

U.S. SEC has Modernized its Property Disclosure Rules for the Mining Sector - *Evolution, Content, Expectations*

Trevor R. Ellis, RM-SME, CPG, CMA, FAusIMM

Mineral Property Valuer
Ellis International Services, Inc.
Denver, Colorado, USA
www.MineValuation.com



National Mining Agency's Mineral Resources and Reserves Week

Bogotá, Colombia, 28-30 November 2018

Disclaimer

The opinions expressed here are primarily from my compilation of opinions expressed by U.S. mining industry personnel who have studied the SEC's new disclosure rules in-depth.

Announcement, 31 October 2018

- Press release by U.S. Securities and Exchange Commission (SEC), titled:
 - *SEC Adopts Rules to Modernize Property Disclosures Required for Mining Registrants*
- The extent of modernization is DRAMATIC!
- The *Final Rule* document released, containing explanations, is huge, 453 pages.
- Rules adopted as Regulation S-K 1300
 - 68 pages
 - Effective early 2019. Compliance required 2021.

Primary Conclusions

- The definitions closely align with CRIRSCO's
 - But, the SEC's are more strictly defined throughout
 - SEC specifications for reporting Mineral Resources are higher
- The regulations are mainly rules-based
 - Not principles-based. Negligible allowance for judgement, initiative, and flexibility.
 - Content of Qualified Person's (QP's) Report is strictly specified in extensive detail.
- QP's liability is high and concerning.
- The reporting (registrant) mining company's disclosure burden is high and concerning.

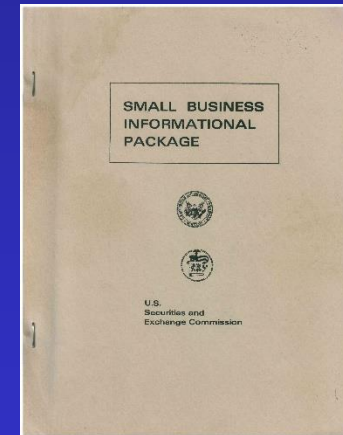
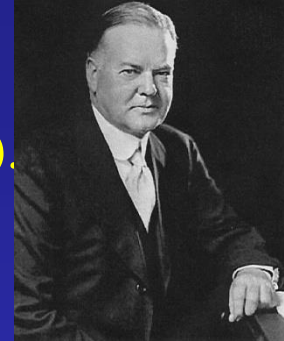
Primary Conclusions

- The new rules might slow the rate of migration of primary listings by mining registrants from the USA to Canada and elsewhere.
- They will not reverse the migration.

(Consensus from interviews)

SEC's History of Mining Regulations

- SEC's focus is investor protection.
- In 1930s, SEC adopted Herbert Hoover's 1909 definitions of Proven, Probable, and Possible Ore. (Resources not recognized).
 - In Hoover, 1909, *Principles of Mining*, 199 pages
 - Hoover: Mining Engineer (Stanford degree 1895), U.S. President 1929-33
- *Industry Guide 7* issued March 1981 (then not titled)
 - Published as a 2-page set of instructions (in small font)
 - Defines Proven and Probable Reserves. No Possible Reserves allowed.
 - Restricts disclosure of quantitative estimates to reserves only
 - Restricts value estimates to reserves only
 - No technical competency requirement – policing difficulties resulted
 - Text never modified in its 37 years
 - Abolished when *Regulation S-K 1300* is in effect.
- The SEC's fear that the U.S. public would not understand the difference between *Mineral Resources* and *Mineral Reserves*, continued into this century.



SEC's History of Mining Regulations

- However, an exception to Guide 7 existed:
 - Information disclosure allowed in U.S. by SEC if disclosure was required by state or foreign law, or if disclosed to a potential acquiring or merging party.
- Then, 1991, the Canada/US multi-jurisdictional disclosure system (MJDS), provided reciprocal disclosures between Canadian and US issuers.
- Result:
 - By the 1990s, mining industry companies were discovering that Canadian stock exchanges were more favourable for listing than U.S., even for U.S.-based companies.
 - During the 1990s, companies learned that with Guide 7 and the MJDS, if a listing on a U.S. exchange was desired, list first in Canada, then get a secondary listing in the USA. This allowed disclosure of quantitative resource estimates in the USA.
 - With a warning statement to potential U.S. investors to ignore those estimates.

SEC's History of Mining Regulations

- In Denver in 1997, definitions for mineral resources and reserves were agreed upon by representatives from the world's major mining institutes:
 - U.S. (SME), Australasia (AusIMM), Canada (CIM), the United Kingdom (IMM), South Africa (SAIMM).
- By 2000, many U.S. mining industry professionals, including me*, were complaining about negative effects of SEC's Guide 7's ban on reporting quantitative mineral resource estimates
 - Complaints included difficulties obtaining mineral resource estimates for purposes unrelated to regulatory reporting

*In papers authored by Ellis.

SEC's History of Mining Regulations

- In 2001, mining sector registrants found that the SEC was informally allowing disclosure of quantitative estimates of the sum of measured plus indicated resources
 - If termed a “mineral deposit” or “mineralized material,” with a recommended definition included
- In 2003, meetings of SME representatives with SME staff began, for discussing mineral resource and reserve reporting
- In 2012, the SEC with SME began a formal proceeding to modify Guide 7
 - Resulted in Regulation S-K 1300 and abolishing Guide 7
 - Regulation S-K contains the SEC's instructions for filing forms

Content

- In June 2016, the SEC published its proposed Regulation S-K 1300, seeking comment submissions
 - Nearly all submissions expressed serious concerns
- The finalized rules contain extensive modifications in response to the comments
- Close alignment with the CRIRSCO standards
 - Especially as contained in the *SME Guide 2017 edition*
 - But, no external content incorporated by reference, as done by other national securities regulators
 - Therefore, the rules could again become outdated

Content

- The three governing CRIRSCO principles are emphasized:
 - Transparency, materiality, and competence
- Disclosure required for any operation activity (or probable operation) on a mineral property that is material to the business or financial condition
 - exploration, development, producing, or reclamation property, or royalty holding.
 - Determination of materiality is principles-based.

Content

- A “technical report summary” must be submitted for each material property, or material group of properties
 - The rules strongly state the requirement for “summary” content, but some requirements specify detailed data that could be massive
 - E.g., specifics for hundreds of mining claims, hundreds of drill holes, or thousands of mineral samples
- The report must be written by one or more QPs
 - The definition of Qualified Person closely aligns with CRIRSCO’s Competent Person definition

Content

- The definitions for Mineral Resource, Mineral Reserve, and many other technical terms, closely, but not exactly align with CRIRSCO's.
 - As compared to in the CRIRSCO Template and SME Guide, little elaboration and explanation is included to guide the application of the definitions.
 - The resource and reserve definitions are stricter, as are some others, due to small wording changes converting them to being prescriptive, rather than principles-based.
 - E.g., for a Mineral Reserve, extraction must be demonstrated to be “economically viable” rather than “could reasonably be justified.”
 - For a Mineral Resource, “eventual” is deleted from “reasonable prospects for eventual economic extraction.”
- The levels of confidence that the QP must state have been increased throughout the rules over CRIRSCO's

Content

- Content of the technical report summary
 - The QP(s) must include the following, “to the extent the information is material”:
 - Executive Summary
 - Introduction
 - Property Description
 - Accessibility, Climate, Local Resources, Infrastructure, Physiography
 - History
 - Geological Setting, Mineralisation, and Deposit
 - Exploration
 - Sample Preparation, Analyses, and Security
 - Data Verification
 - Mineral Processing and Metallurgical Testing
 - Mineral Resource Estimates
 - Mining Methods
 - Processing and Recovery Methods
 - Infrastructure
 - Market Studies
 - Environmental Studies, Permitting, and Plans, Negotiations, or Agreements with Local Individuals or Groups
 - Capital and Operating Costs
 - Economic Analysis
 - Adjacent Properties
 - Other Relevant Data and Information
 - Interpretation and Conclusions
 - Recommendations
 - References
 - Reliance on Information Provided by the Registrant

Concerns

- SEC wants either the QP or the registrant to be liable for all information disclosed
 - Even information developed by specialist professionals
- The QP and registrant are both held to the same liability standards for incorrect statements.
- Liability protections recommended for the QP:
 - A corporate arrangement can minimize the QP's liability risk: The QP's corporation signs the report as itself a QP. The name of the individual QP person is not disclosed in the report.
 - Or, the QP would be protected if he or she is an employee of the registrant when developing the report.

Concerns

- QP will likely be responsible for validating information and providing opinions and conclusions on aspects outside their expertise
 - E.g., a QP geologist may be expected to validate and opine on mineral processing and environmental matters.
- The requirements for the QP to verify the validity of the work of others for every aspect of the report, could be burdensome and conflict with the “relevant experience” requirement.
- The prescriptive wording throughout the rules has significantly raised the hurdle relative to CRIRSCO-based standards for declaring both mineral resources and mineral reserves, and for the individual categories within those.

Concerns

- Requirements for an exploration company to disclose material property acquisitions and material exploration data. Could lose a competitive advantage or have its acquisition strategy blocked. May damage a joint venture agreement.
- Producers of coal, aggregates, and industrial minerals, could lose market advantages due to requirement to disclose information that is presently kept confidential, such as sales contract prices for their products. Disclosure could also damage a client.
- The public disclosure of a Preliminary or Final Marketing Study could be fatal for non-freely traded commodity projects. “Their competitors can immediately block that strategy.”*
- Numerous lesser concerns expressed.
 - Uncertainties of meaning of ambiguous and confusing sentences.
 - Uncertain whether the SEC will strictly enforce various stringent or burdensome requirements.

*SME reviewer

Mining Industry Finance

- In the London-based Mining Journal's 92-page, 2018, *Global Finance Report*, the U.S. only receives two tiny mentions.
- The five stock exchanges reviewed are: Canada's TSX and TSX-V; London's LSE main and AIM; and Australia's ASX.
- Major mining companies wanting to raise \$Billions will seek that in the USA.



Supplemental Conclusions

- The major financial action for the mining industry remains north of the U.S.-Canada border – Toronto and Vancouver. Companies will continue to list there to be amongst the action.
- To stop the migration of mining industry primary listings from the U.S. to Canada and elsewhere, Regulation S-K 1300 needed to be in place in 1995.*
- The regulations may slightly improve investor confidence in the stocks of the few remaining primary listings on the major and secondary markets.
- Issuers of small and thinly traded offerings (over-the-counter and off-market securities) that fall under SEC filing requirements, will likely find compliance difficult, troubling, and expensive. They may also consider registering outside the U.S., joining the migration.
- In 5-10 years from now, the rules might encourage more primary U.S. listings, dependent on how they are implemented.*

*SME reviewer