# ASIC'S GUIDANCE ON PRODUCTION TARGETS FOR MINING COMPANIES - ARE WE CLEAR?

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Legal Briefings – By **Simon Reed** and **Michelle Palethorpe**

On 12 April 2016, the Australian Securities and Investments Commission (ASIC) released Information Sheet 214: Mining and resources: Forward-looking statements (Information Sheet 214) on forward looking statements commonly made in the mining and resources industry relating to production targets and forecast financial information.

**In Brief**

- Under the ASX reserves and resources reporting regime, listed mining companies must have 'reasonable grounds' for reporting a production target or financial forecast derived from a production target
- ASIC has released guidance which indicates that a project at the development stage will be less likely to have 'reasonable grounds' for forward looking statements
- Where secured funding for a project is not in place, ASIC is more likely to consider taking 'regulatory options'

On 12 April 2016, the Australian Securities and Investments Commission (ASIC) released Information Sheet 214: Mining and resources: Forward-looking statements (Information Sheet 214) on forward looking statements commonly made in the mining and resources industry relating to production targets and forecast financial information.

Information Sheet 214 covers, amongst other topics:

- that for reasonable grounds to be established, the JORC Code (Australasian Code for Reporting Exploration Results, Mineral Resources and Ore Reserves prepared by the Joint Ore Reserves Committee of The Australasian Institute of Mining and Metallurgy, Australian Institute of Geoscientists and the Minerals Council of Australia 2012 Edition) mineral resource estimates used must be based on a sufficient level of geological knowledge and confidence, and all JORC Code modifying factors must be sufficiently progressed;

- how the legal requirement to have reasonable grounds applies to ore reserve and mineral resource estimations;

- how the reasonable grounds requirement applies to the JORC Code's 'economic' modifying factor if secured funding is not in place;

- what you can disclose if you do not have reasonable grounds for forward-looking statements;

- what the requirements are for updating forward-looking statements when a company's circumstances change or a project changes hands, and

- what areas ASIC focuses on when assessing forward-looking statements.

**Ore reserve or mineral resource?**

Under Figure 1 of the JORC Code, mineral resources are defined with increasing levels of geological knowledge and confidence. Figure 1 also sets out the ‘modifying factors’ which relate to the considerations used to convert mineral resources to ore reserves and includes economic factors.

Information Sheet 214 notes that the definition of ‘ore reserve’ in the JORC Code is the ‘economically mineable part of a measured and/or indicated mineral resource’ under reasonable financial assumptions. Therefore, ASIC notes a correctly estimated ore reserve will be sufficient to establish reasonable grounds for a production target or forecast financial information based on a production target.

However, where less than ore reserves are reported, that is, measured, indicated or inferred mineral resources, ASIC states in the guidance that a reasonable basis on a mere geological knowledge and confidence basis, will not be sufficient.1 In this case, the JORC Code 'modifying factors' will also need to be sufficiently progressed, that is, the mining, processing, metallurgical, infrastructure, economic, marketing, legal, environmental, social and government requirements.

**Where secured funding is not in place**

Information Sheet 214 confirms recent industry speculation (see our article: Stricter approach on production targets for junior mining companies2) that ASIC will be concerned, and consider regulatory action, if no objectively reasonable grounds have been disclosed that support a conclusion that funding for a project will become available as and when required by the development or production schedules for the project.

ASIC refers to guidance in Regulatory Guide 111: Content of expert reports, which states that there may be a reasonable basis for the use of a discounted cash flow valuation methodology (DCF) before a project generates cash flows as long as, at the date of reporting, the expert has reasonable grounds for the forward-looking information. If there are no reasonable grounds, then ASIC suggests other valuation methodologies should be used. ASIC also states that the fact that a mining project can be financed by a third party does not mean that the third party will go ahead with the project.

One conclusion that could be drawn from this commentary is that a DCF valuation will only be appropriate where project funding arrangements are in place (rather than the company being reasonably satisfied that funding will be obtained) to fully fund each stage of the development schedule/mine plan.

This could give rise to a practical difficulty for junior mining companies who are at the stage of seeking financing arrangements for a project but for which alternative valuation models (such as market-based comparator methodologies) are not appropriate for the relevant project or are not favoured by potential financiers.

Information Sheet 214 also sets out a list of factors to consider in assessing reasonable grounds if funding is yet to be secured which includes: the company's size and capitalisation relative to the upfront capital expenditure requirement; the financial position of the company; the debt/equity financing track record and support; the dilutive effects of any financing to existing shareholders; support for substantial shareholders or other joint venture partners; the projects financial metrics; and the overall state of the relevant economies, demand/supply for the proposed mineral production and current debt/equity capital funding markets.

Unfortunately, ASIC stopped short of providing guidance on how it would apply each of these factors which may continue to result in different assessments on what is "reasonable" in the market.

## Updating forward looking statements and projects changing hands

Where a production target or forecast financial information based on a production target has been disclosed to the market, ASIC recommends that companies should be checking periodically whether the underlying mineral resource estimates and modifying factors remain unchanged and continue to be sufficient to support the statements.

ASIC cautions against a buyer automatically republishing a vendor’s production target without assessing whether circumstances have changed. This includes where the buyer has insufficient stand-alone financial capacity or where a DCF valuation uses the vendors funding position or corporate financial hurdle rates.

## Implications for mining companies

It is likely that the effect of ASIC’s stated position is that mining companies who have not declared an ore reserve will be unable to disclose production targets or DCF valuation models unless they have firm commitments (likely to be in writing) to fund each stage of a project and all the other modifying factors are reasonably likely to be achieved. This is particularly the case in a heightened disclosure period such as where a company is undertaking fundraising activities or is involved in a control transaction.

ASIC suggests in Information Sheet 214 that, in these circumstances, instead of disclosing a production target a company can make ‘aspirational statements’, announce exploration targets or disclose parts of a preliminary study that do not contain forward-looking statements. For example “the results of the preliminary study were positive and that the results justify the entity to commit to the next stage of exploration and development”.

Whether this information is enough to satisfy financiers and investors remains to be seen as the sector continues to face numerous additional challenges in attracting financing and developing projects.

## Endnotes

Note that ASX Listing Rule 5.15(a) prohibits the use of explorations targets alone, or in combination with only an inferred mineral resource, in support of a production target.
Stricter approach on production targets for junior mining companies
More information

For information regarding possible implications for your business, contact Simon Reed or Michelle Palethorpe.

# ABOUT THE AUTHORS

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# KEY CONTACTS

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