \$33 million Phase 2 project to develop a high-grade nickel deposit at McCreedy/ Coleman Mine, which was announced in 2000, was under budget and on schedule until the work stoppage that occurred as a result of the three-month strike which began June 1, 2003. This project is expected to allow McCreedy/ Coleman Mine to increase its production by over 60 per cent from 2002 levels by early 2005. The \$34.8 million Phase 3 project for this mine, which was announced in 2003, was also on budget and on schedule until the work stoppage.

The Company's surface exploration program continued in 2003 to test and evaluate both near-mine and new exploration targets in the South Range and East Range of the Sudbury basin, the Copper Cliff and Worthington Offsets and the footwall of the North and East Range.

At the Copper Cliff offset, a surface drilling program was initiated to test large gaps in drilling located between the Pump Lake mineral deposit at the Copper Cliff North mine and the Murray mine. This program was halted as a result of the three-month strike at the Ontario operations but will resume in 2004.

An advanced surface exploration program was completed in 2003 at the 740 zone in the Kelly Lake ore body at the Copper Cliff South mine. This program was successful in further defining continuity and grade distribution

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of the zone and increasing the grade and tonnage of the estimated ore reserve. In addition, the program identified further exploration targets for follow-up in 2004.

An exploration program was initiated in the East Range of the Sudbury basin designed to follow up on geophysical conductors identified during an ongoing program of resurveying and deepening old exploration boreholes. Exploration focused on the Ella Lake area where a new zone of contact mineralization was identified. Further drilling is planned to the footwall of this zone for high-grade footwall-type mineralization in 2004.

In October 2000, a decision was made to proceed with a \$12 million project to develop the low-grade area of the Ontario operations Stobie mine. The development and construction needed for production to begin through the ore-handling component of this project was completed in late 2001. Ongoing lateral development and construction on the individual mining levels are scheduled to continue until the end of 2005. Production from this project began in 2001 and is expected to be at 5,900 tonnes of ore per day in 2004, increasing to 6,700 tonnes of ore per day in 2006. The current plans are to operate a new ore-handling system as part of this project until the end of 2006.

In 2003, development work continued on the first of the expected two phases of the Creighton Deep project, a project that was originally announced in 1998. Capital expenditures on this project totalled \$2.7 million in 2003. The development of the second production level (the 7,680-foot level) as part of the first phase began in early 2003 and the first phase of the project is expected to be completed in 2006. Production from the first phase totalled 111,800 tonnes of ore grading 4.0 per cent nickel and 2.5 per cent copper in 2003 and production is expected to continue at a rate of approximately 300,000 tonnes of ore per year until 2015 if the Company proceeds with the second phase of the project. The Company is currently evaluating the second phase of this project which would involve access to an additional ore body at Creighton Deep. The estimated ore reserve that would be accessed in the second phase of the project is 4.0 million tonnes grading 3.7 per cent nickel and 3.9 per cent copper between the 7,680-foot level and the 8,220-foot level. This estimate includes an additional 660,000 tonnes of ore grading 4.0 per cent nickel and 5.1 per cent copper added in 2003 as a result of exploration in a high-grade footwall zone.

In 2002, a decision was made to proceed with a \$67 million project to deepen Garson mine from the 4,470-foot level to the 5,070-foot level to access seven million tonnes of proven ore reserves grading 1.76 per cent nickel, 1.37 per cent copper and 1.1 grams per tonne of combined platinum-group metals and gold. This project is expected to increase mine production at Garson Mine by 10 per cent to 2,087 tonnes of ore per day and extend the life of the mine until approximately 2012. Construction of major mine facilities and development as part of this project started in the summer of 2002. The project is on schedule to ramp-up to full production by the fourth quarter of 2004.

In January 2002, the Company entered into an option agreement with FNX Mining Company Inc. ( FNX ) relating to certain rights extended to FNX to explore and develop five non-core properties of the Company in the Sudbury basin. The properties covered by this agreement all have a history of past production but were inactive and the Company had no further plans for the exploration or development of these properties. Subject to meeting certain conditions enabling it to exercise the option to acquire a 100 per cent interest in the mineral rights to these properties, FNX agreed, pursuant to the terms of the option agreement, to spend Cdn.\$14 million over a 16-month period beginning in January 2002 and was granted an option to earn a 100 per cent interest in the mineral rights in these properties by spending a further Cdn.\$16 million over the next four years. On December 10, 2003, FNX announced that, effective December 1, 2003, it had completed its total expenditure commitment and had exercised its option to acquire a 100 per cent interest in the mineral rights covering the properties. As part of the agreement, Inco had initially acquired common shares and common share purchase warrants of FNX representing a total equity interest in FNX of 19.9 per cent on a fully-diluted basis. However, the Company's ownership position was diluted to about 12 per cent as of year-end 2002 due to the issuance of additional shares by FNX and the sale of FNX shares by the Company. The Company completed the sale of its shares in FNX in May 2003. Under the terms of a related offtake agreement, Inco also has the right, but not the obligation, to purchase and refine all of the ore production from the properties covered by the option agreement. During 2003, exploration, consisting of surface and underground diamond drilling, ground and airborne geophysics, mapping, and prospecting was carried out on the properties covered by the option agreement. In addition FNX's partner,

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Dynatec Corporation, commenced advanced underground exploration, development and mining at one of the properties. FNX is currently shipping ore to the company from one of the properties under the offtake agreement.

In the Thompson nickel belt, the regional surface exploration program continued over the OIC Leases that were issued to the Company by the Province of Manitoba. The surface geophysical component of the regional exploration program was completed in 2003. Follow-up drilling on several targets which had been outlined was carried out. The drilling confirmed the presence of the favourable ore-hosting formations and approximately 90 per cent of the drill holes intersected zones of sulphide, confirming the effectiveness of this exploration method. Several of the holes did intersect narrow widths of nickel-bearing sulphides. However, these intersections, although encouraging, are not currently viewed as having a high potential to represent an economic deposit. Several target environments would require additional drilling and two have not yet been drilled. No additional work is, however, planned in these areas during 2004.

Underground exploration continued in 2003 at both the Thompson and Birchtree mines at the Manitoba operations to test for extensions to known deposits and to identify new satellite deposits.

An advanced exploration program continued in the 1-D Lower ore body of the Thompson mine located below the 1,100-metre level. Drilling has provided more detail on the shape of the deposit and the distribution of grades, and added to the estimated ore reserves. In the third quarter of 2003, a feasibility study was completed for a portion of the 1-D Lower ore body between the 1,100-metre and 1,280-metre levels. Estimated ore reserves in this area include 1.9 million tonnes grading 2.2 per cent nickel of estimated proven ore reserves and 2.9 million tonnes grading 2.2 per cent nickel of estimated probable ore reserves. Initial ore from this orebody is planned to be accessed during the first quarter of 2004.

During 2003, additional drilling was completed on 30 metre spaced sections that extend the 1-D lower ore body to the south. The 1,068-metre level exploration drift was subsequently extended 150 metres further south and drilling continued late in the year. During 2003, a total of 13,698 metres of diamond drilling was carried out on the 1-D Lower ore body. Results from this work are being assessed and drilling is expected to continue on the southern extension of this ore body in 2004.

As discussed under Mining and Production General above, the Company's Manitoba operations have been transitioning from the high-grade Thompson mine, the principal source of ore for these operations, to the lower-grade Birchtree mine. In 2003, work continued on the two-year project to deepen Birchtree mine at the Manitoba operations at a cost of \$48 million, a project which is expected to extend the life of this mine by at least 15 years.

A drilling program was continued at the Birchtree mine in 2003 to test the down-dip extension of this mine's 108 zone above the 840-metre level. A total of 9,045 metres of drilling was completed in 2003. Results are being assessed and this program will continue in 2004, in conjunction with ramp development from the 1,050-metre level.

Exploration continued during 2003 at the Mel project, located 25 kilometres north of the City of Thompson, under the terms of an agreement signed with Nuinsco Resources Limited ( Nuinsco ), in August 1999. The agreement grants Nuinsco the right to acquire the mineral lease that covers the Mel deposit and 60 contiguous mining claims by incurring aggregate expenditures of \$6 million by February 2006, subject to Inco's right to buy back a 51 per cent interest in the deposit by spending the next \$6 million over a further four-year period. Under the terms of this agreement, all production from any commercial quantities of ore discovered would be delivered to Inco's Thompson facilities for processing on then prevailing market terms. During 2003, Nuinsco funded a program of surface downhole electromagnetic ( DHEM ) surveys and 987 metres of diamond drilling over favourable environments identified by Audio-magneto-tellurgic ( AMT ) surveys that were carried out by the Company. Massive sulphide was intersected that explains the DHEM anomalies but no significant nickel mineralization has been encountered on the Mel claims to date. Several DHEM conductors that are associated with the Pipe Formation have not been tested and additional surface DHEM surveys and diamond drilling are planned for the Mel project in 2004.

In 2003, exploration began at the TNB South project that is centred approximately 100 kilometres southwest of the City of Thompson. The property covered by this program is contiguous with the southwest boundary of the

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Inco OIC Leases and extends 50 kilometres further to the southwest. Canadian Royalties Inc., under the terms of an agreement entered into with the Company in October 2003, has the right to earn a 50 per cent interest in the property covered by the agreement by funding 100 per cent of exploration expenditures, totalling \$5 million over five years. Inco has a right of first refusal on all production from any commercial quantities of ore discovered. During 2003, line cutting in preparation for a regional AMT survey began. In addition to AMT surveys, surface DHEM and diamond drilling programs are planned for 2004.

In 2003, field exploration apart from the Company's producing mines and development projects focused on Brazil, Australia, the United States, Canada and China. In Turkey, the joint venture with Dowa Mining Co., Ltd. of Japan was terminated by mutual consent and operations by Inco's subsidiary, Dardanel, were terminated and the Company's exploration office in Ankara was closed.

In Brazil, a large-scale reconnaissance program with Teck Cominco Limited continued to explore for copper-gold and copper-zinc deposits. Inco's Brazilian subsidiary completed an exploration program on two copper-gold properties in the northeastern Brazilian states of Ceará and Piauí. No further work will be carried out on these properties. Canico Resource Corp. (Canico) completed the initial phase of a drilling and resource evaluation program on the Onça Puma nickel laterite property in the Carajas district in Brazil under agreements entered into in 2002 with the Company covering this property. Canico acquired a 100 per cent ownership interest in the property in February 2003 by raising \$22.5 million to complete a bankable feasibility study. As part of the agreements covering this property, Inco received initially a total equity interest, including warrants, of approximately 18 per cent in Canico. As of March 10, 2004, Inco's interest in Canico was about 14 per cent as a result of dilution from financings by Canico. Under the terms of a related offtake agreement, Inco has the right to process and/or market all product from the Onça Puma property. No fieldwork was carried out during 2003 in Peru, and the joint venture with Southwestern Resources Corporation covering certain properties in Peru was terminated.

In Australia, three copper-gold prospects and three lead-zinc prospects were drilled in collaboration with PlatSearch NL. In March 2003, a memorandum of understanding was signed with LionOre Australia Pty Ltd. whereby Inco would agree to spend Aus \$15 million over approximately a four year period on exploration for nickel on certain tenements in Western Australia. In the event of a discovery, Inco would earn the right to participate in further exploration on the properties to earn either an equity position in a major deposit or the right to purchase the production from the deposit.

In Canada, Inco's joint venture with Soquem continued during 2003, following up targets identified by airborne geophysical surveys flown by the Company over parts of Québec. Two joint ventures with Aurora Platinum Corp. in Northern Ontario continued in 2003 under which Aurora, using historic Inco airborne geophysical data, conducted follow-up exploration with Inco retaining a right to purchase any nickel, copper, and platinum-group metal products produced from the properties covered by these joint ventures, as well as the right to buy back into any properties acquired or elect to take a royalty. Inco entered into three new agreements in 2003 using Inco's historic airborne geophysical database. The agreements are with Aurora Platinum Corp. covering the Abitibi greenstone belt of Ontario and Québec, Canabrava Diamond Corporation, covering the Winisk area of Northern Ontario, and Freewest Resources Canada Inc., covering the Musketeer River area of Northern Ontario. Inco also completed a preliminary exploration program consisting of ground geophysical surveys and diamond drilling follow up on the Redstone nickel property which is under option from Timmins Metal Corp. Inco has the right to acquire a 70 per cent interest in the property.

Inco continued to actively evaluate exploration projects in China during 2003. Exploration was initiated on the areas covered by two cooperative joint venture agreements in Jilin province, one with Jilin Nickel Industry Group Ltd. and the other with Geological Survey Institute, Jilin Province, and exploration is planned to continue under these agreements in 2004. Memoranda of understanding covering certain exploration areas have also been signed in Yunnan and Sichuan provinces of China and the Company has been evaluating other exploration targets in China.

See Voisey's Bay Nickel Company Limited Voisey's Bay Deposit above for information on exploration activities at the Voisey's Bay project.

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All of the estimated ore reserves referred to in this section are included in the table entitled Company-wide estimated ore reserves under Ore Reserves and Mineral Rights above.

### ***Research and Development***

The Company's central research and development facility, J. Roy Gordon Research Laboratory ( JRGRL ), is located at Sheridan Park, Mississauga, Ontario. JRGRL is operated by Inco Technical Services Limited, a wholly-owned subsidiary of Inco Limited. In 2003, the Company commissioned its hydrometallurgy miniplant for the Voisey's Bay project in another building it acquired located in Sheridan Park.

The Company's research and development activities at JRGRL are organized into two groups, process research and product research.

Inco believes that it is a nickel industry leader in research and technology development. The Company's research and development focus is closely aligned with its key strategic objectives, including becoming the lowest-cost nickel producer and increasing revenue from value-added nickel products. The Company's major research and development projects currently include the development of metallurgical and environmental process improvements for existing operations, hydrometallurgical process development work, as part of the Hydromet R&D Program for the Voisey's Bay project, and the development of proprietary value-added nickel products. Research and development expenditures totalled \$27 million in 2003, principally due to increased spending on the Hydromet R&D Program, compared with \$17 million in 2002 and \$20 million in 2001.

Inco's process research and technology development work is conducted in partnership with operating teams at the Company's operating locations and its major project teams. These efforts are aimed at improving metals recoveries and achieving cost reductions, as well as developing opportunities for increased operating earnings through process modifications. During 2003, the process research group continued to assist in further improving the performance of the Clarabelle Mill, the Copper Cliff smelter and the refineries at the Company's Ontario operations. Further progress was made in 2003 towards improving smelter efficiencies through improved flash furnace utilization and throughput and in developing practical alternatives for the continued reduction of sulphur dioxide emissions from the Copper Cliff smelter. The Company also continued to work on the simplification of its processes for the recovery of platinum-group metals, gold and silver in order to lower operating costs.

At the Company's Manitoba operations, the process research group continued to work with mill and smelter personnel to address changes in ore composition that are anticipated as a result of the increased production of ore from Birchtree mine. As a result of this work, a new flotation circuit was successfully commissioned at the Thompson mill in 2003, resulting in significantly improved rejection of rock minerals without reducing nickel recoveries. In the future, the resulting higher concentrate grades may allow smelting through only one furnace at Thompson.

The process research group is also responsible for developing new processes for the recovery of nickel, cobalt and copper from the Goro and Voisey's Bay ores. During 2003, process research and process engineering personnel engaged in a successful program to demonstrate the Voisey's Bay milling process at the pilot plant scale and to continue the development, as part of the Hydromet R&D Program, of a hydrometallurgical process for Voisey's Bay nickel concentrate at the miniplant level. High concentrate grades of 20 per cent nickel and above were consistently achieved from the material from the Ovoid zone at approximately 90 per cent nickel recovery levels. Significant progress was made at the hydrometallurgy miniplant to define the process and the design parameters for the demonstration plant to be built at Argentia, Newfoundland and Labrador beginning in 2004. The new hydrometallurgy process is expected to produce nickel at significantly lower capital and operating costs than conventional smelting plus refining.

In the area of product research, Inco maintains a highly-focussed research and development program, aimed at creating new, proprietary value-added nickel products, as well as new applications for existing products, and at providing technical assistance to customers for these products. The product research group works in close collaboration with Inco Special Products, which has responsibility for all business activities related to the Company's specialty nickel products. Projects are led and conducted using cross-functional teams. A stage-gate process is employed to evaluate the technical and business success and opportunities.

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The rechargeable battery, powder-metallurgy, electronic and other markets continue to grow and broaden into diverse applications, creating new requirements for specialty nickel products. To serve these rapidly evolving markets, Inco's product research group has been developing new sintering nickel powders, extra-fine powders used in battery and electronic applications and nickel foam and felts for battery and fuel cell applications. During 2003, development of a fine nickel powder suitable for applications in the powder metallurgy industry continued. A new powder, tentatively called T110 PM, was introduced to selected users. It has potential applications in the press and sinter market, in diamond bonding, hard metals and metal injection molding.

On the basis of experimental work conducted in 2001 and 2002, a pilot plant for development and production of fine nickel powder for applications in multi-layer ceramic capacitors was constructed at the company's Novamet facilities in New Jersey. In addition to allowing the Company to study parameters with respect to the production of these powders, the pilot plant will enable the production of samples for commercial testing and will support the Company's possible commercial entry into this market.

The Company also operates a mines technology department at its Ontario operations. This department carries on projects in the areas of mines automation and mining methods and mine design, including projects relating to backfill and rock mechanics research. The mines technology department endeavors to leverage its resources through participation research consortiums with other mining companies.

***Metals Recycling***

Inco's subsidiary, The International Metals Reclamation Company, Inc. (Inmetco<sup>(8)</sup>), located near Pittsburgh, Pennsylvania, is a world leader in metals recycling. Using proprietary Inco technology, Inmetco recycles nickel, chromium and iron from stainless steel mill and metal finishing wastes and nickel and cadmium from spent batteries.

Inmetco's net sales to customers, which are included in Other in the table under Sales above, were \$35 million in 2003, compared with \$30 million in 2002 and \$29 million in 2001.

Certain feedstocks and by-products of Inmetco's process are regulated as hazardous or residual wastes by the U.S. Environmental Protection Agency (the EPA) and the Commonwealth of Pennsylvania. While such regulation increases the demand for Inmetco's services in some respects, it also increases Inmetco's operating costs. The Company expects that in the years ahead the EPA and the Commonwealth of Pennsylvania may issue a number of new regulations that could impose additional costs on Inmetco's operations, while other potential rules could reduce regulatory burdens. The Company is not able to predict at this time the effect that such additional regulations could have on its operating costs and financial condition.

***Environment, Health and Safety***

The Company's operations are subject to numerous environmental laws and regulations relating to, among other things, air emissions, water discharges, soils, recycling and waste management, decommissioning and reclamation, and employee health and safety. While environmental requirements vary considerably from country to country, future laws and regulations may be expected to impose stricter environmental requirements on the mining and metals processing industries in general, and on specific uses of certain metals. The Company devotes considerable resources to its performance under and compliance with the environmental, health and safety laws and regulations to which it is subject. However, the impact of future laws and regulations in these areas on the Company cannot be predicted with any degree of certainty.

***SO<sub>2</sub> Emissions******Sudbury***

Total sulphur dioxide (SO<sub>2</sub>) emissions at the Company's Ontario smelting operations were 169,000 tonnes in 2003, below the current maximum SO<sub>2</sub> emission limit of 265,000 tonnes which was established by the Government of Ontario in 1994. These emissions totalled 243,000 tonnes in 2002 and 232,000 tonnes in 2001.

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<sup>(8)</sup> Inco trademark.



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The reduction in SO<sub>2</sub> emissions in 2003 was due principally to the three-month strike at the Company's Ontario operations referred to above.

In February 2002, the Ontario Ministry of the Environment (the MOE) issued a control order (the February 2002 Control Order) requiring reductions of SO<sub>2</sub> emissions at the Company's Ontario smelting operations by 34 per cent, from the current limit of 265,000 tonnes to 175,000 tonnes annually, by the end of 2006, and reducing the limit for SO<sub>2</sub> ground level concentrations (GLCs) by 32 per cent, from the then current level of 0.50 parts per million (ppm) to 0.34 ppm, effective April 1, 2002. GLCs refer to the concentrations of SO<sub>2</sub> at ground level after being emitted from the emissions stack and forced to the ground by atmospheric conditions rather than being dispersed. Fugitive emissions, emissions which are caused when SO<sub>2</sub> gases exit the Company's operations through roof ventilation equipment, windows, doors and other openings, are also controlled under this order. During 2003 there were seven exceedences of the new GLC limit – four from the stack and three fugitive. This compares with three exceedences in 2002 – two from the stack and one fugitive. The Company is subject to possible regulatory action as a result of these exceedences, but has not received any indication from the MOE whether or not any charges will be laid. In order to continue to meet the SO<sub>2</sub> and GLC limits, it is likely that the smelter will be operated at reduced capacity for brief periods over the next few years when adverse meteorological conditions, such as temperature inversion events or the absence of wind, for plume dispersal exist.

In 2002, the Province of Ontario issued a discussion paper covering proposals for further reductions in SO<sub>2</sub> emissions by non-ferrous smelting operations in Ontario, including the Company's operations. The federal government of Canada has also recently designated for further regulation certain SO<sub>2</sub> and particulate emissions from copper-smelting operations such as those Inco has in Ontario. To this end, the Canadian federal government has proposed, on an informal basis, certain initiatives which would be applicable to metals processing operations in Canada, including those of the Company, that would have the effect of requiring operators such as the Company to prepare and submit a plan outlining measures to be taken to reduce these emissions to meet specified levels. While the Company does not currently believe that these initiatives will be put into effect, if they did come into effect as proposed they would require the Company to commit to material additional capital expenditures and/or significantly reduce our production of nickel and certain other metals by as early as 2008. While the Company is not able to determine the effect, if any, of these recent developments and significant changes in regulatory emission limits and other environmental laws and regulations that may be enacted in the future due to the uncertainty surrounding the timing and ultimate form that such changes may take, any such changes could have a material adverse effect on the Company's business, results of operations, financial condition and liquidity.

The Company remains committed to further reductions in SO<sub>2</sub> and other emissions on a cost-effective basis and will continue to evaluate and pursue the development of technologies to meet these challenges, taking into account cost-benefit considerations. While the Company is not able to determine the effect, if any, of significant future changes in regulatory emission limits beyond the February 2002 Control Order and other environmental laws and regulations that may be enacted in the future on its results of operations or financial condition due to the uncertainty surrounding the timing and ultimate form that such changes may take, any such changes could have a material adverse effect on the Company's business, results of operations, financial condition and liquidity.

During 2002, the Company began a \$90 million investment project covering fluid bed roaster (FBR) off-gas scrubbing technology intended to reduce SO<sub>2</sub> emissions to the new levels under the February 2002 Control Order to be effective by the end of 2006. This FBR project is also expected to have the added benefit of decreasing total metal emissions of nickel, copper, arsenic and lead by 80 to 100 tonnes per year. The FBR project involves the installation of water scrubbers that clean the SO<sub>2</sub> gases by removing, principally, particulate matter. The SO<sub>2</sub> gases are then directed to the acid plant to be converted into sulphuric acid. The FBR project will also provide the Company with the ability to treat the same types of gases coming from certain other smelting furnaces. As part of the February 2002 Control Order, the Company has agreed to continue its research into the technology and economics of further SO<sub>2</sub> and total metals reductions, and report to the MOE and the public on the progress of this research program. The February 2002 Control Order also calls for a final report by the Company on how further SO<sub>2</sub> and total metals reductions could be achieved to be submitted to the MOE by December 31, 2010. The February 2002 Control Order expires on December 31, 2012. In 2003, as part of the FBR project, Inco commenced construction of the weak acid treatment plant. This plant, which will be



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operational in 2004, will receive the scrubbed metals from the SO<sub>2</sub> gases and will fix the arsenic compound that can be placed into the tailings area. This will result in a 10 tonne per year reduction in arsenic emissions from the stack.

Canada signed and ratified the Kyoto Protocol to the United Nations Framework Convention on Climate Change (the Kyoto Protocol ) in December 2002. The Kyoto Protocol calls for significant reductions in emissions of greenhouse gases, such as carbon dioxide, and nationwide ceilings on such emissions. In November 2002, the Canadian federal government released an initiative, the Climate Change Plan for Canada , which includes specific requirements to also limit the discharge of carbon dioxide and other greenhouse gases. As of early March 2004, neither the Kyoto Protocol nor this initiative has established what the allocation of reductions among various sources of greenhouse gases would be. While the precise impact on the Company s Canadian operations and the operations of others who provide energy or other products or services to the Company is uncertain at this time, the Company anticipates that compliance with these initiatives could have a significant adverse effect on its business, results of operations and cash flows.

*Thompson*

The Company s Thompson, Manitoba smelter operated during 2003 under a regulation issued by the Manitoba government which limits emissions of SO<sub>2</sub> from the Company s Manitoba ores to 23,000 tonnes per month and 220,000 tonnes per calendar year. Inco met both of these limits during 2003, with the total of such emissions at 191,000 tonnes for the year. These emissions totalled 210,000 tonnes in 2002 and 217,000 tonnes in 2001.

*Port Colborne and Sudbury Soils*

The Company has been working with regulatory authorities and other interested parties to evaluate elevated levels of nickel and other metals in soils located in the vicinity of the Company s processing facilities in Sudbury and Port Colborne, Ontario that may have been affected by the historical emission of windblown metal-containing particulates. The Company believes that the Ontario government guidelines (the MOE Remediation Guidelines ) for the remediation of metals in soils which were issued by the MOE in 1996 do not satisfactorily account for the importance of metal speciation (the different chemical substances and forms in which metals occur), which controls the ability of metals in soils to cause potential toxic effects. In 1998, the Company submitted a generic risk assessment of nickel in surface soils to the MOE. This study, which was authored by recognized experts, concluded that potential toxicity of nickel in soils to certain sensitive plant species was the only health or ecological risk resulting from the range of nickel concentrations expected in generic soils, and that risks to other organisms, including wildlife, grazing animals and humans, were negligible. The study indicated that soil acidity, and the related nickel ion bioavailability, was the principal factor controlling toxicity. Research on sensitive plant species funded by the Company subsequent to this generic assessment confirmed that adjusting soil acidity was both a practical and an effective solution to removing the toxic effects of elevated nickel concentrations in the soil to sensitive plants.

*Port Colborne*

In 1998, the Company began discussions with the City of Port Colborne and the MOE concerning certain metals found in the surface soils downwind of the Company s Port Colborne refinery. MOE soil sampling results released in January 2000 indicated a wide area having surficial soils with levels of nickel, copper and cobalt above the generic levels established by the MOE for phytotoxicity. Based upon these results, the Company suggested that a community based risk assessment ( CBRA ) process, funded by the Company, would represent a more objective, fair and efficient way of assessing any risks from these levels than conducting numerous site-specific risk assessments. The CBRA process was accepted by the MOE and the City of Port Colborne and in April 2000 the Port Colborne city council appointed a seven-member Public Liaison Committee (the PLC ), consisting of local citizens, to interface and work with the Company and its consultants on the CBRA process. A stakeholder technical sub-committee was also formed consisting of representatives of the MOE, the Regional Public Health Department, the City of Port Colborne, Inco and consultants. In November 2000, the scope of work for the CBRA process was agreed upon and work commenced. The CBRA process has focussed on ecological

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and human health assessments involving all potential pathways for exposure to specified metals for all living species and all health endpoints.

In 2001, the CBRA evaluated soil analyses to determine if there existed any additional inorganic or organic chemicals of concern ( CoCs ) related to Inco s historical operations. The only additional CoC found beyond nickel, copper and cobalt and potentially linked to Inco s operations was arsenic, which was added to the three existing CoCs for all health and environmental assessments within the CBRA process. The testing carried out on soils in the vicinity of the refinery showed lead levels higher than generic levels established by the MOE, but completely within the range found in older communities throughout North America caused principally by societal use of lead-based paints and leaded gasoline until the mid-1970s and the improper disposal of lead-acid automobile batteries. Even though the Port Colborne refinery emitted some lead-containing particulates during its approximately 80 years of operation, an inventory of such emissions, together with air dispersion modeling, has shown that expected soil lead concentrations from such emissions are a tiny fraction of the lead observed in soil. A comprehensive report on lead as a CoC within the CBRA was written in 2003 and is currently being peer reviewed. This report confirms that the Company should not be held responsible for the lead found in soils in Port Colborne.

During preliminary discussions on the CBRA in 2000 with the MOE and the PLC, some residents expressed concerns about health risks to children attending schools and playing in school yards during dust-generating activities such as plowing and cultivation in agricultural fields adjacent to the schools. In response to these concerns, the Company retained consultants to conduct air sampling campaigns during periods when no field activities were being conducted and also during periods when tractor and plowing work was being conducted in preparation for the planting of crops. Results from these studies were released in late 2000, showing very low total nickel, copper, cobalt and arsenic levels in dusts collected at the schools. These levels were far below the Ontario ambient air standards for these elements.

The objective of the CBRA is to assess human and environmental health risks from multi-pathway exposures to CoCs in Port Colborne. If risks are found to exist at unacceptable levels, as defined by governmental authorities, then the CBRA will also recommend options for the remediation of soils to remove those risks. As a result of this effort, the CBRA will be able to derive Port Colborne-specific soil concentrations for each CoC that will not be a risk for environmental and human receptors in the community and all soil types and uses occurring in the community. Significant progress was made in 2003 with the completion of two draft reports, one on the natural environment and the second on commercial crops. Both of these reports have undergone extensive review by the consulting company hired to assist the PLC and by external independent peer reviewers. Revisions to these draft reports in response to the reviews are expected to be tabled in mid-2004. After appropriate public consultation, the final reports are expected to be sent to the MOE for its approval at the end of 2004. A third report concerning human health risks was drafted in 2003. It has not yet been peer reviewed, but submission of the report in final form is expected in 2004. While the results of the CBRA have not yet been finalized, based on the information available to date, it appears that a relatively small area of land in Port Colborne could require remediation. While it is not possible to predict the exact area of such land or the cost of any required remediation at this time, the Company believes that, to the extent that remediation is required, adding limestone to the soils to adjust soil acidity may represent a cost-effective solution.

In late March 2001, two developments occurred in connection with the historic operations of Inco s refinery in Port Colborne, Ontario: (i) the filing of a purported class action proceeding in an Ontario court and (ii) the release of a report by the MOE covering elevated levels of nickel and other metals found in the soils at depth (below five centimetres) on 16 out of nearly 180 properties sampled by the MOE in Port Colborne (the March 2001 MOE Report ) and the issuance of a draft remediation order by the MOE.

The purported class action proceeding originally filed against Inco and several other parties under Ontario class action proceedings legislation claimed Cdn.\$600 million in compensatory damages and Cdn.\$150 million in punitive damages covering certain residents who lived in the Port Colborne area since 1995 and allegedly suffered a decline in their property values as a result of, and health and other injuries from exposure to, metals and related emissions from the refinery. In June 2002, hearings were held in the Ontario Superior Court of Justice to consider whether this action, or any portion of it, should be certified to proceed as a class action. In July 2002 the court

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rejected certifying any part of the action as a class action. The plaintiff appealed this decision and the appeal, which revised the original pleadings and focused on the plaintiff's claim for damages for property value diminution only, resulting in a significant reduction in the number of citizens that the plaintiff is purporting to represent, was heard in June 2003. In early February 2004, the Ontario Divisional Court rejected the plaintiff's appeal. Soon after this decision was released, the plaintiff sought leave to appeal to the Ontario Court of Appeal. We expect to know whether or not the court will grant leave (that is, permission) to the plaintiff to appeal to the Court of Appeal by the end of May 2004.

With respect to the issue of the finding of nickel, in particular nickel oxide as the primary form, at various depths in the Port Colborne soils adjacent to the Port Colborne refinery, the March 2001 MOE Report established an intervention level of 10,000 ppm or more of nickel as a potential health risk and soil samples taken by the MOE reflected nickel concentrations above this level on 16 properties. While the Company did not accept the March 2001 MOE Report's findings and conclusions, in response to the report it proposed a voluntary remediation program for the 16 properties whereby the Company offered to remove and replace the soil on these properties to bring them below the 10,000 ppm level.

In April 2001, the Company submitted a detailed comment letter to the MOE on the March 2001 MOE Report. Based upon such key issues as what the exposure pathways would be and the level of exposure from nickel oxide and other forms of nickel found in the soils at depth, the Company did not believe that the levels of nickel found as reported in the March 2001 MOE Report represented a health hazard. In May 2001, the MOE indicated that, given the comments it had received on the March 2001 MOE Report from the Company and others, it would effectively be withdrawing the report and draft order and would be undertaking further studies and analyses. A revised draft report was issued for public comment by the MOE in late October 2001 together with a new draft order which would have required that 25 properties, based upon the soil sampling by the MOE reflected in the March 2001 MOE Report, be remediated given a slightly lower intervention level for nickel, 8,000 ppm, established by the MOE in its revised report. The Company submitted a new comment letter to the revised report and revised draft order in late November 2001. In March 2002, the MOE released its report and order in final form. It contained a somewhat different methodology for calculating health risks for certain pathways, but retained 8,000 ppm nickel in soils at depth as the intervention level, and the MOE issued a broad order to Inco to remediate properties having soil nickel levels above that level and undertake certain other activities (the March 2002 Order). Inco did not believe the intervention level of 8,000 ppm nickel in soils at depth was supported by the scientific information available and believed that the March 2002 Order imposed a number of other remediation and sampling obligations that were not supported by the findings in the March 2002 report.

The Company kept its voluntary remediation program open for the original 16 properties and extended its voluntary offer to the additional nine properties identified by the MOE as having in excess of 8,000 ppm nickel in soil (the 25 properties). Only five property owners have chosen to participate in the Company's voluntary remediation program to have the Company remove and replace the soil on their properties. We have been advised that the owners of the remaining 20 properties (except one property which the Company owns) are represented by the same counsel that represents the plaintiff in the class action proceeding referred to above.

In April 2002, Inco appealed the March 2002 Order. A group of citizens also appealed the March 2002 Order, asserting that the Order was too lenient. The appeals were heard by the Ontario environmental review tribunal (the Tribunal), starting with preliminary sessions in November 2002. On the first day of the preliminary hearing, motions were made by both appellants regarding the scope of the hearings. Inco moved that the appeal should deal only with human health risk associated with systemic nickel intake, which was the basis of the March 2002 Order. The citizens' group, on the other hand, indicated that the hearings should consider all environmental endpoints and also respiratory cancer. The review tribunal accepted the Company's motion to limit the scope of the appeal to issues arising from the March 2002 Order only. Counsel for the citizens' group appealed this decision by way of a judicial review, which was heard in March 2003. The judicial review concluded that the tribunal was correct to limit the scope of its hearings and the hearings resumed in September 2003. As a result of the Company receiving clarification from the MOE on the scope of its 2002 Order, and with the agreement of the citizens' group to withdraw its appeal, the Company withdrew its appeal and the Order was re-instated with an expiry of December 2004. In September 2003, representatives of the Company and the MOE

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visited all properties that had not been remediated under the Company's voluntary program to discuss the proposed remediation of each property. In October 2003, the Company submitted a remediation plan to the MOE and to all but one of the property owners. A remediation plan for the one remaining property is expected to be submitted to the MOE and to this property owner by the end of March 2004. Comments were received from the affected property owners and the Company responded by revising its remediation plan and filing it with the MOE in early December 2003. As of December 30, 2003 the Company was notified by the MOE that the revised plan was acceptable. Removal and replacement of soil on these properties is expected to occur when the ground becomes workable in the spring of 2004.

In late January 2004, we received notice that the affected residents were making an application for leave to appeal the MOE's acceptance of our revised remediation plan to the Tribunal. The Tribunal has asked the residents to provide submissions as to whether the Tribunal has jurisdiction to consider the application for leave to appeal before it will consider the leave application.

In April 2001, in response to the draft order accompanying the March 2001 MOE Report, the Company voluntarily undertook additional sampling in residential areas adjacent to the area where the 25 properties are located. Based upon this additional sampling by the Company, no additional properties were found to require remediation.

As part of the CBRA process, the Company agreed to carry out a special health survey of Port Colborne residents, to be conducted by a team of medical experts, to determine if adverse health effects linked to CoCs in the soils are currently being experienced by people in the community. The Company retained Ventana Clinical Research Corporation ( Ventana ) to conduct this work. During 2001, Ventana interviewed citizens in the community and medical professionals and presented a conceptual scope of work in October 2001. This scope of work was reviewed, revised and prioritized by the stakeholders during 2002. The scope of work contemplated the following four studies: (i) a population health survey to identify if there is a higher prevalence of any particular disease in residents of Port Colborne compared to residents of comparable communities ( Study A ), (ii) if determined necessary by the results of Study A, an epidemiological case control study on any diseases found in Study A to determine if the diseases are linked to exposure to CoCs ( Study B ), (iii) a study of the incidence of hospital admissions relative to a comparative community ( Study C ), and (iv) a study of the incidence of cancer rates using national and provincial databases ( Study D ). Work began on Study A in December 2002 and a draft report is expected by the spring of 2004. Study C, which compares the incidence of hospital admissions in Port Colborne with data from similar communities in Ontario, was completed in 2003. The draft report on the findings of Study C is currently undergoing Company and peer review. Study D remains in the planning stage. Once Study A and Study C have been completed, whether or not Study B is necessary will be reviewed. We cannot predict with any certainty whether Study B will be necessary. If it is undertaken, it is currently expected that it would start in 2005.

At the beginning of the CBRA process in 2000, the Company also agreed to undertake a study on the socio-economic impacts that the CoCs in soils may have or may be causing. Efforts to draft an appropriate scope for such a study have been unsuccessful and it is not known at the present time if such a study will ultimately be conducted by the Company.

Given the existence of various legal appeals and scientific and medical studies currently underway, it is impossible to predict the effect that these actions and studies could have on the Company's business, results of operations and financial condition.

*Sudbury*

In September 2001, the MOE released a report indicating that it had analyzed soil samples collected within the Sudbury area for various substances, including arsenic and certain other metals. This report stated that nickel, copper, cobalt and arsenic in some soil samples were in excess of the applicable MOE guidelines and that the elevated concentrations of these metals in the soils were attributable to the history of nickel-copper mining and smelting in the area by Inco and Falconbridge. The two companies agreed to jointly fund risk assessments for human and environmental health in the Sudbury region. They have also joined the MOE in extending soil sampling to areas that were undersampled.

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The Sudbury area soil data in the MOE's report showed nickel concentrations lower than those found in Port Colborne soils, but the potential area affected in Sudbury is larger than in Port Colborne. Some of the work being conducted at Port Colborne will be applicable to Sudbury, but the risk assessment for Sudbury must be based on the specific soil types located there. During 2001, the City of Greater Sudbury, the Regional Health Department, the MOE, Inco and Falconbridge formed a technical committee (the Sudbury Technical Committee), with Health Canada participating on behalf of First Nations communities, to guide the risk assessment work on nickel, copper, cobalt and arsenic in soils and other related environmental media. This was followed by the formation by the Sudbury Technical Committee of a public advisory committee consisting of ten citizens and the appointment of a process observer responsible for reviewing the timeliness, effectiveness and transparency of the risk assessment process.

In 2002, the Sudbury Technical Committee defined the scope of work for the human health and environmental health risk assessments, issued a comprehensive request for proposals to carry out the assessment, reviewed six proposals submitted and chose the winning bid based on technical, economic and public communication criteria. The risk assessments will be carried out by the Sudbury area risk assessment group (SARA), a consortium of firms having the collective experience necessary to conduct this multi-disciplinary project. The consortium includes a number of environmental management and analytical firms. Work was started under a preliminary contract in December 2002 and the final contract was signed by Inco and Falconbridge in 2003.

Extensive public consultation was carried out in 2003 and will continue throughout the risk assessment process. Analysis of several thousand new soil samples was completed by SARA and two additional elements, selenium and lead, were added to the list of CoCs for the community. The scope of work for the environmental risk assessment was tabled in September 2003 and is currently undergoing review by peers. The scope of work for the human health risk assessment is in preliminary draft form. Both of these scopes of work are expected to be completed in mid-2004. Ambient air monitoring was initiated in October 2003 and preliminary garden vegetable sampling was conducted in the summer of 2003. The risk assessments are scheduled to be completed by mid-2005. Inco's share of the cost of the work is about \$2 million. It is impossible to predict what remediation may be recommended from these assessments, but it is well known that the Sudbury area has undergone successful re-greening efforts over the last several decades and has experienced a significant ecological recovery.

*Decommissioning and Reclamation*

Inco is committed to decommissioning its facilities, at both existing and inactive mine sites, in an environmentally sound manner commonly referred to as progressive decommissioning. In Ontario, progressive decommissioning is ongoing at the Copper Cliff tailings area where exposed tailings are being covered. In 2003, the Company continued to maintain more than 1,500 hectares of vegetated cover on inactive tailings for stabilization purposes. In 2003, the Company continued its decommissioning and reclamation projects at both operating and non-operating properties in Ontario including demolition and closure work at Shebandowan, Crean Hill and Froid-Stobie mines and the Port Colborne Refinery, recontouring at Whistle Mine, tree planting and groundwater assessment. In Manitoba, the Company submitted reclamation plans for the Thompson mine and processing facilities to the Manitoba government. Reference is also made to Future Removal and Site Restoration; Closure and Post-Closure Plans below.

*Revegetation Programs*

A significant part of the Company's environmental programs in both Canada and Indonesia involves the revegetation of mined-out lands and areas affected by mining and processing activities to return them to a natural state.

In 2003, Inco continued to produce seedlings at its underground nursery in Creighton Mine. The nursery is located at a depth of more than one kilometre, where temperature and humidity are constant. Automated watering and lighting systems optimize the growth of seedlings year-round. Approximately 200,000 seedlings were grown, of which 142,000 were planted in the Sudbury region, in 2003. The remainder of the seedlings were donated to the City of Sudbury and various community groups.

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At PT Inco in Indonesia, reclamation efforts continue to focus on returning to mined out areas the waste rock and soil that was removed to access the ore and planting trees in these areas. The objective of this program is to maintain the size of the mine footprint to a maximum of 650 hectares and restore mined out areas to their natural state.

*PT Inco*

PT Inco's operations are subject to environmental regulations and permits issued by the Government of Indonesia. PT Inco is in compliance with these permits except for the release of soluble nickel, manganese and occasionally chromium in its liquid effluent discharges into a small stream adjacent to its operations and the levels of emissions of particulates from its facilities. In recent years, PT Inco has implemented a number of projects which have reduced the levels of nickel, manganese and chromium in its effluent discharges and is continuing its efforts to bring these levels within the regulated limits. By dredging, PT Inco has been able to increase the retention capacity of its sediment ponds and nickel concentrations in effluent were in compliance for 2003. Since 2000, PT Inco has also had a program in place with the government for investigating the most effective way to further reduce its particulate emissions. This program includes an action plan and periodic reporting to the government. PT Inco also initiated a dust handling program in 1999 to address issues associated with various dust handling processes at PT Inco. This program includes the installation of equipment, in particular additional electrostatic precipitators ( ESPs ), and other solutions to reduce dust emissions. The principal sources of dust emissions and other particulate emissions from PT Inco's facilities are PT Inco's dryers, reduction kilns, converters and electric furnaces. A new ESP was constructed and commissioned on one of PT Inco's three dryers in 2001 and operated in 2002, so that all of PT Inco's dryers had installed ESPs. This investment has resulted in a substantial decrease in dust from this source and PT Inco is now in compliance with permitted dust emissions levels from its dryers. Modifications to the ducting to one of PT Inco's five kilns has resulted in decreased dust emissions and this effort will be extended to the other two similar kilns. Two newer kilns are equipped with ESPs and operate at low dust emissions, below permitted levels. By the third quarter of 2003, all five kilns at PT Inco were approaching compliance with permitted dust emission levels. PT Inco has also installed an automated pneumatic dust handling system which collects and transports dusts for reprocessing and standby blowpot systems have been installed on four of PT Inco's kilns to allow maintenance to be performed without interrupting the control and collection of dust. The fifth kiln was constructed with standby blowpot capacity, so all five kilns now have this standby capacity. An audit of the blowpot systems is being prepared and it is expected that the audit will recommend further improvements to enhance their performance and reduce fugitive emissions. PT Inco's three converters are in compliance with permitted dust emission levels. The principal remaining sources of dust emissions are PT Inco's four furnaces and PT Inco and an independent engineering firm are continuing to study options for cleaning the furnace off-gases with a pilot test program scheduled for late 2004 or early 2005. Workplace dust issues are also being addressed to improve workplace quality. During 2003, a number of significant improvements were realized as part of PT Inco's overall dust handling program, including a modification of the dust collection system of the kilns to allow for increased dust capture. While PT Inco (i) has kept the relevant governmental authorities apprised of those situations where it has not been in compliance with certain emission limits as noted above, (ii) has been working with these governmental authorities in respect of such regulatory issues and (iii) has not received any indication from such governmental authorities that it would be subject to any penalties or sanctions for such exceedences, PT Inco may still be subject to regulatory actions by such governmental authorities for non-compliance with certain emission limits.

*Future Removal and Site Restoration; Closure and Post-Closure Plans*

The following includes information that appears in *Management's Discussion and Analysis of Financial Condition and Results of Operations* under Item 7 of this Report and in Notes 1 and 13 to the financial statements under Item 8 of this Report.

The operations of the Company have been, and may in the future be, affected from time to time in varying degrees by changes in environmental laws and regulations, including those for future removal and site restoration costs. Both the likelihood of future regulations and their overall effect upon the Company vary greatly from

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country to country and are not predictable. The Company's policy is to meet or, if possible, surpass environmental standards set by relevant legislation, by the application of technically proven and economically feasible measures. Environmental expenditures that relate to ongoing environmental and reclamation programs are charged to earnings as incurred or capitalized and depreciated depending on their future economic benefits. Estimated future removal and site restoration costs are charged to earnings on a straight-line basis over the estimated remaining life of the related business operation. Actual removal and site restoration expenditures are charged to the related liability.

The estimation of future removal and site restoration costs depends on the development of environmentally acceptable closure and post-closure plans, which, in some cases, may require significant research and development to identify preferred methods which are economically sound and which, in many cases, may not be implemented for several decades. The Company has continued to utilize appropriate technical resources, including outside consultants, to develop specific site closure and post-closure plans in accordance with the requirements of the various jurisdictions within which it operates. Typical closure and progressive rehabilitation activities include, where applicable, demolition of buildings, removal of underground equipment, sealing of mine openings, treatment to reduce or prevent acid generation from stockpiled waste materials such as tailings, general clean-up activities aimed at returning the area to an environmentally acceptable condition, and post-closure care and maintenance.

In accordance with environmental regulations adopted by the Province of Ontario in 1991, the Company developed rehabilitation and site restoration plans associated with the eventual closure of its operations in that province. The Company filed three closure plans by the end of 1997, having previously received approval from the Province of Ontario for the consolidation of its operating mines and properties in that province into 15 sites for purposes of closure plans, and the remaining 12 closure plans were filed by the end of 1998. As a result of provincial regulatory changes which became effective in 2000, the plans were refiled to meet these changes in 2001. The Company believes that cost-effective tailings disposal alternatives exist within the ongoing operating activities of its Ontario operations which would limit site restoration at closure to a care and maintenance activity, thus significantly reducing the costs of such site restoration. Under such environmental regulations, Inco is required to provide, and has provided, letters of credit for three closed properties in Ontario (Whistle mine, Shebandowan mine and Crean Hill mine) in the amount of \$21 million as at December 31, 2003.

In accordance with environmental regulations adopted by the Province of Manitoba in 1999, the Company has submitted reclamation and closure plans for all its facilities in the province. The Company submitted two reclamation plans for its mines and processing facilities in Manitoba in 2000, two plans in 2001 and the remaining two plans were submitted in 2003. These reclamation and closure plans have been accepted by the Government of Manitoba.

Closure plans for the proposed mine and mill facilities were prepared and submitted to the environmental assessment panel in 1998 in connection with the environmental review process of the Company's Voisey's Bay project in the Province of Newfoundland and Labrador. A draft closure plan was submitted to the provincial authorities in September 2002 and was reviewed and accepted as part of the application for a mining lease for this project. Closure plans for the Goro mining area were prepared and submitted in January 2002 to the Government of the South Province of New Caledonia in connection with the operating permits application (*installation classée* application).

The Company follows a policy of progressive rehabilitation at its Indonesian operations whereby land disturbed by mining activities is revegetated on an ongoing basis. In 2003, a closure plan was developed for PT Inco's operations which will be finalized in 2004.

Inco developed a draft closure plan for its Exmibal facility in Guatemala during 2003. This plan is expected to be completed by mid-2004.

In the United Kingdom, the Company's operations at Clydach and Acton have each submitted closure plans to the relevant governmental authorities as a part of the resubmission of their operating authorizations and as required under new legislation arising from the EU Integrated Pollution Prevention and Control directive.

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In the United States, a closure plan has been prepared for Inmetco and site characterization studies for closure plans are in the process of being prepared for Novamet.

Substantial removal and site restoration costs are incurred on an ongoing basis with the objective of significantly reducing future removal and site restoration costs that may otherwise be incurred following the closure of any sites. This progressive rehabilitation includes tailings management, land reclamation and revegetation programs, decommissioning and demolition of plants and buildings, and waste management activities. Operating costs associated with ongoing environmental and reclamation programs, including progressive rehabilitation, totalled \$39 million in 2003, \$13 million in 2002 and \$12 million in 2001 and are included in cost of sales and operating expenses. Capital expenditures on environmental projects totalled \$28 million in 2003, \$9 million in 2002 and \$17 million in 2001. The Company currently anticipates that capital expenditures on environmental control and related projects in 2004 will be approximately \$60 million.

Although the ultimate amount to be incurred is uncertain, the total liability for future removal and site restoration costs in respect of the Company's worldwide operations, to be incurred primarily after cessation of operations, is estimated to be approximately \$141 million at December 31, 2003, based upon certain discount rates and timing with respect to when these costs would be expected to be incurred applied in accordance with the new accounting standard that the Company has adopted, compared with \$119 million at December 31, 2002 and \$121 million at December 31, 2001. Effective January 1, 2003, we adopted a new accounting standard of the Canadian Institute of Chartered Accountants relating to asset retirement obligations. This standard significantly changed the method of accounting for future removal and site restoration costs and prior period consolidated financial statements have been restated to reflect this change. The comparative figures for 2002 and 2001 are significantly below previously reported figures due to this change in accounting method which has been applied retroactively. Under this new standard, the liability is accreted over time through periodic charges to earnings. The charge for 2003 was \$9 million. In addition, the asset retirement cost is capitalized as part of the asset carrying value and depreciated over the asset's useful life. The estimate of the total liability for future removal and site restoration costs has been developed from independent environmental studies, which include an evaluation of, among other factors, currently available information with respect to closure plans and closure alternatives, the anticipated method and extent of site restoration using current costs and existing technology, and compliance required by presently enacted laws, regulations and existing industry standards. The total liability for future removal and site restoration costs represents estimated expenditures associated with closure, progressive rehabilitation and post-closure care and maintenance. Potential recoveries of funds from the future sale of assets upon the ultimate closure of operations have not been reflected in the estimate of the total liability or related annual provision. Future changes, if any, to the estimated total liability, as a result of amended requirements, laws, regulations and operating assumptions may be significant and would be recognized prospectively as a change in accounting estimate, when applicable. Environmental laws and regulations are continually evolving in all areas in which we operate.

Changes made in 2000 to mining regulations in the Province of Ontario require the Company to provide letters of credit or other forms of financial security to fund the Company's future reclamation and restoration costs, which are not expected to be incurred for many years, in certain circumstances such as if the Company were to no longer meet certain minimum investment-grade credit ratings for its outstanding publicly traded debt securities and based upon applicable mine life requirements. Although the Company's debt securities are currently rated investment grade, they were rated below investment grade in recent times and there can be no assurance that this situation will not reoccur. If the Company were not able to maintain the minimum investment-grade credit ratings, it is currently estimated that letters of credit or other forms of financial security associated with the currently estimated costs of the eventual future closure of our mines and other facilities in Ontario would have to cover a significant portion of such closure costs. Due to the closure of three mines in Ontario, in 2002 we were required under such mining regulations to provide letters of credit in the amount of \$21 million to secure these near-term closure costs as discussed above. In addition, PT Inco is subject to certain Indonesian regulations which require it to provide security for the reclamation of land areas that have been mined. In the case of the Company's Manitoba operations, in 2003 we submitted closure and reclamation plans for all our operations in that province. We expect that, based upon regulations in the Province of Manitoba, we will be required to provide some form of financial security for our future reclamation and restoration costs in that province. However, it is



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not currently expected that these costs and related security with respect to the Company's Manitoba operations, beyond what has been included in the \$141 million estimated total liability as at December 31, 2003 referred to above, and for PT Inco's operations and/or such financial security to be provided for our Manitoba operations will be of a material amount. These potential costs might not be incurred until many years in the future. If these requirements for letters of credit or other forms of financial security had to be satisfied, they could have an adverse effect on the amounts available for borrowing under the Company's credit facilities.

In view of the uncertainties concerning environmental remediation, the ultimate cost of future removal and site restoration to the Company could differ from the estimated amounts provided. The estimate of the total liability for future removal and site restoration costs is subject to change based on amendments to laws and regulations and as new information concerning the Company's operations becomes available. Future changes, if any, to the estimated total liability, as a result of amended requirements, laws, regulations and operating assumptions may be significant and would be recognized prospectively as a change in accounting estimate, when applicable. Environmental laws and regulations are continually evolving in all areas in which the Company operates. The Company is not able to determine the impact, if any, of environmental laws and regulations that may be enacted in the future on its financial position due to the uncertainty surrounding the ultimate form that such future laws and regulations may take.

*Health and Safety*

The health and safety of the Company's employees are of the highest priority. The prevention of workplace accidents and illnesses is a major goal of the Company. Safety training and educational programs for workers have continued to be enhanced at all of the Company's operations and, through international workshops, sponsored university research and other activities, the Company is a leader in efforts to determine how to better test and assess the impact of metal compounds on humans and ecosystems.

*MITE Research Network*

The Company is one of the major contributors to the Metals in the Environment ( MITE ) research network initiative in Canada sponsored, in part, by the Mining Association of Canada. This five-year program, which will conclude in 2004, includes studies on (i) the relative importance between natural and human sources of metals placed in the environment, (ii) the processes that control the ultimate disposition of metals from whatever source, and (iii) the effects, both beneficial and harmful, that metals and metal compounds have on aquatic and terrestrial organisms. The results from this program are already affecting the course of regulatory activity relating to metals throughout the world. Data generated will assist in carrying out necessary risk assessments and in determining risk management strategies for the continued safe use of the Company's processes and products.

The MITE program has succeeded in bringing together research scientists and government policy makers to cooperatively decide where science is needed in policy development in Canada and to review how the current results from the MITE initiative can be applied. For example, research symposia to discuss the results of the program were held in Ottawa in February 2002 and February 2003. The MITE network has placed two post-doctoral associates, one at Environment Canada and the other at EVS Environmental Consultants Ltd. of Vancouver, to assist in bringing the program's research results into practice in risk assessments and, where applicable, into governmental programs, policies, guidelines and regulations. A major workshop involving government, industry and academia was held in May 2003 to review the current status of research worldwide and to identify remaining knowledge gaps. This workshop resulted in a proposal being put forth for the establishment of a new network of Canadian researchers with a major focus on risk assessment of metals as they pertain to health. Application for principal funding for this proposed new network is being made through the Canadian Natural Sciences and Engineering Research Council.

*Diesel Particulate Matter*

In 1995, the American Conference of Governmental Industrial Hygienists ( ACGIH ) announced its intention to establish for the first time a Threshold Limit Value ( TLV ) for diesel particulate matter ( DPM ) of 0.15 mg/m<sup>3</sup>. This proposed TLV, based primarily on rat and mice studies, constituted nearly a seven-fold

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reduction from the current Canadian target level of 1.0 mg/m<sup>3</sup> DPM. If adopted by regulatory authorities in Canada, this would require substantial changes in the Company's use of diesel equipment in its underground operations since this equipment emits DPM. The Company responded to the proposed TLV by making written and oral presentations to the ACGIH in 1996, noting that toxicological and epidemiological studies on health effects of DPM have given inconsistent and unreliable results and that it would, accordingly, be impossible to set scientifically sound occupational exposure limits for DPM. For a discussion of TLVs, see Regulation of Nickel and Other Nonferrous Metals Occupational Exposure Limits (OELs) in Canada below.

The ACGIH did not take any action to adopt the TLV in 1997 or 1998. However, in 1999 the ACGIH announced that it intended to further reduce the proposed TLV to 0.05 mg/m<sup>3</sup> for DPM of less than one micrometre in diameter. In 2001, it lowered this proposed TLV even further, to 0.02 mg/m<sup>3</sup>, analyzed as elemental carbon. In 2003, however, the ACGIH removed the proposed TLV for DPM from its Notice of Intended Change list and placed it on the list of Chemical Substances and Other Issues Under Study, where it remains for the year 2004. It is not known whether the TLV as proposed in 2001 (or some modification thereof) will be placed on the Notice of Intended Change list again in the future.

The U.S. Mine Safety and Health Administration (the MSHA) initiated a rulemaking activity in 1998 to establish a regulatory exposure limit for DPM in underground mines in the United States. Action of this kind by MSHA is usually considered significant as Canadian provincial governments often consider taking similar action. After a period of extensive public comment, the MSHA adopted its new exposure limit in late 2000 of 0.4 mg/m<sup>3</sup> DPM, determined using the total carbon technique. The new MSHA rule provided an 18-month phase-in period for companies to achieve compliance, at which point the new limit would apply for a period of five years, after which it would be reduced to 0.16 mg/m<sup>3</sup>. It is not known whether, when or how Canadian provincial governments will respond with similar limits, but an ad hoc group of governmental and mining industry personnel (including personnel from the Company) was formed in late 2000 to discuss this subject.

Recognizing the importance of regulatory Occupational Exposure Limits (OELs) for DPM on the Company's operations in Ontario and Manitoba, as discussed under Regulation of Nickel and Other Nonferrous Metals Occupational Exposure Limits (OELs) in Canada below, the Company helped form in 1997 an industry-labour-government research consortium, the Diesel Emissions Evaluation Program (DEEP), to determine sampling and analytical techniques capable of measuring low levels of DPM and to evaluate techniques capable of controlling DPM emissions in workplace air. DEEP has investigated a number of research areas, in particular biodiesel, fuels, maintenance improvements, and the effect of light duty vehicles on DPM in underground mines. In 2000, DEEP extended its original three-year term to allow completion of field tests on particulate filters, which potentially hold the most promise for cost-effective control of DPM. Several of these underground tests began at Inco's Stobie mine in 2001 and continued throughout 2002 and 2003 as long periods of testing are required to determine the expected lifetime of the filters under real operating conditions. These tests indicate that certain filters provide exceptional service, while others fail in some diesel applications. The ultimate choice of which filter will work on which engine is a matter of closely matching the engine's operating parameters with those of the filters. Developing this algorithm for filter selection is the main focus of DEEP as it aims to conclude its work in 2004. Adoption by the Company of ultimate DPM control strategies developed by DEEP, and the cost of such adoption, will depend on a number of factors, including the types of engines used and their duty cycles as well as the final regulatory limit the Company will be required to meet.

*WSIB Occupational Disease Policies*

The Company is subject to workers' compensation laws in various jurisdictions pursuant to which occupational injuries to, and diseases of, individual workers making claims are examined and payments are awarded by a governmental board or agency. The expense of such awards is generally funded by the employer, typically as a percentage of payroll costs within the jurisdiction of the relevant board or agency, and is adjusted according to the experience with such claims either with respect to employees of the particular employer alone or on the basis of all claims in respect of employees in the same industry within the relevant jurisdiction.

In 1994, the Occupational Disease Panel (the ODP) of the Ontario Ministry of Labour (the MOL) concluded that there was a probable connection between miners' lung cancer and all hardrock mining. In 1996,

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the ODP asserted that a 1996 cancer morbidity study conducted by researchers at McMaster University, using a large group of Ontario male nickel production workers from Inco and Falconbridge, confirmed such a connection for nickel miners. Consequently, the ODP recommended that primary lung cancer and the occupation of hardrock mining be categorized under a particular schedule of the Ontario *Workers Compensation Act* which would create a presumption in favour of a causal relationship for lung cancer claims unless the contrary could be proven. In 1997, the ODP issued another report dealing specifically with laryngeal cancer and workers in nickel production. This report relied heavily on the 1996 McMaster University study referred to above. The ODP recommended that laryngeal cancer and certain nickel producing occupations be treated in the same manner as lung cancer and hardrock mining. The Company retained independent medical and epidemiological specialists to analyze these assertions and, as a result, made several submissions to the Workplace Safety and Insurance Board (the WSIB), the regulatory body of the MOL responsible for evaluating and adjudicating workplace injuries and diseases, taking exception to the ODP recommendations, primarily on the basis that tobacco smoking is likely a confounding factor, and to the validity of the findings of both the original hardrock mining report and the McMaster University study. These submissions explained why the Company believed that the ODP report was flawed and suggested that no policies on this matter be established until more methodologically sound studies were conducted. Similar submissions have been made by Falconbridge and by the Ontario Mining Association. Because of these submissions, the WSIB has not taken any action on any of the ODP reports.

In late 1994 the WSIB also revised and extended its policy with respect to lung cancer compensation claims by nickel smelter and refinery workers. Inco objected to the process that was used in considering the revised policy, which, in the Company's opinion, failed to take into account applicable scientific data, and also objected to flaws in the policy itself. As a result of submissions to, and discussions with, WSIB staff, in early 1998 the WSIB proposed a revision to the 1994 policy. However, this revision failed to address the Company's central concerns with the policy and the Company made additional written submissions to the WSIB suggesting further significant revisions. The Company has continued its efforts to have the WSIB change this policy, but no changes have been forthcoming. In mid-2001, the Company was invited to join a special stakeholder panel being formed by the WSIB. This panel, called the Occupational Disease Advisory Panel (the ODAP), consisted of industry and labour representatives from a broad range of industrial sectors. The ODAP's mandate was to advise the WSIB of criteria that should be applied in developing policies, to review contentious policies that currently exist, and to recommend how the WSIB should deal with controversial studies previously conducted by the ODP. During 2003, it became apparent that the ODAP could not reach consensus on a number of important issues and that a report from the ODAP was not possible. Instead, the ODAP Chair, who had been selected and assigned this position by the WSIB, drafted a report which attempted to relate areas of agreement and disagreement of the ODAP's members. The draft was provided to ODAP members for comment in December 2003. It is expected that the Chair's report will be delivered to the WSIB in 2004, but the Company cannot predict what actions WSIB will take as a result of this work.

*Worker Safety*

The table below shows the disabling injury frequency ( DIF ) for the Company in 2003, 2002 and 2001:

	<u>2003</u>	<u>2002</u>	<u>2001</u>
DIF	1.7	1.8	1.8

The DIF is calculated by the Company by multiplying the total number of disabling injuries in a year that employees incurred as a result of work-related injuries by 200,000 hours (which is a constant used by the Mine and Aggregates Safety and Health Association (Ontario) and other similar organizations) and then dividing that product by the total number of hours worked by employees during that year. The DIF disclosed above for 2002 is different from the previously disclosed DIF for 2002 because the DIF for 2002 has been recalculated to reflect information that the Company received subsequent to the previous disclosed DIF for 2002.

In 2001, the Company developed a safety management framework which outlines measures to be taken by all employees to ensure that every employee works as safely as possible. Since that time, each of the Company's operations and subsidiaries has developed and implemented, or is currently developing, a facility-specific plan to implement the safety management framework.

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In 2003, Stobie mine at the Company's Ontario operations was awarded the Ryan Award for Safety for its performance during the previous year. This award is presented to the mine in Ontario with the lowest lost-time injury frequency and no fatalities which has operated for at least 500,000 hours.

*Regulation of Nickel and Other Nonferrous Metals*

Regulatory and non-governmental agencies in the United States, Canada and Europe have proposed and, in certain instances, adopted regulations and other standards relating to environmental releases of nickel, exposure to nickel in various forms, and management of nickel-containing wastes, as summarized below.

*Occupational Exposure Limits (OELs) in Canada*

The ACGIH evaluates toxicological data and establishes a chemical's TLV, an airborne concentration to which nearly all workers can be exposed for eight hours per day for five days per week for their entire working life without suffering adverse health effects. Although the ACGIH has no regulatory power, TLVs are commonly used as starting points for setting mandatory standards for exposure to certain materials by regulatory authorities throughout the world. In November 1997, the ACGIH Board of Directors approved new TLVs and carcinogen classifications for nickel and its compounds. These classifications were published as adopted values in 1998. The new TLVs, which are to be measured as nickel in inhalable particulate, were as follows: 1.5 mg/m<sup>3</sup> for elemental/ metallic nickel; 0.2 mg/m<sup>3</sup> for insoluble nickel compounds; and 0.1 mg/m<sup>3</sup> for soluble nickel compounds and nickel subsulphide (which forms during the metallurgical processing of the Company's nickel ores). The TLV for nickel carbonyl was unchanged at 0.05 ppm. Since 1998, insoluble nickel compounds and nickel subsulphide have been classified by ACGIH as Confirmed Human Carcinogens; soluble nickel compounds have been designated Not Classifiable as a Human Carcinogen; and elemental nickel has been classified as Not Suspected as a Human Carcinogen. Nickel carbonyl was not classified for carcinogenicity at all.

The Province of Manitoba automatically adopts the ACGIH's TLVs as mandatory OELs and it adopted the TLVs for nickel as OELs in 1998. Between 1998 and 2002, the Company's Manitoba operations continued to use established sampling technology because routine samplers for inhalable particulate were not available. However, all samples collected during this period were converted to an inhalable basis using relevant research results. Also during this period, an analytical protocol developed by Inco for determining soluble nickel, oxidic nickel, sulfidic nickel and elemental nickel contents was used to determine the concentrations of nickel in samples for the four types of nickel substances specified in the OEL. In 2002, sampling for types of nickel in the workplace was completed using an inhalable IOM 7-hole sampling system and analyzed for nickel species using the Inco-developed analytical protocol. As the analytical protocol cannot uniquely distinguish nickel subsulfide from other nickel sulfide, additional assumptions about the presence of various sulfides must be made using knowledge about the processes being used from which dust arises. As predicted, few groups of workers were found to exceed the OELs. Action plans were implemented to mitigate such exposures in the surface processing plants. The success of these action plans was evident by a significantly reduced number of individuals having exposures exceeding the OELs in 2003.

The Province of Ontario does not automatically adopt the ACGIH's TLVs and the MOL normally consults stakeholders prior to setting OELs. In the case of nickel, these discussions started in 1999. By mid-2000 the MOL had stated that it intended to adopt OELs for only two of the four ACGIH nickel TLVs, nickel subsulfide and insoluble nickel. The proposed OELs were numerically equivalent to the TLVs, but were based on a so-called total dust sampler, currently used extensively in Ontario, instead of an inhalable dust sampler. However, when the final regulation was published in September 2000, the MOL chose to adopt all four of the ACGIH nickel TLVs as new inhalable OELs. While the Company's Ontario operations would have had relatively minor compliance problems under total dust sampling, significant problems existed for inhalable sampling and inhalable OELs, principally in the smelter, matte crushing and matte separation plants.

In March 2001, a tripartite committee focusing on the review of inhalable levels of nickel, made up of representatives of the MOL, the Company and several locals of the union that represents the Company's workers, was formed by the MOL to cooperatively review and consult on several new commercial products for inhalable

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sampling which became available in 2001. A viable commercial sampler was found to be workable in the Company's workplace environments in May 2001. In October 2002, the tripartite committee concluded its work with an agreement that the analytical technique that Inco adopted for speciation, in conjunction with other analytical techniques necessary to identify the species, all of which would be subject to the professional judgment of an expert in the field prior to acceptance, was a reasonable approach for characterizing OELs for metallic nickel, insoluble nickel, soluble nickel and nickel sub-sulfide in Inco workplaces. To meet these OELs, a four-year workplace environment improvement plan has been developed by the Company and reviewed with the MOL. Approximately \$5 million was committed in 2002 for ventilation improvements to be made over the next few years. In 2003, approximately \$1.6 million was spent on ventilation improvements which resulted in decreases in airborne exposures. For example, in 2003 the matte processing area of the Copper Cliff Smelter, total nickel levels decreased by 25 per cent to 88 per cent. It is not possible to state at this time the full extent of the ventilation improvement program or the total capital expenditures that will be necessary to comply with these OELs at the Company's Ontario operations. The Company and the MOL have agreed in principle to a long-term cooperative approach of engineering control upgrades that will take place in a number of workplaces over several years to meet these OELs.

In 2001, the MOL released a discussion paper concerning a proposed permanent process for up-dating OELs for all workplace substances. Four options for this process were proposed by the MOL, which invited comments on these options from stakeholders. The Company joined other members of the Ontario Mining Association in forming a task force aimed at considering the best process for maintaining OELs that are protective of workers, supported by sound science, and economically practical. The task force released its comments in February 2002. In the opinion of the task force, none of the options suggested by the MOL was acceptable and it suggested a fifth option in which an independent expert advisory group would review each candidate OEL for its scientific, as well as practical, basis. There was no response from the MOL on this proposed option in 2003. The Company cannot predict the effect that further reductions in OELs for workplace substances could have on its operations or financial condition.

*Occupational Exposure Limits (OELs) in the U.S. and the U.K.*

The Company is generally in compliance with the permissible exposure limits for all forms of nickel that are currently applied by the U.S. and U.K. governments.

*U.S. Environmental Regulatory Actions*

In 1990, the United States Congress amended the U.S. Clean Air Act to require, among other things, that 189 chemicals or chemical groups (including nickel compounds) be regulated as hazardous air pollutants (HAPs). Pursuant to this legislation, the EPA has been promulgating stringent technology-based standards for controlling emissions of HAPs from designated source categories. This process will continue in the future and ultimately may include the promulgation of additional risk-based standards. Some of these standards may limit emissions of nickel and its compounds, most likely through limits on overall emissions of particulate matter. The Company is unable to determine what nickel-emitting sources may ultimately be covered by such standards or to predict what capital expenditures or operating cost increases the Company or its customers may incur as a result of the promulgation of such hazardous air pollutant standards.

In July 1999, the EPA issued its final Integrated Urban Air Toxics Strategy under which 33 HAPs judged to pose the greatest threat to public health in urban areas are to be targeted for future regulation. Nickel compounds were among the 33 HAPs listed under this strategy. As a result, nickel compounds will be included by the EPA in periodic National Air Toxics Assessments (NATAs) designed to estimate and track trends in emissions, ambient air concentrations, population exposures, and associated characterizations of risk. In June 2002, the EPA released the Final National-Scale Air Toxics Assessment for 1996 (NATA-1996), which estimates emissions, ambient air concentrations, and population exposures for the 33 HAPs referred to above based on a 1996 emissions inventory, and characterizes the resulting population risks on a national and regional basis. This assessment reflected much lower total national emissions of nickel compounds than an earlier estimate that was based on information for 1990. NATA-1996 found that concentrations of nickel compounds in the ambient air were not of concern with respect to non-cancer health effects. However, nickel compounds were characterized as

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being a more significant contributor to potential cancer risks. That finding was based on what the Company and other nickel producers believe to be a flawed methodology for estimating potential cancer risk. The nickel industry has made a submission to the EPA, asking that the methodology be corrected, so that a more appropriate risk characterization can be made in the next release of NATA information, which is scheduled at three-year intervals. In addition to issuing NATAs, the EPA's Urban Air Toxics Strategy will target various sources of hazardous air pollutants for further emissions reductions. In the case of nickel compounds, some of these sources are likely to be fossil fuel combustion units, while others may involve nickel-using industries such as stainless steel manufacturing and metal plating. The Company is unable to predict what impact, if any, the inclusion of nickel compounds on the EPA's Urban Air Toxics and related assessments might have on nickel users and, indirectly, on the Company's operations or financial condition.

In December 2002, the National Toxicology Program ( NTP ) within the U.S. Department of Health and Human Services released its Tenth Report on Carcinogens ( ROC ). In these bi-annual reports, NTP lists various substances that it concludes are either known to be human carcinogens or reasonably anticipated to be human carcinogens. Previous versions of the ROC listed metallic nickel and certain nickel compounds as reasonably anticipated to be human carcinogens. Metallic nickel remained in that category in the Tenth ROC. However, nickel compounds as a class (with no differentiation) were listed as known to be human carcinogens. That broad listing runs counter to arguments that Inco and other nickel producers had made to NTP over the years, and the Company continues to believe it is not scientifically justified for various types of nickel compounds. Since nickel compounds already had been characterized as carcinogenic to humans by the International Agency for Research on Cancer, it is not clear what additional impact, if any, NTP's listing of nickel compounds as known to be human carcinogens in the Tenth ROC will have on businesses that produce, use, handle, or otherwise manage nickel compounds and wastes in which they are contained. Similarly, since metallic nickel has been listed as reasonably anticipated to be a human carcinogen by the NTP for many years, it is not clear what effect, if any, the reaffirmation of that listing in the Tenth ROC will have. Nickel alloys, stainless steels and other alloys that contain nickel, also were evaluated for possible listing in the Tenth ROC, but after all the evidence was considered, they were not included as either reasonably anticipated or known to be human carcinogens. Following publication of the Tenth ROC, the Company in conjunction with nickel producer associations, formally requested that NTP correct certain information in the Tenth ROC regarding nickel metal and nickel compounds. That request was rejected late in 2003. An appeal of that rejection is pending.

In December 2002, the EPA adopted sweeping amendments to its Inventory Update Rule ( IUR Amendments ) implementing provisions of the U.S. *Toxic Substances Control Act*. The IUR program requires manufacturers and importers of covered chemical substances to submit quadrennial reports of specified information if they produce or import more than a designated amount of a covered chemical at any one site. Prior to the adoption of the IUR Amendments, inorganic chemical substances (like nickel and its compounds) had been exempt from IUR reporting. The IUR Amendments removed that exemption so that inorganic chemicals will be subject to the IUR program in the next reporting cycle, covering calendar year 2005. While the basic reporting threshold has been increased from 10,000 pounds per site to 25,000 pounds per site, the information required to be reported has been dramatically expanded, particularly for sites that produce or import more than 300,000 pounds of a covered chemical during the reporting year. The new processing and use information required in those cases will be burdensome to collect and report; however, this expanded requirement to report processing and use information will not apply to inorganic chemicals like nickel until the 2010 reporting year. While the new IUR reporting requirements will impose additional costs and burdens on the Company and various of its U.S. customers, they are not expected to have a material adverse effect on the Company's operations or financial condition.

*Canadian Environmental Protection Act*

In 1994, under the *Canadian Environmental Protection Act* ( CEPA ), two federal government departments, Environment Canada and Health Canada, published toxicity assessments of 17 substances, including nickel and its compounds. The assessment concluded that metallic nickel was not considered toxic under CEPA. However, oxidic, sulphidic and soluble compounds of nickel were considered toxic, according to statutory definitions and criteria. As a result of this assessment, together with CEPA toxic classifications for mercury, lead, and certain

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compounds of arsenic and cadmium, a base metal smelter Strategic Options Process ( SOP ) was conducted in 1997 with the result that the industrial sector committed to develop site-specific environmental management plans and reduce sector-wide releases of arsenic, cadmium, lead, mercury and nickel by 80 per cent from 1988 (as the base year) to 2008.

In 1999, a revised CEPA was enacted and has been viewed as granting increased authority to, and mandating increased attention by, federal departments in data collection, pollution prevention and other regulatory actions. As a result of the revised CEPA, Environment Canada has initiated several additional programs. One has been to review the progress being made under the original base metal smelter commitments made as part of the SOP and possibly accelerating their implementation. Another program has been to take action regarding substances known to be toxic under CEPA, including emissions of dioxins and furans, sulphur dioxide and particulate matter. The Company is part of the industry group interacting with Environment Canada on these programs. During 2003, this group examined the options for regulations that might be employed under CEPA to control substances listed as toxic. Presently, pollution prevention plans and a code of practice for base metal smelters are under active debate at a multi-stakeholder level, with a view to using this as the basis for the regulation of toxic substances under CEPA.

Another CEPA-related program seeks to categorize and prioritize all substances on the Domestic Substances List (the DSL ), a list of more than 20,000 substances which are permitted to be produced in or imported into Canada. New substances that are not on the list are required to undergo a pre-manufacturing appraisal in order to be added to the list. Environment Canada has elected to apply criteria for this process that the Company believes are inappropriate for inorganic substances. These criteria were originally developed for synthetic organic chemicals and involve assessments of persistence, bioaccumulation and toxicity. In 2001, an expert advisory group, including a consultant representing the Mining Association of Canada, was organized by Environment Canada for the purpose of reviewing the scientific validity of using persistent, bioaccumulative and toxic ( PBT ) criteria for inorganic substances. In late 2001, this group issued its findings and recommendation to Environment Canada. This group concluded that the persistent, bioaccumulative criteria do not properly categorize metals and other inorganic substances. However, recognizing that the use of PBT criteria is legislated, the group recommended that all inorganic substances should be considered as persistent for the purposes of this categorization, and that toxicity alone should be the criterion by which inorganic substances should be categorized. In June 2002, Health Canada made a proposal for categorizing human exposure to substances on the DSL on the basis of use and on the basis of industry codes originally attached to substances when they were placed on the list. Discussions on this proposal continued through 2003 and the Company cannot at this time identify or predict what additional operating or capital expenditures will be required by the Company to meet the ultimate regulations that may result from these and other possible CEPA-based and Environment Canada programs.

*California Regulatory Actions*

In 1991, the California Air Resources Board ( CARB ) identified nickel and its compounds as a toxic air contaminant. A series of guidelines were then issued for assessing risks of non-occupational exposure, and acute and chronic reference exposure levels ( RELs ) were proposed along with a cancer potency factor for nickel compounds. Because the Company and other nickel producers believed that the guidelines and RELs were not well-founded scientifically and might lead to unjustifiable controls being placed on users of nickel in California and elsewhere, Inco and other nickel producers made submissions criticizing the methods used by the CARB in developing the RELs. In February 2000, California adopted final RELs. Although the final RELs represent an improvement over the initial proposals, the Company believes they are still unjustifiably low. Although the RELs do not appear to have had a significant impact on nickel users in California, the Company is unable to predict at this time what long-term impact the RELs will have in California or, indirectly, in other jurisdictions in which nickel is produced or used.

In June 2003, the California Office of Environmental Health Hazard Assessment proposed a Child-Specific Reference Dose ( CSRD ) for nickel to be used in school site risk assessments. Nickel producer associations of which the Company is a member submitted comments questioning the scientific basis for the proposed CSRD and arguing that it should be at least five times higher. The California Office of Environmental Health Hazard

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Assessment has not yet taken final action on the proposal, which is awaiting external peer review. However, the Company does not believe that the CSRD, even if adopted as proposed, would have a material adverse impact on its operations or financial condition.

Late in 1999, the California Office of Environmental Health Hazard Assessment proposed a public health goal ( PHG ) of one microgram of nickel per litre of drinking water. In conjunction with other nickel producers, Inco submitted comments arguing that this proposal was scientifically unjustified. In August 2001, a final PHG of 12 micrograms of nickel per litre of drinking water was adopted by the California authorities. Although not itself a mandatory standard, this goal presumably will serve as a benchmark for setting a drinking water standard in California. This goal could also affect the perception of the health risks associated with nickel by producers and users of nickel-containing products. In addition, this PHG may have an impact on the EPA 's consideration of a future drinking water standard for nickel or on the drinking water guideline values for nickel being developed or reviewed by the World Health Organization, as discussed below, or by other bodies.

### *Right-to-Know Legislation*

Right-to-Know and other reporting laws have been adopted in many jurisdictions in which the Company operates. These laws generally require employers to advise their workers and their local communities, as well as specified governmental authorities, of the kinds and amounts of specified chemicals, including some chemicals made or used by the Company, which may be present in the workplace, released to the environment, or sent to a recycling or waste management unit, and to develop emergency response programs. Compliance with these Right-to-Know requirements has had no material effect on the Company 's financial position or operations.

### *Harmonization of Classification and Labeling of Chemicals*

In 1990, the International Labour Organization (the ILO ) initiated a project to harmonize existing systems for the classification and labeling of chemicals. This goal was endorsed by the 1992 UN Conference on Environment and Development ( UNCED ) and was included as one of the six areas for action identified in Chapter 19 of Agenda 21 of UNCED on the environmentally sound management of toxic chemicals. UNCED recommended that a globally harmonized hazard classification and compatible labeling system, including material safety data sheets ( MSDSs ) and easily understandable symbols, should be available, if feasible, by the year 2000. In September 2001, a Harmonized Integrated Hazard Classification System for Chemical Substances and Mixtures was approved by the ILO 's Task Force on Harmonization of Classification and Labeling and endorsed by the OECD 's Joint Meeting of the Chemicals Committee and Working Party on Chemicals, Pesticides and Biotechnology. This document and similar documents on Physical Hazard Classification and Hazard Communication Tools were merged to form the Globally Harmonized System ( GHS ). The GHS was adopted by the UN Subcommittee of Experts on the GHS on the Classification and Labelling of Chemicals and the UN Committee of Experts on the Transport of Dangerous Goods and the GHS in December 2002. The GHS system is now ready for adoption by individual countries.

Although adoption of the GHS continues to be considered voluntary, the goal of the Intergovernmental Forum on Chemical Safety, endorsed at the September 2002 World Summit on Sustainable Development is to have as many countries as possible implement the GHS by 2008. As well, Asia-Pacific Economic Cooperation (APEC) is recommending the GHS be adopted, on a voluntary basis, by 2006, and Australia has committed to adopting the GHS by 2006. The countries that are signatories to the North American Free Trade Agreement (Canada, the United States and Mexico) have committed to review their internal systems and consider adopting the GHS. Canada is expecting adoption by 2008. The Company does not believe that the adoption of the GHS will have a material impact on its results of operations or financial condition.

### *European Union Actions*

There are several key areas under discussion at the European Commission concerning nickel in respect of workplace legislation, public health and consumer product legislation, and environmental legislation. In 2003 ten new member states were invited to join the European Union ( EU ) as of May 1, 2004. There will be a re-election of members to the European Parliament in each member state in June 2004. It is not known what impact



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these changes to the EU membership may have on the EU legislative process, but we believe that there will be changes in the area of policy development as a result of the increase in EU membership.

In policy terms, the single biggest development during 2003 was the adoption by the European Commission in late October 2003 of the draft legislative text of a new chemical policy (the NCP) for the EU that will supersede some 30 pieces of current EU legislation. The legislation, which still must be debated and approved by the European Parliament and adopted by the European Council before it can take effect, is not expected to come into force before 2006 at the earliest. The new policy, referred to as REACH (for registration, evaluation, and authorization of chemicals), would place more responsibility on companies to register, test and secure regulatory approval as a condition for producing or importing chemicals in the EU. The registration and evaluation requirements would be triggered by the tonnage of certain substances produced in or imported into the EU. In addition, authorizations would be required for chemicals of high concern, including those which are classified as category 1 or 2 carcinogens, mutagens, or reproductive toxicants and those classified as PBT in the environment. In effect, the REACH system would require producers/ importers of such chemicals to obtain a permit to market them based on their use patterns. It is unknown whether the European Parliament will approve the REACH program as adopted by the European Commission or if amendments will be tabled. As approved by the European Commission, REACH applies to ores, concentrates and intermediates of the mining and metals industries, while exempting comparable materials from the organic compound product chain. It also applies to massive forms of metals and their alloys, which typically are viewed as less hazardous to human health and the environment. The concerns of the metals industry are being tabled through a metals forum group made up of Eurometaux (the non-ferrous metals producers association in the EU), Eurofer (the iron and steel producers association in the EU), and Euroalliage (the alloys producers association in the EU). A socio-economic study, looking at business consequences of the proposed NCP, is under way to assess its potential impact on these sectors. Industry may incur significant costs for administration and implementation, as well as research funding if the NCP is adopted in its present form.

EU Regulation 793/93(EEC), the so-called existing substances regulation, is concerned with the evaluation of the risks of and controls for existing substances. Five nickel substances are listed for review under this regulation. The Company believes that this is the single most comprehensive legislative review of nickel in respect of human health, public health, consumer health and the environment that has been undertaken by a governmental authority worldwide. This legally driven initiative started in 1996, when Denmark, allegedly concerned about the ability of nickel to cause dermal sensitization, placed elemental nickel and nickel sulphate on the third priority substances list developed by the European Commission. In 1996, the Danish Environmental Protection Agency (the DEPA) was appointed the principal agency for conducting risk assessments on these substances. In 2000, three additional nickel compounds, nickel carbonate, nickel chloride and nickel dinitrate, were added to the risk assessment program as part of another priority substances list developed by the European Commission.

These nickel risk assessments have progressed slowly due, in part, to the rapidly changing methodologies for assessing environmental risks of metals in general. The nickel industry has been successful in demonstrating that further research and testing is required for a scientifically credible environmental risk assessment of nickel. A formal research program has been agreed with the European Commission for this work, the details of which will be finalized in early 2004, with an anticipated completion date of early 2005. At that stage, the technical debate on safe levels of nickel in all of the environmental compartments (soils, water and sediment) will resume.

In the area of health risk assessment, the classification of soluble nickel compounds has been referred to the specialized experts group (the SEG) of the European Commission's working group on classification, which is a subgroup of experts of the cancer, mutagenicity and reproductive toxicity classification group. The proposal has been made by the DEPA that all soluble nickel compounds are category 1 carcinogens, i.e. known human carcinogens. Currently, soluble nickel compounds are classified as category 3 carcinogens, which is a much less toxic classification. The evidence to support this classification is being reviewed in the context of the classification criteria of the EU. The nickel industry will be allowed to present scientific information on nickel to the SEG in April 2004.

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Further research and testing on mutagenicity has been mandated for nickel compounds. Mutagenicity is closely related to carcinogenic potential (genotoxic or non-genotoxic mode of action) and helps determine safe levels of nickel exposure. A research proposal has been developed by the nickel industry. This proposal is being reviewed by a technical group of experts and is expected to be agreed on by the technical meeting on risk assessment in March 2004. The research is expected to be completed in 2005.

Soluble nickel compounds have been proposed as category 2 reproductive toxicants under the EU classification system. This proposal is expected to be confirmed at the European Commission classification group meeting in 2004. Such a classification will mean that soluble nickel compounds will be subject to authorization under the REACH program described above. Nickel metal has been proposed as a category 3 reproductive toxicant and respiratory sensitizer. The issue also will be discussed by the classification committee in 2004.

In August 2003, the DEPA released its first draft report concerning risk characterization of the nickel compounds as part of the risk assessment process. This draft report is being reviewed by industry and member states experts and is expected to be revised in late 2004, when further discussions are planned. It is anticipated that the OELs for both metallic nickel and soluble nickel compounds may be lowered as a result of new information in this report. The data to support the proposal to lower nickel OELs are also being reviewed by the European Commission's scientific committee on occupational exposure limits (SCOEL), which has been considering nickel occupational exposure limits for several years. A draft criteria document on occupational exposure limits for nickel was presented to SCOEL in 1997. That document is now being revised. The revised version is expected to be made available to SCOEL in the spring of 2004. New science based OELs for nickel may be recommended.

At this time it is not known what impact these risk assessments and OEL reviews will have on the Company's operations or those of its customers. Recognition is given in the draft risk characterization report to the need for pragmatism, that is, to consider economic and technical feasibility data to be provided by the nickel industry. Further studies on dermal exposure in workplaces have also been suggested as part of the draft risk characterization report. The European nickel group risk assessment team, to which Company personnel belong, is working closely with the European Commission and the DEPA on the nickel risk assessments.

The European Commission's Air Quality Directive is concerned with controlling certain substances in ambient air (nickel, cadmium, arsenic and polyaromatic hydrocarbons). The Directive includes proposed limit values for nickel of 20 nanograms per cubic metre. Control measures proposed for nickel producers and users disregard the fact that the nickel industry is a minor contributor to nickel in ambient air while fossil fuel combustion is the greatest source. It also ignores the fact that point source control of nickel emissions will likely go beyond what is technically feasible under the existing EU Integrated Pollution Prevention Control Directive, which applies to all industrial installations in the EU, even using the best available technology. Moreover, the limit values proposed have no techniques for standardized measurement. The metals industry position, developed by Eurometaux and others, is that the proposed Directive is impractical. Discussions continue at the European Parliament level, and it is unknown what the final outcome will be.

The European Commission's Water Framework Directive, which regulates water quality standards in the EU, listed nickel as one of the priority substances of concern and indicated that nickel may be subject to emission control measures that are more stringent than those currently in effect. It is not yet known what the EU nickel water quality standards will be or what will be the consequences to industries producing or using nickel in the EU.

Several directives related to the end of life of nickel products are still being finalized and/or implemented in the EU. These include a directive on integrated product policy, end of life for vehicles, waste electrical and electronic equipment, restrictions on the use of hazardous substances in electrical and electronic equipment, and the revised batteries directive. The revised batteries directive has been debated at the European Commission, which decided against a ban on nickel-cadmium batteries in favour of putting in place more stringent recycling targets. This new version of the battery directive is likely to be debated at the European Parliament early in 2004 and, if sanctioned by the Parliament, would come into force over the next few years in all EU member states.

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The Seveso 2 Directive recently reissued by the European Commission is concerned with preventing major accidents and releases of hazardous materials at industrial installations. Industrial installations that store or produce certain tonnages of hazardous substances listed in the Seveso Directive must make a safety report to their local authorities and obtain a permit for operation. Nickel oxide (granular form) remains listed in the Directive.

Consideration is being given to revising the European Commission's Marketing Restrictions and Use Directive, which regulates the use of nickel in articles in direct and prolonged contact with skin, such as jewelry. An association of nickel producers of which the Company is a member is closely following this initiative as part of its product stewardship activities.

To comply with pollution control regulations in the U.K., the Company's refineries at Clydach, Wales and Acton, England have obtained the necessary authorizations to continue to operate. These authorizations include prescribed emission release limits and are conditional upon the Company carrying out certain environmental improvements. In order to achieve continuous improvement, the government reviews these authorizations at least every four years, at which time new environmental improvement conditions may be established. In late 2001 and early 2002, these authorizations were resubmitted to the relevant governmental authorities as required under new legislation arising from the EU Integrated Pollution Prevention and Control directive. The authorization for the Acton refinery has been received and there are no environmental improvement conditions attached to it that are expected to have an adverse effect on operations. The authorization for the Clydach refinery was received containing several environmental improvement conditions relating to reduced water and air emissions. A phased program is in place to ensure this operation fulfils these requirements within the agreed timeframes. Given that both the Acton and Clydach refineries have received ISO 14001 certification, it is not expected that any of these conditions will have an adverse effect on operations at the Clydach refinery.

### *WHO Drinking Water Guidelines*

The World Health Organization (the WHO) periodically reviews its guideline values for contaminants in drinking water. Its most recent review of nickel in drinking water began in 1995. Over the past several years nickel producers' organizations, including NiPERA, have made submissions to the WHO concerning the most appropriate method for extrapolating animal test data to humans. The WHO recommended an extraordinarily stringent guideline value of 20 micrograms of nickel per litre of drinking water. This value was disputed by the nickel industry and, in a final action in 1997, the WHO accepted the value as provisional. In 2000, a new regulatory research study on the reproductive effects of ingested nickel in animals was completed. This study, which was funded by the nickel industry, provides an improved scientific basis for setting a nickel guideline level for drinking water and has been submitted to the WHO for its consideration. While WHO is not a regulatory body itself, the WHO guideline values influence governmental regulatory agencies around the world in adopting standards. It is impossible to predict what the final guideline level for nickel in drinking water will be, what effect it will have in specific jurisdictions, including Canada, or what impact it will have on the Company's results of operations or financial condition.

### *Other Environmental Control Regulations*

The Company and other mining companies in Canada are aware of and concerned about the increasing desire on the part of many regulatory authorities throughout the world to limit the mining, refining and use of metals in the future. This desire is based on the belief of governments in the changing expectations of society towards various approaches to the concept of sustainable development, a concept that has been defined by regulatory and other bodies differently but, at a minimum, appears to focus on meeting the needs of the present without compromising the ability of future generations to meet their own needs. In response to this view, the Company believes that there is a tendency for some governments to use inadequate or incorrect information, to rely on inappropriate methodologies, and to apply the so-called precautionary principle in an unwarranted manner in making regulatory decisions regarding metals. An example of this approach is the predisposition by some regulators to identify metals, including nickel, as persistent, bioaccumulative, toxic (PBT) chemicals that should be targeted for use reduction or waste minimization.

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In 1998, the EPA published a draft list of 53 chemicals or groups of chemicals described as PBT substances that were to be the focus of a voluntary waste minimization initiative. Eleven of the 53 chemicals on the list were metals, including nickel. The inclusion of nickel on this list, if finalized, could have led to increased regulation of nickel, placing additional burdens on customers and users of nickel and possibly resulting in the substitution of other products for nickel. In submissions made to the EPA, the Company pointed out that the scoring and ranking scheme used to develop this list does not, on a scientific and technical basis, properly apply to metals, so that nickel should be removed from the list. Similarly, at an expert workshop conducted under the joint sponsorship of EPA and other organizations in January 2000, the prevailing view was that PBT criteria, which were developed to evaluate potential environmental hazards of organic chemicals, could not appropriately be applied to metals and inorganic metal compounds. These views apparently had some effect. In the summer of 2002, EPA released the final version of what is now referred to as the Waste Minimization Priority Chemicals List. Only three metals, cadmium, lead and mercury, are included on the list, and they were selected for reasons that do not involve a PBT determination.

For the last two years, EPA has been engaged in developing a comprehensive cross-agency metals assessment framework that will establish guidance for EPA programs to use in assessing the hazards and risks of metals and metal compounds. Completion of the framework is expected in the second half of 2004 or the first half of 2005. In the fall of 2003, a series of white papers addressing various issues relating to the hazard assessment of metals was submitted to the EPA. These white papers, prepared by independent experts under contract to the EPA, emphasized the complexity of evaluating the hazard potential of metals and questioned the scientific basis for applying to metals the same PBT criteria that the EPA uses to evaluate the hazards of organic compounds. In light of this, it seems likely that the metals assessment framework as ultimately adopted by the EPA will take a different approach one that is more suitable for evaluating the hazards of metals and inorganic metal compounds.

In the future, as in the past, various supranational, national, provincial, state and local governments and authorities under which the Company operates may impose regulations covering the emission of air pollutants, the discharge of process wastewater and the generation, storage, treatment and disposal of liquid and solid wastes that could apply to various of the Company's operations and that could impose additional compliance costs on the affected Inco operating entities or on nickel-using industries. No proposed regulation of which the Company is aware would currently impose costs that would materially affect the Company's financial position or operations. Reference is made to the discussion of future removal and site restoration costs and related plans under Future Removal and Site Restoration; Closure and Post-Closure Plans above.

*Environment, Health and Safety Audits*

The Company has, over the past number of years, conducted environment, health and safety (EH&S) audits at its wholly-owned operating facilities as well as at operations in which it has at least a 50 per cent equity interest and certain affiliates in which it has less than a 50 per cent equity interest. The EH&S audit program is reviewed annually by an external consultant in order to provide the Company with an independent review of the program, evaluate the extent to which the program is meeting Inco's goals and objectives, and determine whether the program is in accordance with standard industry audit practices. The Company has broadened the focus of its EH&S audits from compliance audits, aimed at identifying specific problems, to management system audits that seek not only to identify problems but also to examine the root cause of these problems and correct deficiencies in the system. The program comprises 17 key areas (six environmental, two health, eight safety and one administrative). Audit results are reported to the facility management, which develops an action plan to correct any deficiencies. The Environment, Health and Safety Committee of Inco's Board of Directors oversees the program, reviewing audit findings and action plans. EH&S audits were conducted at 9 facilities worldwide in 2003.

*Environmental and Health Management Systems*

In 2001, the Company's Canadian operations began to develop and implement formal environmental management systems conforming to the Mining Association of Canada's Environmental Management Framework (the EMF). The EMF also conforms to the ISO 14001 Environmental Management System Standard.

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The Company's operations in the United Kingdom, ITL, Jinco and Taiwan Nickel have been certified to the ISO 14001 Environmental Management System Standard.

In order to conform to the ISO 14001 Standard, in 2001, the Company broadened its environmental, health and safety policy to include policies related to social responsibility and sustainable development and to include pollution prevention as key elements of its policy. Work also began on the identification and ranking of environmental aspects and effects relating to the Company's operations and the development of action plans to deal with any significant environmental effects. This work continued in 2003.

In 2001, the Company established an internal working group to undertake an analysis of current health practices and activities in the Company's operations in Canada and the United Kingdom with a view to creating a single overarching health management system (HMS). The HMS would provide a mechanism for workplace health management to assist in meeting applicable legal and other health requirements. In mid-2002, the Company elected to develop an integrated Health, Safety and Environmental Management System consistent with the Occupational Health and Safety Management System (OHSMS) 18001 in the U.K., the ISO 9001 quality standard, the environmental management system standard ISO 14001, and the Mining Association of Canada's EMF.

### ***Employees***

At year-end 2003, the Company had 10,478 employees, compared with 10,534 employees at year-end 2002 and 10,258 employees at year-end 2001. At year-end 2003, 6,589 of the Company's employees were located in Canada, 167 in the United States, 392 in the United Kingdom, 2,977 in Indonesia and 353 in other countries. Most full-time employees participate in the Company's performance through profit-sharing or other bonus arrangements.

In late August 2003, the Company and its unionized hourly production and maintenance workers at its Ontario operations reached agreement on a new collective agreement. This agreement followed a three-month strike that began on June 1, 2003. The new agreement, which remains in effect until May 31, 2006, included increases in wages and pensions, an agreement with the union to reduce the cost of delivering health care benefits while preserving benefit levels, and certain efficiency improvements and cost savings on health care benefits. The Company's three-year collective agreement with its unionized office, clerical and technical employees at its Ontario operations remains in effect until March 31, 2004. At this time, the Company cannot predict whether a new agreement with the employees can be reached by March 31, 2004. The Company does not currently expect that, if these employees were to go on strike, there would be any significant disruption to production at the Ontario operations or any other adverse effect on this unit's results of operations. At the Manitoba operations, the Company's three-year collective agreement with its unionized production and maintenance workers remains in effect until September 2005. In Indonesia, PT Inco entered into a new two-year contract with its unionized employees in January 2003 which expires in December 2004. In New Caledonia, the Company has two unions representing some of its employees. Through an employer's association of which VBNC is the controlling member, the Company negotiated a collective agreement in September 2002 covering the construction of the initial phase of the Voisey's Bay project.

### **Miscellaneous Investments**

In connection with the disposition of the battery and related products businesses conducted by Inco ElectroEnergy Corporation (IEEC), which was completed in 1983, the Company assumed responsibilities for certain expenditures and other costs associated with certain proceedings or administrative actions initiated by or involving the EPA or state environmental agencies concerning certain facilities operated by these businesses. It also assumed responsibility for compliance by these facilities with applicable local environmental regulations covering the treatment or discharge of certain wastewaters, compounds or effluents into publicly-owned treatment works, sewage systems, groundwater resources and watercourses and the related cleanup of deposits of certain minerals and compounds from such watercourses. The Company's total accounting reserve relating to these remaining responsibilities, which reflects their estimated cost, increased to \$30 million at year-end 2003 due primarily to the cost estimates developed during 2003 associated with remediation plans for two former industrial

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sites in the United States where the Company had moved forward with the review by applicable state regulatory agencies of these remediation plans it had developed for these sites, compared with \$7 million at year-end 2002 and \$8 million at year-end 2001.

### **Other Information**

In addition to properties discussed under **Description of Business** above, certain of Inco's sales offices are leased and the Company also leases office space in Toronto, Ontario; London, England; Saddle Brook, New Jersey; and in certain other locations around the world.

Operations in certain foreign countries involve certain risks, including risks of monetary instability, changes in exchange rates, inconvertibility of currencies and expropriation and nationalization. For example, Indonesia experienced a significant devaluation of its currency and other economic issues in recent years and the uncertain political situation in Indonesia, primarily the result of the economic, social and political issues facing that country, could adversely affect PT Inco's ability to operate and, accordingly, the Company's results of operations, financial condition and prospects. For further information on the political situation in Indonesia, see **PT International Nickel Indonesia Tbk General** above.

For financial information by geographic location, see Note 19 to the financial statements under Item 8 of this Report.

### **Shareholder Rights Plan**

The Company's current shareholder rights plan is set out in a Rights Plan Agreement, as amended and restated as noted below, entered into between the Company and CIBC Mellon Trust Company, as Rights Agent, and is designed to (i) encourage the fair and equal treatment of shareholders in connection with any bid for control of the Company by providing them with more time than the minimum statutory period during which such bid must remain open in order to fully consider their options, and (ii) provide the Company's Board of Directors with additional time, if appropriate, to pursue other alternatives to maximize shareholder value.

The plan was initially approved by the Company's Board of Directors in September 1998 and became effective in October 1998. It was amended in certain respects by the Company's Board of Directors in February 1999 to ensure that it was consistent with rights plans which had been recently adopted by other Canadian companies. The amended plan was approved by the shareholders at the Company's 1999 Annual and Special Meeting of Shareholders in April 1999. In February 2002, Inco's Board of Directors approved certain minor amendments to the plan to ensure that its terms remained consistent with other rights plans in Canada and unanimously recommended that the plan, as proposed to be amended, be reconfirmed, as amended and restated, by the shareholders. Such reconfirmation by the shareholders was obtained at the Company's Annual and Special Meeting of Shareholders in April 2002. The plan remains in effect until October 2008 subject to reconfirmation by holders of the Company's voting securities at the Company's annual meeting in 2005.

The rights issued under the plan are attached to and trade with the Company's Common Shares and no separate certificates will be issued unless an event triggering these rights occurs. Certificates evidencing Common Shares will be legended to reflect that they evidence the rights until the Separation Time (as defined below). Holders of the Company's LYON Notes and the certificates of entitlement attached thereto (which entitle their holders to receive rights in the event that the related security is converted into Common Shares) will generally be entitled to receive, upon conversion of the relevant security and presentment of the certificate of entitlement, respectively, rights in an amount equal to the number of Common Shares issued upon conversion of such securities.

The rights will separate from the Common Shares and be transferable, trade separately from the Common Shares and become exercisable at the time (the Separation Time) when a person acquires, or announces its intention to acquire, beneficial ownership of 20 per cent or more of (i) the Company's then outstanding Voting Securities (defined at this time to be the Company's Common Shares) or (ii) its then outstanding Common Shares alone, in either case without complying with the permitted bid provisions of the plan (as summarized below), or without the approval of the Company's Board of Directors. Should such an acquisition occur, each right would

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entitle its holders, other than the acquiring person or persons related to or acting jointly or in concert with such person, to purchase additional Common Shares of the Company at a 50 per cent discount to the then current market price. The acquisition by any person (an Acquiring Person ) of 20 per cent or more of the Company s Common Shares or Voting Securities, other than by way of a permitted bid, is referred to as a Flip-in-Event . Any rights held by an Acquiring Person will become void upon the occurrence of a Flip-in-Event.

A permitted bid is a bid made to all holders of the Company s outstanding Voting Securities that is open for at least 60 days. If, at the end of such 60-day period, more than 50 per cent of the Company s then outstanding Common Shares, other than those securities owned by the party making the bid and certain related persons, have been tendered, such party may take up and pay for the Common Shares but must extend the bid for a further 10 business days to allow other shareholders to tender, thus providing shareholders who had not tendered to the bid with enough time to tender to the bid once it is clear that a majority of Common Shares have been tendered.

Under the plan, the Company can (i) waive its application to enable a particular takeover bid to proceed, in which case the plan will be deemed to have been waived with respect to any other takeover bid made prior to the expiry of any bid subject to such waiver or (ii) with the prior approval of the holders of Voting Securities or rights, redeem the rights for nominal consideration at any time prior to a Flip-in-Event.

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**Item 3. *Legal Proceedings***

There are no material pending legal proceedings to which the Company or any of its subsidiaries is a party or of which their property is the subject. The Company and its subsidiaries are subject to routine litigation incidental to the business conducted by them, to various environmental proceedings, and to other litigation related to such business that the Company does not believe to be material. Among the environmental proceedings are claims for personal injury, enforcement actions and certain claims dating back a number of years in which one of the Company's subsidiaries was designated, under the United States federal environmental law known as Superfund, or CERCLA, as a potentially responsible party. The Superfund claims assert that, as a potentially responsible party, the Company's subsidiary sent waste to a contaminated landfill or similar site and is jointly and severally liable for the cost of remediating such site. These claims have not proceeded to a point where a reliable assessment can be made of the costs to the Company, assuming responsibility is found to exist or liability is determined, but the Company believes, based upon its present information concerning these matters and its past experience, that its potential liability, if found to exist, would not be significant.

The Company has from time to time been named as a party or charged in connection with the alleged violation of, including exceeding regulatory limits relating to discharges under, certain environmental or similar laws and regulations applicable to its operations in Canada and elsewhere. Such proceedings have involved, and with respect to currently pending charges may ultimately involve, fines or similar sanctions in excess of \$100,000. However, none of these currently pending or threatened proceedings are material, either singly or in the aggregate, to the Company's results of operations, financial condition or liquidity.

**Item 4. *Submission of Matters to a Vote of Security Holders***

None.



**Table of Contents****Executive Officers of Inco Limited**

The names, offices held and ages as of February 20, 2004 of the executive officers of Inco Limited are shown below.

<b>Name</b>	<b>Office</b>	<b>Age</b>	<b>Officer Since</b>
Scott M. Hand	Chairman and Chief Executive Officer	61	1984
Peter C. Jones	President and Chief Operating Officer	56	1997
Stuart F. Feiner	Executive Vice-President, General Counsel and Secretary	55	1992
Peter J. Goudie	Executive Vice-President, Marketing	55	1997
Farokh S. Hakimi	Executive Vice-President and Chief Financial Officer	55	2002
Logan W. Kruger	Executive Vice-President, Technical Services	53	2003
Ronald C. Aelick	Executive Vice-President and President, Canadian and U.K. Operations	55	1995
Wm. Gordon Bacon	Vice-President, Technology and Engineering	59	1997
Subhash Bhandari	Vice President and Chief Information Officer	59	2001
Bruce R. Conard	Vice-President, Environmental and Health Sciences	61	1995
Mark J. Daniel	Vice-President, Human Resources	57	2000
Philippus F. du Toit	Managing Director, Voisey's Bay Nickel Company Limited	51	2003
Donald T. Hurley	Vice-President and Treasurer	56	1998
John B. Jones	Vice-President, Business Development Asia	61	1999
Gary G. Kaiway	Vice President, Taxation	55	2001
William B. Kipkie	Vice-President, Inco Special Products	58	2003
Ronald A. Lehtovaara	Vice-President and Comptroller	53	1996
William A. Napier	Vice-President, Environment and Health	49	2000
S. Nicholas Sheard	Vice-President, Exploration	54	2003
Alan C. Stubbs	Vice-President, Public and Government Affairs	59	1999

Each executive officer is elected by the Board of Directors of Inco Limited annually, at the first meeting of such Board ( Annual Board Meeting ) after the annual meeting of shareholders, for a term of one year or until a successor shall have been duly chosen and qualified, except in those cases where an executive officer is elected at other than the Annual Board Meeting, in which event such executive officer's tenure will expire at the next Annual Board Meeting unless re-elected. Such tenure is subject to an officer's resignation or removal as provided in the Company's By-law No. 1, its sole by-law, and the Company's standing resolution adopted pursuant thereto.

Except for the officers mentioned below, each executive officer named above has been an officer or executive or key managerial employee of Inco Limited or one of its subsidiaries during the past five years. From October 1997 until November 1999, Mr. Hakimi was Vice-President and Treasurer of Cyprus Amax Mineral Company, a leading producer of copper and the world's largest producer of molybdenum, based in Englewood, Colorado, and from January 2000 until July 2001 he was Vice-President and Chief Financial Officer of Rio Algom Limited, a global mining and metals company based in Toronto, Ontario. From September 1998 until June 2002, Mr. Kruger was President and Chief Executive Officer, Hudson Bay Mining and Smelting Co. Limited, a mining company based in Winnipeg, Manitoba, and from June 2002 until September 2003, he was Executive Vice President and Head of Copper, Anglo American plc, a global mining and metals company based in London, England. From May 1997 until January 2000, Mr. du Toit was Operations Director, Voest Alpine Industries Inc., an engineering company based in Poole, England, and from February 2000 until April 2003 he held senior management positions, most recently President, with Diavik Diamond Mines Inc., a diamond mining company based in Yellowknife, Northwest Territories. During the five-year period prior to joining the Company, Mr. Bhandari held senior management positions, most recently General Manager, Purchasing and Information Systems, with Toyota Motor Manufacturing Canada Ltd., an automobile manufacturing company based in Cambridge, Ontario; Mr. Kaiway held senior management positions, most recently Vice-President, Taxation, with Placer Dome Inc., a

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gold mining company based in Vancouver, British Columbia; Mr. Sheard held senior management positions, most recently Global Exploration Manager, with MIM Holdings Pty Ltd., a base metals, gold and coal mining company based in Brisbane, Australia; and Mr. Stubbs was Vice-President, Public Affairs, MacMillan Bloedel Limited, a forest products company based in Vancouver, British Columbia. None of these companies is affiliated with Inco Limited.

The dates shown in the table extend from the first date of election as an executive officer of the Company. There are no family relationships among the directors and executive officers of Inco, and no arrangements or understandings between any executive officer and any other person pursuant to which he was elected as an executive officer.

**Table of Contents****PART II****Item 5. *Markets for Inco Limited's Common Shares, Related Shareholder Matters and Inco Limited's Issuances or Purchases of Equity Securities*****Common Shares*****Market Information***

There are two principal markets on which the Company's Common Shares are traded, the New York Stock Exchange (the NYSE) and the Toronto Stock Exchange (the TSX).

The high and low closing sale prices for the Company's Common Shares as reported on the NYSE and the TSX for each quarter during the past two years are as follows:

**New York Stock Exchange (U.S. \$)**

	2003				2002			
	1st Q	2nd Q	3rd Q	4th Q	1st Q	2nd Q	3rd Q	4th Q
High	23.12	21.17	28.51	40.90	19.82	23.66	22.45	21.99
Low	18.00	18.30	20.98	28.30	16.52	18.98	15.30	15.51

**The Toronto Stock Exchange (Cdn. \$)**

	2003				2002			
	1st Q	2nd Q	3rd Q	4th Q	1st Q	2nd Q	3rd Q	4th Q
High	35.40	28.67	38.46	53.63	31.40	36.25	33.91	34.25
Low	26.35	25.15	27.99	37.98	26.35	30.16	24.30	24.80

On March 12, 2004, the closing sale prices for the Company's Common Shares were \$34.90 on the NYSE and Cdn.\$46.68 on the TSX.

During the fourth quarter of 2003, no equity securities of the Company were sold by the Company which were not registered under the Securities Act of 1933, as amended.

***Holder of Common Shares***

The total number of holders of record of the Company's Common Shares as of February 20, 2004 was 18,009.

***Dividends***

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Subject to the preferential rights of any prior ranking shares (of which none were issued and outstanding as of the date of this report), the holders of Common Shares are entitled to such dividends as may be declared by the Board of Directors out of funds legally available therefor. No dividend or other distribution on the Common Shares shall be paid, and no Common Share shall be acquired for value, unless dividends on all outstanding Preferred Shares have been paid for all past quarterly periods.

At its meeting in February 1999, the Board of Directors eliminated the payment of quarterly dividends in respect of the Common Shares. The Board continues to review on a periodic basis the declaration and payment of dividends on the Common Shares in the future. The Company's dividend policy, under normal circumstances and after taking into account the Company's short-term and long-term needs and objectives, is to declare and pay dividends on the Common Shares averaging approximately one-third of reported net earnings over a period of years. A sustainable level of regular quarterly dividends would be paid, adjusted, when appropriate, by extra dividends. The quarter-to-quarter decision as to the restoration and amount of any quarterly dividend per Common Share is reviewed by the Board of Directors and determined with reference to a number of factors, including current business results and cash needs.

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### ***Common Share Purchase Warrants***

As part of the redemption price the Company paid in connection with the redemption of the Company's Class VBN Shares discussed under Class VBN Shares below, the Company issued approximately 11 million Common Share Purchase Warrants (the Warrants). The Warrants were issued under, and are governed by, a Warrant Agreement dated as of December 1, 2000 by and among the Company, CIBC Mellon Trust Company, as the Canadian Warrant Agent, and ChaseMellon Shareholder Services, L.L.C., as the U.S. Warrant Agent (the Warrant Agreement).

Each whole Warrant entitles the holder to purchase one Common Share at an exercise price of Cdn.\$30.00 (or the equivalent in U.S. dollars based upon then prevailing exchange rates at the time of exercise), subject to certain adjustments (the Exercise Price), until 5:00 pm (Toronto time) on August 21, 2006. Any Warrants not exercised prior to such date will expire. A Warrantholder does not have any voting or pre-emptive rights or any other rights as a shareholder of the Company until the Warrants held by such holder have been duly exercised and Common Shares of the Company have been issued to the holder pursuant thereto.

The Warrant Agreement provides that the Exercise Price and/or the number and kind of securities or property issuable on the exercise of the Warrants are subject to adjustment in certain events, including (1) the subdivision or consolidation of the Common Shares, (2) the issuance to all or substantially all the holders of Common Shares of a stock dividend or other distributions excluding any issuance of securities to holders of outstanding Common Shares which constitutes a Dividend Paid in the Ordinary Course (defined generally in the Warrant Agreement to include dividends or other distributions exceeding certain threshold aggregate or annual amounts based upon the value of the dividends or other distributions paid or consolidated net earnings for specified periods), and (3) the distribution to all or substantially all the holders of Common Shares of (i) shares of any other class, (ii) rights, options or warrants to acquire Common Shares, or (iii) cash, property or other assets of the Company (excluding, in each case, Dividends Paid in the Ordinary Course).

The Exercise Price and/or the number and kind of securities or property issuable on exercise will also be subject to certain adjustments in connection with certain other events, including any change, reclassification or alteration of the Common Shares, the consolidation, amalgamation, merger or other similar arrangement of the Company with another Company, or the transfer of all or substantially all of the Company's assets.

No adjustment in the Exercise Price or the number or kind of securities or property issuable upon exercise will be required to be made (1) unless the cumulative effect of such adjustment or adjustments would change the Exercise Price by at least one per cent or, in the event of a change in the number of Common Shares purchasable upon exercise, the number of Common Shares issuable would change by at least one one-hundredth of a Common Share or (2) in respect of the issue of Common Shares pursuant to (i) the exercise of the Warrants or (ii) the Company's Optional Stock Dividend Program and Share Purchase Plan and options granted current or former employees of the Company or any other option or share purchase plan.

The Warrant Agreement provides that modifications and alterations to it and to the Warrants may be made if authorized by extraordinary resolution and if all other necessary approvals are received. The term extraordinary resolution is defined in the Warrant Agreement to mean, in effect, a resolution passed by the affirmative votes of the holders of not less than 66 2/3 per cent of the Warrants represented and voting at a meeting of Warrantholders or an instrument or instruments in writing signed by the holders of not less than 66 2/3 per cent of the outstanding Warrants. The Warrant Agreement and the Warrants may be modified and altered without authorization by extraordinary resolution and if all necessary approvals are received in order to cure defects or ambiguities, to make ministerial amendments otherwise provided that the rights of Warrantholders are not materially adversely affected thereby.

The Warrants are listed on the TSX and on the NYSE. Subject to applicable law, Inco may purchase Warrants in the market or by tender or private contract, and any Warrants so purchased will be cancelled.

### ***Other Information***

Under its articles of continuance, the Company is authorized to issue an unlimited number of Common Shares.

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For a description of the Company's outstanding debentures and notes which are convertible into Common Shares, see Notes 11 and 14 to the financial statements under Item 8 of this Report.

The Common Shares have general voting rights. At shareholders' meetings, each holder of these securities is entitled to one vote for each share held and there are no cumulative voting provisions. See Note 17 to the financial statements under Item 8 this Report.

### **Class VBN Shares**

At a special meeting of shareholders held on November 28, 2000, the Company received the requisite shareholder approval to amend the terms of the Class VBN Shares that had been created in August 1996 in connection with the Company's acquisition of Diamond Fields to provide for their redemption. The amendments allowed the Company to redeem each of its Class VBN Shares for Cdn.\$7.50 (or the equivalent in U.S. dollars) in cash and a fraction, 0.45, of a Warrant. For a description of the Warrants, see "Common Share Purchase Warrants" above. All of the Class VBN Shares were redeemed by the Company, effective December 14, 2000, for a total redemption price of \$133 million plus approximately 11.6 million Warrants which were reserved for issuance. As of December 31, 2003, 2002 and 2001, approximately 11 million Warrants had been issued in connection with this redemption. Approximately 550,000 Warrants still have not been issued given the limited number of holders of Class VBN Shares who did not accept the redemption consideration and elected under applicable legislation prior to the effective date of the redemption to have a court in the Province of Ontario determine the fair value of their Class VBN Shares. Through March 12, 2004, this court proceeding was still in discovery and related preliminary stages.

### **Preferred Shares**

#### *Certain Provisions of the Preferred Shares as a Class*

##### *Issuable in Series*

The Company's authorized share capital includes 45 million Preferred Shares issuable in series, each series consisting of such number of shares and having such provisions attached thereto as may be determined by the Board of Directors of the Company, subject to a maximum aggregate issue price of Cdn.\$1,500 million (or the equivalent in other currencies). As of the date of this Report, no Preferred Shares were issued or outstanding.

##### *Priority*

The Preferred Shares of each series rank on a parity with the Preferred Shares of every other series, and prior to the Common Shares with respect to the payment of cumulative dividends and the distribution of assets on a liquidation, dissolution or winding up of the Company or for the purpose of winding up its affairs ( "liquidation" ).

##### *Creation and Issue of Additional Preferred Shares*

Subject to applicable law, the Company may, without the consent of the holders of the Preferred Shares as a class, (i) create additional Preferred Shares, (ii) create preferred shares of another class or classes ranking on a parity with the Preferred Shares with respect to the payment of dividends and/or the distribution of assets on liquidation and (iii) increase any maximum number of authorized shares of any one or more of such other classes of shares. If (but only so long as) any dividends are in arrears on any outstanding series of the Preferred Shares, the Company may not, without the consent, by a simple majority of the votes cast, of the holders of the Preferred Shares as a class, (i) issue any additional series of the Preferred Shares, or (ii) issue preferred shares of another class ranking on a parity with the Preferred Shares with respect to the payment of dividends and/or the distribution of assets on liquidation.

##### *Class Voting Rights*

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The holders of the Preferred Shares are not entitled to any voting rights as a class except (i) as provided above, (ii) as provided by law, or (iii) with respect to the right to vote on certain matters as described under

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Modification below. When the holders of Preferred Shares vote as a class, or when two or more series of Preferred Shares vote together at a joint meeting, each holder has one one-hundredth of a vote in respect of each Canadian dollar (or its equivalent in a foreign currency at the date of issuance) of the issue price of the Preferred Shares he or she holds.

The Board of Directors of the Company may, at the time of creation of any series of Preferred Shares, confer voting rights on such series in addition to the voting rights of the holders of the Preferred Shares as a class. It is the Board of Director's intention that, with respect to the creation of any future series of Preferred Shares, to the extent that such Preferred Shares would have general voting rights then such shares would not have more than one vote in respect of each Preferred Share. The voting rights attached to the Series E Preferred Shares as a series are summarized below under Certain Provisions of the Series E Preferred Shares as a Series Series Voting Rights .

*Modification*

The class provisions attaching to the Preferred Shares may be amended at any time with such approval of the holders of such shares as may then be required by law or by the rules of any stock exchange on which the shares or any series of Preferred Shares are then listed. Currently, this approval requirement is by at least two-thirds of the votes cast at a meeting of such holders duly called for the purpose and at which a quorum is present, or as are required by the rules of any stock exchange upon which the shares of any series of Preferred Shares are then listed. In addition, the approval by at least two-thirds of the votes cast at a meeting of the holders of all shares of the Company carrying general voting rights is currently required by law for the amendment of such class provisions.

*Series E Preferred Shares*

The Series E Preferred Shares issued in August 1996 in connection with the acquisition of Diamond Fields were redeemed by the Company on May 1, 2003.



**Table of Contents****Securities Authorized for Issuance Under Equity Compensation Plans**

The number of shares of the Company that may be issued upon the exercise of outstanding options, warrants and rights under the Company's equity compensation plans at December 31, 2003, the weighted average exercise price of such options, warrants and rights, and the number of shares remaining available for future issuance under such plans are shown in the following table:

Plan category	(A) Number of securities to be issued upon exercise of outstanding options, warrants and rights <sup>(1)</sup>	(B) Weighted average exercise price of outstanding options, warrants and rights	(C) Number of remaining securities available for future issuance under equity compensation plans (excluding securities reflected in column (A)) <sup>(2)</sup>
Equity compensation plans approved by security holders	4,572,605	\$23.43	3,785,000(3)
Equity compensation plans not approved by security holders			
<b>Total</b>	<b>4,572,605</b>	<b>\$23.43</b>	<b>3,785,000(3)</b>

- (1) Includes shares authorized for issuance upon the exercise of options outstanding as of December 31, 2003 under (i) the Company's 1993 Key Employee Incentive Plan and 1997 Key Employees Incentive Plan, each of which has been superseded and under which no further options may be granted; (ii) the Company's 2001 Key Employees Incentive Plan; and (iii) the Company's 2002 Non-Employee Director Share Option Plan which has been suspended by the Company's Board of Directors as of February 3, 2004 (the 2002 NEDSOP).
- (2) Includes shares authorized for issuance as of December 31, 2003 pursuant to the exercise of options which may be granted under the Company's 2001 Key Employees Incentive Plan and the 2002 NEDSOP.
- (3) Includes 200,000 Common Shares available for future issuance under the 2002 NEDSOP. See Note 1 above.

**Other Information**

There are no charter or contractual provisions expressly limiting either the amount of cash dividends which the Company may declare and pay on its Common Shares or the right of non-residents of Canada, as such, to hold or vote any of the Common Shares of the Company. There are, however, certain requirements on the acquisition of control of Inco's securities by non-residents of Canada. The *Investment Canada Act* (the Act) requires notification to and, in certain cases, advance review and approval by, the Government of Canada, of the acquisition by a non-Canadian of control of a Canadian business, all as defined in the Act. Generally speaking, in order for an acquisition to be subject to advance review and approval, the asset value of the Canadian business being acquired must meet or exceed certain monetary thresholds. See also the discussion of the Shareholder Rights Plan under Shareholder Rights Plan above and in Note 17 to the financial statements under Item 8 of this Report.

Canadian federal tax legislation, in conjunction with applicable tax treaties, generally requires a 15 per cent withholding from dividends paid to the Company's shareholders resident in the United States, the United Kingdom and most western European countries. Similarly, depending upon applicable tax treaties, dividends paid to other non-residents of Canada are subject to a withholding tax at a maximum rate of 25 per cent. Interest payable on the Company's debt securities held by non-Canadian residents may also be subject to Canadian withholding tax, depending upon the terms and provisions of such securities and any applicable tax treaties. United States backup withholding may apply to dividend and certain other payments made to beneficial owners of the Company's shares who are United States persons for United States federal income tax purposes and who (i) fail to provide an accurate taxpayer identification number or are notified by the Internal Revenue Service that they have failed to report all interest and dividends required to be shown on their federal income tax returns or (ii) in certain circumstances, fail to comply with applicable certification requirements.

Canadian federal tax legislation, in conjunction with applicable tax treaties, generally requires that we withhold 15 per cent from dividends paid by the Company to its shareholders resident in the United States, the United Kingdom and most western European countries. Similarly,

depending upon applicable tax treaties,

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dividends paid to other non-residents of Canada are subject to a withholding tax at a maximum rate of 25 per cent. The amount of a stock dividend (for tax purposes) would generally be equal to the amount by which the stated capital of the Company has increased by reason of the payment of such dividend. Under regulations presently in effect in the United States, the Company is generally subject to the U.S. backup withholding rules which would require withholding at a rate of 28 per cent on dividends and interest paid to certain U.S. persons who have not provided the Company with a taxpayer identification number. Recent legislation enacted in the U.S. has reduced the tax rate to 15 per cent on dividends paid to U.S. individual shareholders of non-U.S. corporations such as the Company that meet certain requirements.

Through subsidiaries and affiliates, the Company's operations are conducted in numerous countries and some \$2,600 million of the Company's consolidated total assets are located outside Canada and the United States. Accordingly, operations are subject to various governmental policies or regulations and changes therein and the risks associated with doing business in many overseas locations.

At year-end 2003, 62 per cent of the holders of our common shares had addresses in Canada, 28 per cent had addresses in the United States and 10 per cent elsewhere. With respect to our Common Shares, as of year-end 2003 Canadian residents of record held 46 per cent of our issued and outstanding Common Shares, United States residents of record held 53 per cent and residents of record of other countries held one per cent.

**Table of Contents****Item 6. Selected Financial Data**

The following table provides selected financial data as reported in the Company's Consolidated Financial Statements on the basis of Canadian generally accepted accounting principles ( GAAP ):

	Year Ended December 31,				
	2003	2002 <sup>(3)</sup>	2001 <sup>(3)</sup>	2000 <sup>(3)</sup>	1999 <sup>(1)(3)</sup>
		(Restated)	(Restated)	(Restated)	(Restated)
	(\$ in millions, except per share amounts)				
Net sales	\$2,474	2,161	2,066	2,917	2,113
Cost of sales and operating expenses	\$1,735	1,378	1,416	1,776	1,604
Depreciation and depletion	\$ 265	255	263	265	248
Selling, general and administrative	\$ 169	136	111	105	99
Asset impairment charges	\$	2,415			
Interest expense	\$ 44	50	56	83	73
Income and mining taxes	\$ (49)	(639)	(85)	225	25
Earnings (loss) from continuing operations	\$ 137	(1,482)	304	399	16
Earnings (loss) from discontinued operations	\$				(5)
Net earnings (loss)	\$ 137	(1,482)	304	399	11
Preferred dividends	\$ (6)	(26)	(26)	(26)	(26)
Accretion of convertible debt	\$ (7)	(4)	(3)		
Premium on redemption of Preferred Shares	\$ (15)				
Net earnings (loss) applicable to common shares	\$ 109	(1,512)	275	373	(15)
Net earnings (loss) per common share basic <sup>(2)</sup>	\$ 0.59	(8.27)	1.51	2.06	(0.08)
Common shares outstanding (weighted average, in millions)	185	183	182	182	176
Total assets	\$9,006	8,577	9,630	9,726	9,618
Long-term debt	\$1,409	1,546	759	952	1,154
Convertible debt	\$ 606	238	231		
Preferred shares	\$	472	472	472	471
Class VBN shares	\$				753

(1) Certain information for the year 1999 has been restated to reflect the retroactive application of the asset and liability method to calculate deferred income and mining taxes (see Note 2 to the Company's 2001 financial statements).

(2) Net earnings (loss) per common share is calculated by dividing net earnings (loss) applicable to Common Shares by the weighted-average number of Common Shares issued and outstanding for the relevant period.

(3) Reference is made to Note 2(c) to the financial statements under Item 8 of this Report.

There are a number of differences between Canadian and United States GAAP. The differences, insofar as they affect the Company's Consolidated Financial Statements, relate to accounting for post-retirement benefits, depreciation and depletion, intangible assets, research and development, exploration, asset impairment, our convertible debt, derivative instruments, investments, income and mining taxes and reporting of comprehensive income. A full discussion of these differences is presented in the Notes to the financial statements under Item 8 of this Report and, in particular, Note 23 to such financial statements.

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The following table reconciles results as reported under Canadian GAAP with those that would have been reported under United States GAAP:

	Year Ended December 31,				
	2003	2002	2001	2000	1999 <sup>(1)</sup>
		(Restated) <sup>(2)</sup>	(Restated) <sup>(2)</sup>		
		(\$ in millions, except per share amounts)			
Earnings (loss) from continuing operations					
Canadian GAAP	\$ 137	\$ (1,482)	\$ 304	\$ 400	\$ 17
Increased post-retirement benefits expense	(37)	(23)	(22)	(22)	
Decreased depreciation and depletion expense	38	13			
Increased intangible assets amortization expense	(2)	(2)			
Increased research and development expense	(5)	(6)	(8)		
Increased exploration expense	(4)	(3)	(7)		
Increased asset impairment charges		(708)			
Increased interest expense	(25)	(9)			