AMERICAN INSTITUTE OF MINERALS APPRAISERS

NEWSLETTER

February 2001 Vol. 5, No. 2

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2001 Annual Membership Meeting

Trevor Ellis, AIMA, President

Our 2001 Annual Membership Meeting will be held in the early evening of Monday, February 26, 2001, at the Wynkoop Brewpub, 1634 18th St (Wynkoop and 18th St), in lower downtown Denver, Colorado. The Meeting will be held in conjunction with the SME Annual Convention, February 26-28, which itself is held in nearby Denver Convention Center.

The Wynkoop Brewpub was the location of our First Annual Membership Meeting in 1999. The reception begins at 4:15 PM. The business meeting will be from 4:45 – 6:15 P.M. Thereafter, we will have dinner.

These schedules have been selected to fit with any SME commitments that our AIMA members may have. We would like as many members as possible to stay and continue a lively and informal discussion over dinner.

To get to the Brewpub from the Convention Center, walk north on California or Stout Street to the 16th -Street Mall, and take the west-bound Mall Shuttle to Wynkoop Street. Then walk north to 18th Street. There is no entrance fee for our meeting, but drinks and food are the individual's responsibility. Guests are welcome. For questions or to submit agenda items, contact Trevor Ellis at 1-303-399-4361, ellis@minevaluation.com.

Should the AIMA Have a New Member Class?

We have regrettably received two requests for resignation of AIMA membership from distinguished members. There is no doubt that our recent dues increase is felt strongly by retirees. Any solution for these senior members who still might want to contribute to the AIMA even while not practicing? Let us discuss at the Annual Meeting. *John Gustavson, Secretary*

IASC Reviews Extractive Industry Valuation Issues

Trevor Ellis, AIMA, President

In November 2000, the International Accounting Standards Committee (IASC) released its Extractive Industries Issues Paper. It contains tentative recommendations and a comprehensive questionnaire for responses. The International Valuation Standards Committee (IVSC) is the little sister of IASC, with a significant level of cooperation occurring between the two (see *International Valuation Standards 2000*, AIMA Newsletter, July 2000, p. 3).

The Steering Committee on Extractive Industries will likely develop a set of international accounting standards for financial reporting by the extractive industry, to cover all minerals, including petroleum. Based on past practice, much of the valuation portion of the standards will likely be directly collated into the International Valuation Standards.

At the IVSC's request, your President will be working with our Australian, Canadian and UK counterparts and the IVSC in the hope of drafting a coordinated response document to submit to IASC. IVSC has also indicated that once the IASC extractive industry standards are released, it wants me to assist them in developing a set of guidance notes for extractive industry valuation for inclusion in the International Valuation Standards.

The end result of the combination of the International Accounting Standards and International Valuation Standards can be expected to have a substantial impact on minerals industry appraisals internationally, and eventually domestically. The result has the potential to constrain or expand our basis and frequency of minerals appraisals for company accounting and financial reporting purposes. For a benchmark, we only need to look at the difficulties that the Securities Exchange Commission's restrictive Industry Guide

cont'd below

AIMA MEMBERSHIP NUMBERING SYSTEM

Upon the decision by the majority of the membership at our last Annual Meeting, each member has been assigned a "Dash Number", which may be used as a membership number. Thus, the **year of certification** followed by the Dash Number (assigned chronologically during that year) becomes a member's number.

There is no requirement at this time that a member must use the Dash Number. A member can sign off on an appraisal report in at least four ways:

Joe Doakes, Certified Minerals Appraiser
Joe Doakes, Certified Minerals Appraiser, 1997
Joe Doakes, Certified Minerals Appraiser, 1997-5
Or even just simply:
Joe Doakes

New certificates will be issued upon request and upon payment of $25.00 to the Institute for the graphics, handling and shipping costs. Please, note that any such new certificate will only sport the signatures of the current officers and not the (now historic) John Henry's of the original officers.

New seals and stamps will also be issued upon request at the regular prices.

Member Name	Member Number
Adams, Cameron	1999-1
Albert, Mitchell E.	1995-4
Alderman, Jr., Sidney S.	1993-6
Barby, Brad G.	1993-8
Bate, Richard L.	1999-2
Briggs, Arthur R.	1995-1
Cartwright, Michael R.	1992-3
Crabtree, Albert L.	1994-3
Ellis, Trevor R.	1994-1
Fly, J. Paul	1993-1
Garb, Forest A.	1993-2
Gregg, Lawrence T.	1996-2
Guarnera, Bernard J.	1995-3
Gustavson, John B.	1992-1
Hart, Robert N.	1999-5
Henderson, Jr., Thomas B.	1995-2
Hoover, Earl G.	1993-3
Jennings, William F.	1999-6
Kern, Jeffrey R.	1999-3
Lawrence, Ross D.	1999-4
Lilley, Wesley W.	1996-1
Limb, Joseph Stuart	1993-9
Melbye, Charles E.	1993-4
Moritz, Edwin C.	1993-7
Pickering, Jr., Sam M.	1998-1
Rothermel, R.V.	1993-10
Slothower, Ben H.	1993-5
Stewart, James M.	1994-2
Warnken, Donald E.	1992-2
Wyman, Richard V.	1993-11

IASC Reviews Extractive Industry Valuation Issues
(cont'd from above)

7, and its predecessor Form S-18 from 1981, has caused the U.S. mining industry and some of us minerals appraisers by restricting public reporting of quantitative estimates and value of mineral deposits to only proven and probable reserves. The International Accounting Standards have achieved a high level of acceptance around the world in recent years, and there is a lot of pressure on the U.S. from both inside and outside, to fall in line in accepting its principals.

A few of key items relevant to us from the Steering Committee's tentative recommendations are by item number:

> 5. *The primary financial statements of an extractive industries enterprise should be based on historical costs, not on estimated reserve values.*

6. *Information about reserve quantities and values, and changes in them, should be disclosed as supplemental information*.

33. *Disclose proved and probable reserves separately, and within proved disclose proved developed and proved undeveloped reserves separately*.

The committee is seeking input on a lengthy list of Basic Issues. Two of particular relevance to us are:

Basic Issues 14.4 - Disclosure of mineral resources: *Should quantities of estimated mineral 'resources' be disclosed, and if so what categories of resources should be disclosed?*

Basic Issue 15.2 - Value of properties held for exploration: *Should the value of mineral properties held for exploration be disclosed?* Note that here they are only considering historical or book value, not current value.

A couple of initial observations that I have made from browsing through the Summary document are:

The issue of whether to allow disclosure of *possible reserves* as well as *proved* and *probable* is still alive (sub-issue 14.3.3). This is surprising and disconcerting to see, given that in 1997 the international Council of Mining and Metallurgical Institutions excluded *possible reserves* from the internationally accepted reserve-resource definitions.

There is no hint of a thought of providing for disclosure of the current value of resources or exploration properties.

The major international accounting houses of KPMG and PricewaterhouseCoopers have had substantial influence in the development of the Issues document. The U.S. SEC has strongly lobbied to restrict reporting of the value of mineral deposits to only *proved and probable reserves* and that being only on an historical cost basis. Its basis for this is that there is no common standard for valuation of mineral properties within the extractive industries. We must take note and continue to work towards developing and applying an internationally accepted set of standards for minerals appraisals.

Comments are due to IASC by June 30. A comprehensive 44 page summary of the Issues document in *pdf* format can be downloaded from the IASC website, *iasc.org.uk* by going to *current projects*. For anyone who may be interested in ordering a copy of the entire Issues document, the price is approximately US$51. If you are unable to work out how to order it on-line, I can provide you with the order form.

I consider the outcome of this study to be very important to our future. Please provide any comments you may have to me by phone 303-399-4361 or e-mail ellis@minevaluation.com by February 24 so that we can discuss them at the AIMA and SME Annual Meetings. Feel free to also provide input as an individual directly to the steering committee.

A similar Issues Paper is due out at the end of January 2001 from IASC on Present Value. We should also take a strong interest in that one.

Valuation Papers, SME 2001 Annual Meeting Denver, Colorado, Feb 26-28, 2001

The 2001 convention of the Society of Mining, Metallurgy and Exploration will have two sessions of papers devoted to appraisals in the minerals industry. The sessions will be in the morning and afternoon of Tuesday, February 27, this being the day after the AIMA Annual Meeting.

Trevor Ellis, AIMA President, has organized and is chairing the sessions for the second year in succession. Of the 13 papers, five are by AIMA members and a sixth has a member as coauthor.

The morning session is titled, **Valuation Issues I: Case Studies**. The following are the six papers scheduled for this session, with their abstracts.

Selection of the Appropriate Discount Rate for Valuing a Mining Property, Bernard J. Guarnera, AIMA Member, President & CEO, Behre Dolbear & Company, Inc., Denver, CO.

Selection methodologies for discount rates vary. The paper will discuss a method successfully used in multiple valuation exercises for mineral properties.

Comparable Sales in the Market: Do They Really Exist? James J. Hodos, Onstream Resource Managers, Inc., Carson City, NV.

When discussing the methods of determining the fair market value of a mining property, it is continually heard that "every mining property is unique so there can be no comparables" or other such similar refrain. The truth of the matter is that the "nay-sayers" either do not understand what a “comparable sale” really is or have not invested the energy into examining the market. Comparable sales can - and do - exist for many of the mining properties being appraised and this method should be embraced and employed by mineral appraisers and industry purchasers and not dismissed quite so cavalierly.

Valuation of Utility Assets under Deregulation, Mary B. Cain, Masters Degree Candidate, Division of Resource Management, West Virginia University, Morgantown, WV; Jeffrey R. Kern, AIMA Member, Resource Technologies Corp., State College, PA; Thomas F. Torries, Ph.D., Professor, Division of Resource Management, West Virginia University.

Until recently, the generation of electricity was regulated in all states and the value of generation assets in a regulatory environment for ad valorem taxation were based largely on the book value of the plant plus the rate of return on capital allowed by the state regulatory agency.

This method of appraising utility generation assets is inappropriate in a competitive environment because past capital expenditures are not relevant in a competitive environment. However, it is not clear what valuation methods are appropriate after restructuring. This paper identifies key problems and advantages of other appraisal methodologies and makes comments on various valuation and taxation methods.

Mineral Appraisal Issues in Court Testimony, J. Stuart Limb, AIMA Member, CMC Inc., Scottsdale, AZ.

The presentation is based on actual issues which arose during the presentation, preparation, and defense of mineral appraisal values involving litigation and actual or possible testimony in court. Specific legal issues and restraints should be discussed with a client’s attorney at the commencement of the appraisal process.

Comparison of projections, made as of the appraisal date, with subsequent, actual, results interfacing with other experts. Full narrative appraisal, limited appraisal, restricted appraisal, or summary appraisal?

Secret Factors, Which Create Value Premiums, Douglas B. Silver, Balfour Holdings, Inc., Englewood, CO.

Gold is one of the most liquid commodities. Anyone can pick up the telephone and buy or sell it. There are no special rules or privileges required to be a buyer and refineries insure that all gold coins and bars have standard compositions. Therefore, it would seem logical then that an ounce is an ounce, regardless of its source.

It also stands to reason that no premiums should be paid in the gold mining acquisition markets because no one's ounces are of better quality than anyone else’s. Reality tells a different story. Certain company’s ounces are worth more than others, even when one completely removes hedging issues and the cost of production. Why this occurs is one of the great mysteries of the world, until now.

This presentation will explain how one can increase the value of their ounces (from the acquisition perspective) through the presentation of case histories and statistics, which highlight these fascinating phenomena.

Ripe or Rotten? What Companies are Paying for Industrial Mineral Acquisitions, John B Lizak, Mineral Valuation & Capital, Inc., Northampton, PA.

Mergers and acquisitions have been occurring at a rapid pace in the industrial minerals and construction materials industries. This paper is an outgrowth of direct involvement in over 175 of these acquisition transactions.

Acquisition prices will be compared to the values obtained via traditional corporate valuation techniques. The findings will demonstrate that traditional corporate valuation techniques often do not lead to an appropriate valuation of an industrial mineral or construction material company.

The findings will also enable company owners, buyers, and investment intermediaries to update their corporate valuations in light of the heightened interest in industrial mineral and construction material acquisitions.

The afternoon session is titled: **Valuation Issues II: Standards and Regulations**. The following are the seven papers scheduled for this session, with their abstracts.

Standards of Value and Appraisal Techniques - Making the Appropriate Selection, Alan K. Stagg, President & Principal Economic Geologist, Stagg Engineering Services, Inc., Cross Lanes, WV.

The appraisal of mineral properties, operations, and companies involves considerably more than a basic understanding of engineering economy and discounted cash flow analysis. A number of standards of value exist, each of which is appropriate in specific situations.
Similarly, a number of techniques exist by which some standards of value can be applied. The selection of the

appropriate standard of value and appraisal technique(s) is critical in the completion of meaningful appraisal, and it is the appraiser's responsibility to make the appropriate selection based on the purpose and intended use of the appraisal.

In this presentation, standards of value and appraisal techniques are reviewed and criteria governing their selection are identified. A number of representative case studies are provided by way of illustration and problems involving the application of each standard and technique are discussed.

Standards for Temporary Takings and Fair Market Rental Value, John B. Gustavson, AIMA Secretary, Gustavson Associates, Inc., Boulder, CO.

Temporary takings differ from permanent takings as the name implies. Likewise, an appraiser may in such cases be faced with having to estimate a fair market rental value instead of the conventional fair market value. The author first outlines several landmark events from about fifty years ago such as the *Kimball Laundry* and *General Motors* cases. At that time the real estate appraisal profession came to grips with temporary takings and applying a fair market rental value.

The concept can also be applied to mineral property valuation, but with several important adjustments. The author describes the lease income approach, the "parked capital" method and the controversial "Delta-DCF" approach.

Under the lease income approach a research of the rental income of comparable properties can derive the fair market rental value. Such income includes advance minimum royalties, option payments, bonuses, and acreage rentals. The "parked capital" method is based on considering the property as a capital asset, the use of which is temporarily tied up. Therefore, a simple multiplication of the property value by an appropriate interest over the amount of time provides a measure of the fair market rental value.

The stage of property development is important. The estimating of rental value must be separated into two specific phases. The first phase is the exploration and evaluation phase during which the mineral rights owner allows an operator to explore and evaluate the property and its potential market. The second phase is the production phase where mineral production is established on a given property.

During the first phase practically no minerals are removed from the property. The minerals are still in the ground even when this phase ends. This initial period will terminate with the expiration of the contract or with the onset of the second phase at the operator's option, the production phase. Any temporary taking during this first period can therefore be handled for the mineral rights owner in complete parallel with a mine operator's rental of the property.

During the production phase the activity involves removal and sale of minerals. Therefore, the mineral deposit is being depleted. For allowing the mine operator to remove and sell the owner's minerals the mineral rights owner receives a consideration. These considerations include royalty payments (for oil and gas and industrial mineral properties), a net smelter return (for precious and base metal properties), a net profits interest or similar considerations.

When a property is at the exploration or evaluation stage, the fair market rental value must be estimated as shown first above, namely on basis of advanced royalties, option payments, cash bonuses and delay rentals and not on basis of lost royalty income. However, if the production phase is interrupted, then the mineral rights owner suffers the loss of royalty income. This may be estimated by analyzing the effect of the delay of royalty income.

Another method is based on considering the property as a capital asset the use of which is temporarily tied up. Even while unused, the "parked" capital still costs the owner money (his cost of capital) during the temporary taking. It is necessary to estimate the value of the asset (its Fair Market Value) as well as the cost of capital (the interest) for the industry sector.

Federal land appraisal standards suggest utilizing an appropriate interest rate on the property value if rental data is lacking. Otherwise, the weighted-average-cost-of-capital is considered as approximating the interest rate for a no-risk (no cash flow risk) delaying the use of capital. It costs the mineral rights owner money to have his capital tied up by the Government. This is also the hurdle rate that companies would seek on any given investment.

Important case histories from the public domain are presented including the *Yuba* gold mining cases. Valuable lessons can be learned from *Yuba*, whether the audience agrees with the court's findings or not. The author discusses the key issue as to whether commodity price changes during the temporary takings period should be considered and, if so, on which basis.
Case histories are then presented including description of approaches and sources of data on "comparable rentals"

in the minerals industry. The case histories include a sand-and-gravel condemnation case and an oil and gas case.

Finally, the author recommends the application of rental-value methodology for appraisal of mineral properties during *transitional* uses. Following again the lead of real estate appraisers such as Eaton (1982) the author describes a valuation of the short-term gold mining use of a residential property.

Development of Canadian Standards and Guidelines for Valuation of Mineral Properties, Keith N. Spence, Co-Chairman, CIM Special Committee on Valuation, Export Development Corporation, Ottawa, Ontario, Canada; William E. Roscoe, PhD, Co-Chairman, CIM Special Committee on Valuation, Roscoe Postle Associates Inc., Toronto, Ontario, Canada.

In the Canadian mining industry, there are at present no comprehensive regulations or standards for valuation of mineral properties. In January 1999, the Mining Standards Task Force of the Toronto Stock Exchange and the Ontario Securities Commission recommended that the Canadian Institute of Mining, Metallurgy and Petroleum (CIM) establish a committee to review and advise on approaches and methods for the valuation of mineral properties.

The CIMVal Committee was established, consisting of experts from the mining industry, consulting, financial and legal communities. It is envisaged that the CIMVal Committee's final report will form the basis for a set of Canadian standards and guidelines for the valuation of mineral properties.

Mineral Valuation in Canada: Where Do We Go From Here? Ross D. Lawrence, AIMA Member, President, Canadian Association of Mineral Valuators, Vice Chairman, Watts Griffis and McOuat, Toronto, Ontario, Canada.

The Mining Standards Task Force Report issued in November 1998 triggered a number of Canadian valuation initiatives. In the regulatory field, National Instrument 43-101 was designed to replace National Policy 2A, while the Ontario Securities Commission issued Rule 61-501 to replace it former policy 9.1.

In the professional field, the Association of Professional Geoscientists of Ontario was given legislative approval in July 2000 and is now gearing up. In the valuation field, two initiatives stand out. First, a special committee of the CIM was formed to produce a standard for the valuation of mineral properties.

SME Industrial Minerals Business Valuation Talk

On Tuesday, February 27, at the SME Annual Meeting in Denver, a luncheon address that should be of interest to many of us in valuation will be given at the Industrial Minerals Division Luncheon.
The speaker is Andrew Latham of the Warrior Division of Standard Americas Inc., the U.S. arm of Standard Bank London Ltd. His talk is titled, *Industrial Mineral Business Valuations*. This luncheon is between the two Valuation sessions described elsewhere in this Newsletter.

Standard Bank is one of the world's foremost corporate finance advisory services firms that is focused on the mineral resources sector, and Warrior is its industrial minerals division. Mr. Latham is based in Warrior's office in New York.

Second, the Canadian Association of Mineral Valuators was formed to certify valuators, set ethical standards and provide all of the services of a professional organization. This paper highlights the valuation milestones and presents an outlook for the future of mineral valuation in Canada.

An Australian Perspective on Mineral Valuation Best Practice, Michael J Lawrence, 1999 AusIMM President, MINVAL Associates Pty Limited, Croydon, NSW, Australia, to be read *in absentia*.

Each jurisdiction has its own rules and requirements that must be respected. However, the increasing globalization of the mining industry, makes it essential that standards of project assessment (evaluation) or valuation (appraisal, as well as reporting standards, are as similar as possible from the viewpoints of the relevant regulatory and the national professional bodies. Also, the accreditation (registration) and discipline of the author of such reports should be similar to facilitate the international mobility of minerals industry professionals.

Australia and New Zealand, particularly through their Australasian Institute of Mining and Metallurgy (AusIMM), have initiated the creation of useful models in these areas. The concepts contained in these codes have been adopted, to varying degrees, throughout the mining world and notably in Canada.

To facilitate the globalization of its codes, AusIMM has embarked on liaisons with many of its kindred bodies over recent years, particularly with IMM (UK), SME

(US), CIM (Canada), SAIMM (South Africa) and with IMAA/PERHAPI in Indonesia. An Australian perspective on the recent Canadian regulatory initiatives is presented and the remainder of the paper presents a personal perspective on mineral property valuation best practice.

U.S. SEC Direction in Disclosure of Mineral Information, Roger L. Baer, Mining Engineer, Division of Corporation Finance, U.S. Securities and Exchange Commission, Washington, DC.

Current U.S. Security and Exchange Commission (SEC) policy concerning public disclosure for mineral-oriented companies is summarized in Industry Guide 7. This guide can be reviewed on the Internet at: http://www.sec.gov/smbus/forms/industry.htm#secguide7 .

The SEC makes a clear distinction between exploration and production-stage companies. Each group has distinctive requirements for good public disclosure of information about their businesses. To more widely disseminate the SEC staff's interpretations and approaches to mining-related disclosure, the staff is currently preparing a document to highlight issues commonly encountered in its reviews of public registration statements, company annual reports and press releases.

This presentation will review current SEC policy and staff interpretations, and comments will be made on how they may affect mine valuation.

U.S. and International Valuation Standards - The Future, Trevor R. Ellis, AIMA President, Ellis International Services, Inc., Denver, CO.

Considerable movement is afoot internationally to rationalize standards and regulations relating to valuations and the qualifications for valuation professionals. In July 2000 the International Valuation Standards Committee released expanded standards, and additional important improvements are planned by 2003. Possible updates to the International Accounting Standards (IAS) and potential adoption of IAS by the U.S. could significantly impact minerals appraisers.

Standards designed specifically for mineral asset valuation are under development in Canada and the U.S., with Australia's internationally respected VALMIN Code providing the benchmark. In the U.S., the all-encompassing Uniform Standards of Professional Appraisal Practice (USPAP) is annually modified and continues to gain deeper acceptance, while the SEC holds fast to its antiquated rule prohibiting reporting of a quantitative estimate and value for non-reserve mineralization.

Some important international trade agreements are driving actions to free the trade in professional services. In July 2000, an international workshop was held to initiate discussion on minimum qualifications for appraisers to work internationally. Pressure for uniform minimum qualifications and rules for professionals internationally will continue to build. The U.S. is historically among the slowest countries to implement such initiatives, with its state level licensure barriers having the potential to cause some of its professionals to be stranded in an international backwater.

Structural change is needed in Australia's VALMIN Code to remove conflict with the latest International Valuation Standards. The mineral valuation standards developers of Australia, Canada and the U.S. should work jointly on updating VALMIN for global use.

Uniform Appraisal Standards for Federal Land Acquisitions
Year 2000 Edition Released!

An updated and substantially revised version of the Uniform Appraisal Standards for Federal Land Acquisitions has been produced. It has been prepared by the Interagency Land Acquisition Conference 2000 and will replace the 1992 edition.

It is available on the US Department of Justice Website www.usdoj.gov/enrd/land-ack/. The server was down when Trevor Ellis attempted to access a copy for review for writing this notice. Nor did the U.S. Government Printing Office list the publication as available for purchase, yet. Has anyone had any luck? Editor

The Editor's Swan Song

I have now for ten years cut and pasted our *Newsletter*. Modern word-processing has certainly eased the task, but we need to hit the newsstands more often. There are just so many appraisal-related issues to present and discuss. We need more case histories, more about our interface with the other appraisal professions and more news about our members.

Earlier this year we had an offer from one member to take over the editorship, but he got involved in too much appraisal work. Later in the year our hard-working President Ellis promised me relief from another willing hand, but the changeover boomeranged. I still ended up with this issue!

We need four issues a year and we need a new Editor! Let us discuss it at the Annual Meeting and maybe divide up the literary contributions among several members. Don Warnken has already offered to help. Anyone else?

In all seriousness, it has been both challenging and exciting to gather the material and see the many different contributions from our members. So what is a few hours of lost sleep or deadlines, which compete with a report to a client? It is all part of being a professional minerals appraiser.

John Gustavson, Your Ex-Editor

LATEST NEWS

The 2001 slate of officers has been elected by a sound majority. We appreciate your confidence and will do everything we can to make 2001 a banner year for our Institute.

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