SMEDG TALK AND DISCUSSION
AUGUST 25, 2016
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Introduction to INFO 214.
Existing situation with regards to the legal framework and industry codes.
What does it all mean?
Practical outcomes.
The industry can take some blame.
Solutions?
Over to you.
What Is Info Sheet 214?

- It is a regulatory information sheet issued by ASIC in April 2016.
- It relates to “forward looking statements” in mining and resources, particularly with regards to production targets, forecast financial information and income-based DCF valuations.
KEY POINTS

- The legal requirement that forward looking statements must be based on reasonable grounds.
- An up to date ore reserve establishes reasonable grounds for a forward looking statement.
- The estimation of a mineral resource alone is not sufficient to establish reasonable grounds.
- For reasonable grounds to be established the JORC code mineral resource must be based on a significant level of geological knowledge and confidence, and that ALL JORC code Modifying Factors must be significantly progressed.
- Modifying factors include the “economic” one (JORC Table 1, Section 4), and INFO 2014 looks at what constitutes reasonable grounds if secured project funding is not in place.
- Also briefly looks at “Aspirational Statements” as opposed to “Forward Looking Statements”
LEGAL BASIS

- Corporations Law – Sections 670A(2), 728(2) and 769C and ASIC Act 12BB(1):
  - Statements about future matters must be based on reasonable grounds at the date that the statements are made, or they will be misleading.
  - The test for “reasonable grounds” is objective, and needs to be tested on a case by case basis.
JORC Code 2012

- Clause 20 – any mineral resource is based on the grounds that there are reasonable grounds for eventual economic extraction.

- Clause 38 – A Scoping Study is an order of magnitude technical study of the potential viability of Mineral Resources, and includes appropriate assessments of realistically assumed Modifying Factors with any other relevant operational factors that are necessary to demonstrate at the time of reporting that progress to a Pre-Feasibility Study can be reasonably justified:
  - A Scoping Study must not be used as a basis for Ore Reserves.
  - Scoping Studies may be based on directly gathered project data together with assumptions borrowed from similar deposits or operations to the case envisaged.
  - Can be based on Inferred Resources, but not on a combination of Inferred Resources and an Exploration Target (refer ASX Listing Rules below).
JORC Code 2012

**JORC Table 1 Section 4 Modifying Factors:**
- Mining - (Section 3 – preliminary assessment).
- Metallurgical - (Section 3 – preliminary assessment).
- Environmental - (Section 3 – preliminary assessment).
- Infrastructure.
- Costs – capital and operating.
- Revenue.
- Market assessment.
- Economic.
- Social.
- Other:
  - E.G. Government agreements, other natural hazards, other legal agreements.
Clause 8 – Valuation of Mineral Assets:
- Market Based.
- Income Based.
- Cost Based.

Income based approaches are suitable in some cases for pre-development projects.
ASX Listing Rules 5.15-5.19:

- Relates to the publication of production targets and forecast financial information.
- Production targets cannot be based solely on an exploration target, a combination of inferred mineral resources and exploration targets or historical/foreign estimates (other than “qualifying foreign estimates”).
- A production target based solely on inferred resources is allowed with certain conditions amongst others:
  - Requires a statement of the factors that lead the entity to believe it a reasonable basis for reporting the production targets.
  - A technical report prepared by an independent competent person to support the production target.
ASIC Guidance

- **RG 170.60-RG 170.62 & RG 228.95:**
  - Companies should also disclose underlying assumptions about forward looking statements so that investors have the information they need to understand the basis on what statements have been made.
  - Need to comply with the JORC and/or VALMIN Codes, or may be taken as misleading. However even if disclosure complies with the codes, it will not automatically comply with the legal requirements of ASX Listing Rules 5.15-5.19 and guidance.
It will be much harder for companies to release the results of Scoping Studies when based largely on mineral resources:

- In producing a Scoping Study, most companies will advance the majority of Modifying Factors, however the one key factor that is being looked at by ASIC and the ASX is the “economic” factor.
The “Economic” Modifying Factor:

- ASIC is flexible to some degree on “reasonable grounds” with regards to publishing forward looking statements when secured funding is not in place.
- However this flexibility will not cover the situation of most juniors, who will require project funding at a multiple of their market capitalisation.
- Having a major partner in place does help.
- Hypothetical funding scenarios will generally be considered as misleading.
- Therefore publishing of an NPV of a project’s worth based on a hypothetical funding scenario is an example of a forward looking statement that is likely to be misleading.
A Scoping Study is an important piece of information and also an effective marketing tool often used in fundraising to enable a company to move to a PFS.

Not being able to publish the results has a number of negative outcomes:

- Investors are not fully informed, and thus will be unable to make a prudent investment decision – just saying in a release that the results of the study were positive and warrant moving onto the next stage is not enough – investors need an idea of the potential project value, even if it will possibly be diluted down the track due to funding, JV’s etc.

- The Board and Management become insiders – they are privy to key inside information that possibly is market sensitive, and thus will not be able to buy shares – it is important to keep the interests of company personnel and shareholders aligned.

- A Scoping Study is commonly on that part of the value curve where best returns are made – you won’t get investment if potential investors are kept out of the loop, and thus part of potential value creation is emasculated.
## The Value Curve

**Life Cycle of a Junior Explorer**

<table>
<thead>
<tr>
<th>EXPLORATION STAGE</th>
<th>MINING STAGE</th>
</tr>
</thead>
<tbody>
<tr>
<td>Concept</td>
<td>Pre-Discovery</td>
</tr>
<tr>
<td>~4 to 5 Years</td>
<td>~1 to 2 Years</td>
</tr>
</tbody>
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*Discovery: Speculation Phase Begins*

Source: Phoenix Copper Corp (TSX-V:PHC)
Will lead to potential conflicts in jurisdictional requirements when operating in multiple jurisdictions:

- If dual listed, conflict between the need to disclose the results of a PEA on the TSX and inability to disclose on the ASX.
- Some countries require detailed information when applying for a Mining Right – this can be done at a relatively early stage and commonly the information is released for public comment.

Possibly drive companies away from the ASX to other exchanges, e.g. the TSX, NSX.
Unfortunately the few have helped spoil it for the rest.

Insufficient disclosure, or poor/misleading assumptions:

- Releases of Scoping Study, and even PFS results without underlying assumptions – I have seen some “fine” examples of these.
- Aggressive inputs, including costs and pricing forecasts in studies, particularly on marginal projects.
- Published research indicates that on average capital cost over runs have been around 35-40% over those presented in development studies over recent years – this was surprisingly greater on the larger projects as well as unsurprisingly on the more marginal ones (in the marginal ones the principals are trying to keep costs down in their development case, hence there is more scope for overruns).
- Potential over-runs of ~20-25% in operating costs.
- This has been exacerbated by the mining boom with escalating costs between the time of a study and development.
- Price and exchange rate forecasting is notoriously unreliable, and caution needs to be taken in what prices and values are used.
- Omission of potentially fatal flaws, or factors that may materially affect the project.
Solutions?

- Allow the publication of studies in the recent past form, however with additional disclaimers:
  - E.g. In an unfunded scenario, state that a study is unfunded, and will rely on project funding to proceed, which will result in significant dilution etc.
- Tighter review of studies/releases by ASIC/ASX before public release, however this will require more time, more people and more money.
- Move to a more prescriptive system (e.g. NI43-101).
- Or just move?
- Any others?
OVER TO YOU...