

AMERICAN INSTITUTE OF MINERALS APPRAISERS

NEWSLETTER

January 2006

Vol.8, No. 1

IN THIS ISSUE

Candidates For AIMA Offices

Annual Meeting

Annual Dues

From The Work Files of the 2005 Ethics Committee

Continuing Education

SME Valuation Session Schedule

Major Advance in Global Classification Standard for Minerals and Petroleum

Administrative Law, Civil Procedure, Environmental Law, Oil & Gas

Fair Value Measurements Project

Estimation and Reporting of Mineral Resources and Mineral Reserves

Candidates For AIMA Offices

Editors Note: Ballots were mailed December 30th

President

Michael Cartwright

Vice President

Charles Melbye

Treasurer

Robert Frahme

Secretary

John Gustavson

Please return your ballot by January 31, 2006.

2006 Annual Meeting

Donald Warnken, President

Our 2006 Annual Membership Meeting will be held on March 27th at the Holiday Inn Select Hotel, Saint Louis, Missouri.

The meeting will begin at 6:00 pm and be held in a "break room" at the hotel. Arrangements have been made for serving dinner in that room following the meeting. Drinks will also be made available. All AIMA Members planning to attend this

important meeting, please notify your President by e-mail at dongene32@sbcglobal.net. A dinner menu will be made available at a later date for those who plan to attend.

We have an agenda which should be of interest to all. Should you wish to add a subject to the agenda, please advise your President by e-mail

The Holiday Inn Select Hotel is located at 811 N. 9th St.

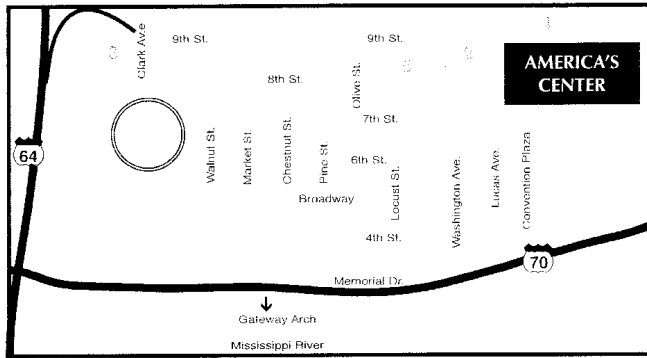
Their telephone and fax numbers are, respectively, 314-421-4000 and 314-436-8932. The hotel is situated on the north side of 9th Street while the America's Center is situated on the south side of 9th Street. Thus, the hotel is situated "across the street" from the SME Annual Meeting/Convention location.

Please advise if you plan to attend. My e-mail address is dongene32@sbcglobal.net.

A vicinity map is presented on page 2.

Continued on page 2

2006 Annual Meeting, *Continued from page 1*



Annual Dues

Annual Dues notices were mailed in conjunction with the Ballot mailing. The dues are \$60 for Full Member and \$30 for Associate and Emeritus (Retired) Members. Please forward your remittance to;

Alan K. Stagg, Treasurer
Stagg Resource Consultants, Inc.
5457 Big Tyler Road
Cross Lanes, WV 25313

From the Work Files of the 2005 Ethics Committee

John B. Gustavson; Ethics Committee Chairman

Many professional societies are currently reorganizing or offering additional certification for their members. Examples are the Society of Mining Engineers and the Metallurgical Society of America. It appears that there is a necessity for a member to subscribe to a Code of Ethics and for the respective society to have the powers to discipline or expel members who violate the Code.

The need for this additional certification is also practical from a business standpoint. It may allow practice by US professionals in places like Canada, where the regulatory agencies require reserve reports to be filed under NI 43-101 (Mining) and NI 51-101 (Oil and Gas). Under these instruments those foreign professionals who are certified by certain accepted societies may file reports with the provisional securities and exchange commissions. State-registered professional engineers from certain states in the US are also accepted.

As a consequence, we are observing a flurry of certification offers by societies, who then again hope to have their certified members added to the list of Qualified Persons. It appears to be a key in all of this that a society must have *teeth* to take action, if a complaint against is filed against one of its members.

AIMA has always had such teeth and this report will show how. The AIMA has had its Code of Ethics for many years and also a well-documented procedure for handling complaints. The procedure was established to provide both a forceful as well as a discreet and fair means of investigating alleged misconduct. The investigation must be sensitive to the rights of the accused individuals, because disgruntled business partners of victims of bad deals frequently misuse complaints of alleged misconduct against their adversaries.

The AIMA manages its ethics complaint investigation through its appointed chairman of the Ethics Committee. I have served in that function for couple of years, and before that in a similar role in a section of the American Institute of Professional Geologists. All complaints are handled with utmost care and confidentiality. Records are carefully kept and the AIMA President is kept advised of all activities.

In the 2004-2005 period a number of cases were investigated, and so none have led to disciplinary action against a member. In the following a couple of these cases will be described and member responses are invited. It is hoped that our membership will appreciate some of the difficulties involved in this necessary function of a certifying institute; also, comments and suggestions may sharpen the teeth, which the AIMA must continue to show in order to live up to our purposes, namely

1. the advancement of the appraisal profession in general and that of the appraisal of minerals in particular,
2. the certification of the qualifications of individual member appraisers to the public, and
3. the promotion of high standards of ethical conduct amongst its members and within the profession of appraisal of minerals.

Case A. A matter was brought to the attention of the AIMA Ethics Committee in which a property owner held a 2-acre marble deposit. The owner had it appraised by a member (name withheld) of the American Society of Appraisers, a person who also was a certified professional geologists by the AIPG. The appraisal methodology was grossly flawed, if not fraudulent. The appraiser (who was not certified by the AIMA) ignored standard mining procedures and simply calculated the volume of a roughly vertical cylinder of marble, divided it up into slabs of floor tile and multiplied that quantity by the going retail price of a finished floor tile.

The result was a billion-dollar level, but erroneous and misleading value. The owner wanted to obtain a bank loan with his marble as collateral, but the potential lender prudently required an additional appraisal. Several AIMA members were approached but turned down the task and informed the Ethics Committee.

Continued on page 3

From The Work Files of the 2005 Ethic Committee, *Continued from page 2*

In the meantime, and having learned of the misleading appraisal the AIPG (of which the appraiser was a certified member) started its own ethics violation investigation. Upon initial contacts and after learning that he was under investigation the appraiser withdrew his membership from the AIPG and removed his AIPG insignia from his web site. The AIPG then dropped its investigation.

However, the AIMA now faced a dilemma:

Recall, that the AIMA had been made aware that a practitioner of minerals appraisals was offering services to the public, but that he was not a member of the AIMA. Therefore, the usual disciplinary actions of the AIMA could not be applied. There was no AIMA disciplinary action, which could take the form of private admonition, public reprimand, suspension of membership, or termination. The preamble to our Ethics Code states: “The Code of Ethics applies to all professional activities of **Members** [*emphasis added*] wherever and whenever they occur.”

The AIMA Ethics Committee is instead faced with the question: Do we have a duty to *police* the field of appraisals by filing a complaint with the ASA (American Society of Appraisers) by whom the above-mentioned appraiser is accredited? Must we do this in order to live up to our purpose paragraph (see the last line of Item 3 above, namely “the promotion of high standards of ethical conduct... within the profession of appraisal of minerals”)? Is promotion synonymous with policing?

The AIMA is fortunate that Michael Cartwright, our President-Elect for 2006 is a long-term ASA member, and it will be on his watch that is question will be answered. Your input is invited.

Case B. Sometimes the investigation of alleged breaches of the AIMA Code of Ethics must be temporarily suspended. This happens in cases when the AIMA has no means of understanding or predicting the outcome of an ongoing court action. A complaint was filed with the President of the AIMA, who instructed the Ethics Committee to follow the AIMA procedures. Upon initial review the investigation of the case had to be suspended.

An AIMA member or rather an employee or agent of a member had been collecting mineral samples without a geologist’s license in one of the states where such are required. We will only comment briefly on the ease with which competent geologists can obtain temporary licenses or other legal instruments or local assistance to avoid violating a state’s licensing laws. It is plain dumb not to do so.

However, in the present case the mineral samples or the analyses thereof were used as evidence in a court case. A judgment was handed down, but the case went into appeal.

One of the parties in the court action filed a complaint with the AIMA against the member for violation of the Code of Ethics. The alleged violation is not subject of this article, but rather the necessity to temporarily suspend an investigation, if such should be justified.

1. Dismiss the Complaint in whole or in part, for lack of evidence, insufficient grounds, or other good cause including availability of legal recourse, and so advise the Complainant.
2. Request the Complainant to provide, within a specified amount of time, further information or documentation, or a more specific statement as to the nature of the Complaint.
3. Appoint an investigator to determine whether there are grounds to proceed in the matter and to prepare a report for the Ethics Committee Chairman.
 - a. The investigator shall not be a member of the Executive Committee.
 - b. In the event that an investigation is commenced, the Ethics Committee Chairman shall notify the Respondent of the fact of the investigation, unless to give such notice would severely and irreparably impair the investigation.
 - c. The investigator’s report shall include the investigator’s findings and any further documentary evidence developed or uncovered by the investigation.

Here it was found that there was an ongoing court case, which may include or lead to *the availability of adequate legal recourse* for the complaining party. In other words, the final outcome of the current appeal, maybe followed by civil action against the Respondent (the employer of the unlicensed sampler) must first be completed.

This may by some members be seen as lack of teeth of the Ethics Committee, but in contrast it protects the public and the AIMA certified appraisers against the misuse of our Ethics Complaints Procedures as a litigation ploy.

Your thoughts on the similarities or differences between unethical behavior and violation of ordinances are also invited.

John B. Gustavson
Ethics Committee Chairman

Continuing Education

For those Members who are wondering where, when and how to fulfill their *Continuing Education* needs, **Robert Frahme** has provided the following schedule of up-coming Year 2006 appraisal classes. These classes are offered by the St. Louis Chapter of the Appraisal Institute.

Continued on page 4

Continuing Education, Continued from page 3

5757 Central Avenue
 Suite D
 Boulder, CO 80301
 e-mail: joegus2711@aol.com

<u>Name of Course</u>	<u>Date</u>	<u>Location</u>
Appraisal Principles	1/23-1/26	(1)
Advanced Income Capitalization	1/30-2/4	(1)
Appraisal Procedures	2/13-2/16	(1)
USPAP (15 hour update)	3/6-3/7	(2)
USPAP (7 hour update)	3/13	(3)
USPAP (7 hour update)	4/3	(2)
Residential Market Analysis		
And Highest & Best Use	4/20-4/21	(4)
Scope of Work	5/8	(2)
Real Estate Finance, Value & Investment Performance	5/15	(2)
Understanding & Testing		
DCF Valuation Models	6/5 (morning)	(3)
Analyzing Distressed Real Estate	6/5 (afternoon)	(3)
Litigation Skills for the Appraiser: An Overview	6/19	(2)
USPAP (7 hour update)	6/23	(4)
Appraisal Principles	9/18-9/21	(1)
Appraisal Procedures	10/23-10/26	(1)
Apartment Appraisals: Concepts & Applications	11/2-11/3	(3)
Analyzing Operating Expenses	12/1	(3)

Abstract

Geothermal rights were owned by government and leased. Surface rights were severed to subdivision developer. An agreement between developer and lessee left a small strip for exploration drilling. A freeway right-of-way bisected that strip. Compensation to the lessees must be appraised, namely value BEFORE minus value AFTER. Income to the property is rental payments, only, since development potential is low. Appraiser found transactions involving geothermal rights, including leases and sales.

A DCF model was constructed by projecting income from hypothetical rental payments. This established the fee mineral owner's geothermal rights (Before Value). The leasehold was estimated based on ratios in comparable oil industry exploration stages. In the After case, the value was impaired proportionately to the remaining percentage of original access. Any geothermal resources were still accessible, but only 65 percent of an already narrow strip in moderately difficult terrain. Thus the After FMV was found. The diminution is the difference between Before and After values.

Presentation 2: Appraisal For Mineral Leases on Arizona State Trust Land.

Time: 2:20 p.m.

Author: Richard Ahem
 Arizona State Land Department
 1616 West Adams
 Phoenix, AZ 85007
 e-mail: rahem@land.az.gov

Abstract:

Arizona State Land Department mineral leasing procedures require the Department to set rents, fix royalty rates and, in some instances, establish the fair market price by appraisal methodologies. The annual rent is determined by the Land Department based on an appraisal of the surface estate. The royalty rate is based on an appraisal of the states' interest as a lessor in the minerals produced. If the gross mineral value is not available from published prices, the gross market value of the minerals produced will be based on an appraisal that estimates the fair market price of the mineral.

Appraisal estimations of royalty rates and market values may be complicated in the case of industrial minerals sold in bulk such as limestone, gypsum, or clay because comparable royalty rates and market prices are not generally available. Commonly, the minerals being mined are not sold in the market place but are used internally by the lessees. Information on actual royalties paid is frequently more

Continued on page 5

All classes will be held in St. Louis, MO. The location of each class is as follows; (1) Best Western Kirkwood Inn, (2) University of Missouri-St. Louis, (3) University of Phoenix – Riverport Campus, (4) Webster Groves Recreation Complex.

Class confirmation, cost and other information can be obtained by accessing their web site at www.stlappraisalinstitute.com.

SME Valuation Session Schedule

Alan K. Stagg

The schedule for the valuation session at the 2006 SME Meeting is as follows.

Session Title: *Appraising Mineral Interests-Keeping Abreast in a Changing World.*

Session Chair: Alan K. Stagg
 Stagg Resource Consultants, Inc.
 P.O. Box 7028
 Cross Lanes, WV 25356

Presentation 1: Appraisal of a Geothermal Mineral Property Under the Unit Rule.

Time: 2:00 p.m.

Author: John Gustavson
 Gustavson Associates, Inc

SME Valuation Session Schedule, *Continued* from page 4

available than data on the royalty rates and market prices that are required for the appraisal. In these instances, it may be necessary to rely on indirect approaches to estimate the appropriate rate and value. One approach would be to back into the required royalty rate and gross mineral value from available data on royalty payments. The cost to purchase the minerals from other sources or of using alternative materials may be used in estimating market value. Operating costs can also be used as a basis for estimating market value in some instances.

The lack of data on comparable royalty rates and mineral values make completing these appraisal assignments a challenging task.

Presentation 3: Selecting the Discount Rate – Whose Interest is Being Valued?

Time: 2:40 p.m.

Author: Craig R. Wood
Stagg Resource Consultants, Inc.
P.O. Box 7028
Cross Lanes, WV 25356
e-mail: cwood@staggconsultants.com

Abstract:

A variety of methodologies exist for selecting a discount rate in appraising mineral interests, with there being no consensus regarding the appropriate one(s) to use. Notwithstanding differences in opinion regarding the methodology, it is important to understand that the interest being appraised is of the primary importance in selecting the methodology or, ideally, the methodologies used. This paper examines two of the most common alternative mineral interests to be value—value from the standpoint of a passive investor and value from the standpoint of the operator of the mineral estate—and discusses appropriate methodologies to be used in selecting discount rates for each.

Presentation 4: Assuring Consistency in Nominal and Constant Dollar Models.

Time: 3:00 p.m.

Author: Robert Frahme
Gustavson Associates, Inc
5757 Central Avenue
Suite D
Boulder, CO 80301
e-mail: rfrahme@gustavson.com

Abstract:

In times of low inflation, appraisers tend to become lax about whether their DCF analyses are in constant or nominal dollars.

We have not experienced serious inflation since the early 1980s so there is an entire generation of appraisers who may have never handled it properly. Even in times of low inflation, appraisers need to know whether they are working in constant or nominal dollars and working in constant dollars does not exonerate the appraiser from a forecast of inflation. Inflation is returning to the economy and this presentation offers a systematic way of handling it in DCF models.

Presentation 5: Interactive Discussion on Discount Rate Selection.

Time: 3:20 p.m.

Moderator: Alan K. Stagg
Session Chair

Major Advance in Global Classification Standards for Minerals and Petroleum

By Trevor R. Ellis, CMA No. 1994-1
Ellis International Services, Inc.

The following is extracted from a report by the author to the International Valuation Standards Committee (IVSC), with minor modifications for the purpose of publication. See AIMA Newsletter, Dec. 2004, for previous coverage of this topic.

I again represented the IVSC at the annual session of the Ad Hoc Group of Experts on Harmonization of Fossil Energy and Mineral Resources Terminology, a body organized by the United Nations Economic Commission for Europe (UNECE). This second session was held at the United Nations' Geneva offices on 9-11 November 2005. The meeting achieved an important agreement for advancement towards uniform global standards for the classification of minerals and petroleum reserves and resources.

The primary focus of the meeting was discussion of the possibility of enhancing the United Nations Framework Classification for Energy and Mineral Resources (UNFC) for implementation globally as the classification standard for use in financial reports under the International Financial Reporting Standards (IFRSs). Presently there are between 100 and 200 mineral and petroleum resource classification (or definition) systems throughout the world — a similar number to what there are countries. Financial reports by a minerals or petroleum company that reports to more than one jurisdiction can be required to comply with differing classification systems and rules, dependent on the jurisdictions in which the reports are being filed. The classification systems used in financial filings may differ from that being used internally by the company geologists and engineers. These may also differ from the classification system required for use in filings with the host government's natural resources department, which system is likely used for compiling and monitoring the state's natural resource base. These inconsistencies result in burdensome costs, plentiful confusion, significant errors, abuse, and sometimes large financial losses and penalties. Substantial

Continued on page 6

Major Advance in Global Classification Standards for Minerals and Petroleum,

Continued from page 5

differences also exist between the minerals and petroleum industries in the definitions and structures of the most commonly used classification systems, adding to the confusion.

There were approximately 50 participants in the meeting. These included representatives from major petroleum companies, major accounting firms, many government agencies, intergovernmental organizations (OPEC and the Nuclear Energy Agency), NGO's (IVSC and the World Energy Council), the Society of Petroleum Engineers (SPE), and the mining industry's Combined Reserves International Reporting Standards Committee (CRIRSCO).

The meeting management invited me to develop one of the few formal presentations given in the meeting. The title of my 20 minute presentation is *Resource Codification, Valuation Standards, and Sustainable Development*. It shows the benefits of resource classification and valuation standards to the sustainable minerals and energy resource development goals of the UN. It also provides a global perspective to the relationship of the UNFC, International Valuation Standards (IVS), and IFRSs. I concluded my presentation with a recommendation that CRIRSCO, SPE and related bodies, work with the UNECE expert group to enhance the UNFC with the best of their respective classification standards and guidelines. This should ensure that the IASB selects the UNFC as the minerals and petroleum classification standard referenced by the replacement IFRS 6 (extractive activities standard) that will result from the IASB's current phase II extractive activities project.

My presentation was well received. Michael Lynch-Bell of Ernst & Young fortified my concluding recommendation with a strong supporting commentary. The meeting unanimously agreed to pursue the enhancement of the UNFC into a strong global "code." The representatives of CRIRSCO and SPE agreed that their respective bodies would create small minerals and petroleum expert teams to carry out the project on a timely schedule.

The UNFC has been evolving since 1992, with early versions focusing on solid minerals, particularly coal. It has been developed through consensus input from western and eastern countries, and from developed and emerging market countries. In 1997, the United Nations Economic and Social Council (ECOSOC) passed a resolution recommending that all UN member countries apply the UNFC to their coal and other solid minerals sectors. In recent years the UNFC has been enhanced by the inclusion of petroleum classification. In July 2004, ECOSOC member states unanimously passed Resolution 2004/233, which recommends that all UN members encourage application of the UNFC worldwide. The contribution of some of our IVSC Extractive Industries Task Force members [Trevor Ellis (AIMA), Donald Warnken

(AIMA), and William Roscoe] was recognized within the approved UNFC document.

Due to this progress, the UNFC is the only widely applied classification system incorporating both minerals and petroleum classification. It is rather unique in that it has been designed for use in market and non-market economies. It is also designed for use at the individual deposit level by companies, through to use in national databases for known and potential resource monitoring. Being based on an alpha-numeric code system, its application is largely independent of language. To date though, it has not been approved for corporate financial filings in the western world. The IVS standard for valuations in the extractive industries references the UNFC, the CRIRSCO classification for minerals, and the SPE/WPC/AAPG classification for petroleum. The CRIRSCO classification is used in standards for corporate reporting to the major western world stock exchanges outside the USA, and is designed only for corporate use in market economic settings. The SPE/WPC/AAPG classification has similar application for reporting outside the USA, and is designed for national resource database use. The U.S. SEC maintains its own constrained reserve definitions and reporting requirements in its regulations for minerals and petroleum companies. Testing of the UNFC has demonstrated better than modest compatibility with the CRIRSCO, SPE/WPC/AAPG, and Russian classifications, which will aid transition to the UNFC.

During the first session of the UNECE's Ad Hoc Group of Experts, in November 2004, some influential countries expressed serious disagreements with many of the recommendations put forth. Therefore, I did not expect the substantial accomplishments of this second meeting. In particular, I was pleasantly surprised by the strong support and assistance offered by the CRIRSCO representatives for enhancing the minerals portion of the UNFC classification.

The objectives agreed upon in the Terms of Reference at the close of this session provide a major advance in the development of global standards for the minerals and petroleum industries. A governance and financing structure for this UNFC enhancement project was also drafted.

Documents and presentations from the meeting are available at www.unece.org/ie/se/reserves.html.

Administrative Law, Civil Procedure, Environmental Law, Oil & Gas

Michael Cartwright has furnished the following court case for our (AIMA Members) information.

Texas Independent Producers & Royalty Owners Association v Environmental Protection Agency, No. 03-3277 (7th Cir. January 27, 2006)

Petition for review brought by organizations representing individuals in the oil and gas industries involving aspects of a
Continued on page 7

**Administrative Law, Civil Procedure,
Environmental Law, Oil & Gas, *Continued***
from page 6

general permit issued by an agency regarding storm water discharge is dismissed for lack of standing due to an exemption contained in the Energy Policy Act.

To read the full text opinion, go to:

<http://caselaw.lp.findlaw.com/data2/circ/7th/033277p.pdf>

United States v McPhilomy, 270 F. 3d 1302 (10th Cir. 2001) – government’s geologist re quantity, quality, and value of stone

Defendants remove several tons of stone from government community pit without proper permits and are charged with theft. Defendants object to testimony from government’s geologist re quality, quantity, and value of stone. **Admissibility affirmed.** Geologist inspected stone, had considerable training and experience, used same methods he utilized when performing work for Bureau of Land Management (BLM). More extensively and costly tests might have been preferable, but geologist’s work was sufficiently reliable to support his opinion on quality of stone. He also employed common method for estimating tonnage—i.e., he estimated volume of stone and calculated weight based on data provided for that purpose in BLM publication. And geologist could properly estimate retail value by inquiring at other stone yards about retail prices of comparable stone.

From <http://www.daubertontheweb.com/geologist.htm>

Fair Value Measurements Project

Info furnished by Michael Cartwright

The Financial Accounting Standards Board (FASB) is expected to issue its *Fair Value Measurements* Statement by the end of 2005. the significance of this statement is that it will establish a framework for applying the fair measurement objective under the generally accepted accounting principals.

Additional information can be obtained from:

<http://appraisalinstitute.org/resources/vfr/infocus/default.asp>.

**Estimation and Reporting of Mineral
Resources and Mineral Reserves**

Info furnished by Michael Cartwright

The Society of Mining Engineers (SME) has submitted a set of recommendations to the Securities Exchange Commission (SEC) concerning the public reporting of reserves and resources. These recommendations can be downloaded in their entirety from the SME website at <http://books.smenet.org/sec>.

The NEWSLETTER is published by the American Institute of Mineral Appraisers, 5757 Central Avenue, Suite D, Boulder, CO 80301
Phone: (303) 443- 2209; Fax (303) 443-3156
E-Mail: gustavson@gustavson.com

Editor: Donald Warnken
E-Mail: Dongene32@sbcglobal.net
