Mineral Property Valuation Standards - A U.S. Perspective

Marching with the International Valuation and International Financial Reporting Standards

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SUMMARY

The author opposes the presently developing movement of national minerals institutes, such as SAIMM, towards drafting comprehensive standards for mineral property valuation following the model of the development of the Reserve-Resource reporting standards. He has campaigned against such undertakings proposed for U.S. minerals institutes such as AIMA and SME. Unlike Reserve-Resource estimation, few valuation issues are unique to the minerals industry.

The *International Valuation Standards* (IVS) of the International Valuation Standards Committee (IVSC) have achieved a high level of acceptance in the developed and lesser developed countries of the world since release of the 2000 edition. IVS provides a comprehensive framework of Generally Accepted Valuation Principles for the Valuation profession internationally, for valuation of all property or asset types, including real property, personal property, businesses and financial interests. IVSC is effectively a sister organisation to the International Accounting Standards Board (IASB). The *International Accounting Standards* (IAS) references and quotes IVS in some instructions for determination of Fair Value. IVSC is a Non-Governmental Organisation (NGO) member of the United Nations and maintains liaison with many important international economic, accounting and financial agencies, such as the OECD, IMF and WTO.

In February 2001, IVSC convened an Extractive Industries Task Force to respond to minerals and petroleum valuation issues raised during the planned development of an International Accounting Standard for the extractive industries. The author led the task force in developing IVSC's initial input to the IASB. IVSC has proposed reconvening the Extractive Industries Task Force in 2002 to rapidly draft a mining and petroleum section for inclusion in IVS, with particular attention given to addressing IASB concerns. The Task Force will likely expand its membership, and draw from the principles included in The AusIMM's VALMIN Code and the Canadian CIMVal Standard now being finalised.

IVSC hopes to have the draft extractive industries section ready by the end of 2002 for distribution in the next edition of IVS as an Exposure Draft for public comment. The section will be concise, since it will be a supplement to the existing valuation framework supplied by IVS, addressing only the essential elements that are specific to minerals and petroleum valuation. The author proposes that the Council of Mining and Metallurgical Institutions (CMMI) then consider developing supplementary guidance and qualifications requirements, with that document incorporating IVS by reference. The mining institutes of individual countries should then adopt IVS and CMMI's supplementary document by reference. They could supplement those with their own document containing guidance unique to their country's situation, and incorporate their own binding instructions and enforcement provisions.

This paper provides the author's preliminary suggestions of how extractive industries guidance should be incorporated into the IVS. It concludes by recommending that SAIMM avoid the difficult, lengthy and contentious process of developing its own valuation code, and instead adopt the IVS and put its full support behind IVSC's development of an extractive industries section for the IVS. It can then adopt a standard that will have the highest level of international recognition and distribution.

INTRODUCTION

Since 1990, the world has made large advances in globalization of trade and financial services. This has been aided by enhancing the General Agreement on Tariffs and Trade (GATT) and implementation of the 1994 General Agreement on Trade in Services (GATS) by the World Trade Organisation (WTO). Such globalization is driving the development and implementation of globally uniform corporate accounting and financial reporting standards. It also is driving the development and implementation of globally uniform valuation standards for all asset types.[1] Uniformity of rules and standards is being demanded by corporations, governments and securities exchanges.

Standards development initiatives for the extractive industries (mining and petroleum) are already being undertaken by the International Accounting Standards Board (IASB) and the International Valuation Standards Committee (IVSC), both based in London. IASB has an Extractive Industries Steering Committee in place that is preparing to draft a financial reporting standard for the extractive industries for inclusion in the International Financial Reporting Standards (IFRS) as a relatively high-priority project. In cooperation with the IASB and largely to support the planned extractive industries financial reporting standard, the IVSC's Extractive Industries Task Force will draft an extractive industries section for inclusion in the International Valuation Standards. Dependent on receiving necessary input from IASB, the IVSC is seeking to have a draft ready for publication by the 2002 year end.

In light of this, the author recommends that national mining institutes should cease their drive to develop national mineral valuation standards.[2] It is time to move forward and work in the global context. We have benefitted greatly from the efforts of members of The Australasian Institute of Mining and Metallurgy (AusIMM) who have worked on the development and growth of the VALMIN Code since 1989, especially the efforts of Michael Lawrence (AusIMM, 1998). Since 1999, we also have greatly benefitted from the efforts of members of the Canadian Institute of Mining, Metallurgy and Petroleum (CIM) who have contributed to the development of the Draft CIMVal Standards published February 2002, and the final standards to be published in May (CIM, 2002). The VALMIN Code and CIMVal Standards have developed from extensive research and considerable thought in formulation. These are two excellent sources to draw upon during drafting of the extractive industries addition to the IVS. The CIMVal Standards will be a particularly useful source since this set is the newer generation and has been developed with its framework, concepts and definitions largely consistent with IVS. "CIMVal intends to be consistent with the general thrust of (IVSC's) work such that, if and when the IVSC's standards are adopted globally in the future, the CIMVal Standards will be readily adaptable." (CIM, 2002, p6). The author commends the CIMVal Committee for this.

It is important that the valuation procedures and reporting requirements for all types of mineral asset valuation mesh with those generally accepted by the global financial community. The best way to achieve this is for our mineral valuation rules and guidelines to be interwoven in the same IVS book with which the global financial community is familiar and looks to as the set of standards for valuation of all types of property and assets in all settings.

The author recommends that South Africa not undertake development of its own mineral valuation standards. Instead it should put its support behind the international initiatives already in place through the IVSC and in conjunction with the IASB. The author has proposed that supplemental guidance of an international nature on minerals valuation and competent person qualifications be provided by the Council of Mining and Metallurgical Institutions (CMMI). National mining institutes and regulatory bodies should adopt IVS and the CMMI's supplemental guidance, and be responsible for enforcement. Guidance on the application of IVS under national regulations and requirements should then be developed by national mining institutes or regulatory bodies.

Immediate adoption of the IVS by SAIMM would provide a useful set of standards for its members through the period of concern to 30 September 2003, despite its lack of specific extractive industries guidance as yet. IVS provides the more important valuation framework based on the Generally Accepted Valuation Principles that represent accepted best practice globally in the Valuation Profession (IVSC, 2001, p16).

IASC AND INTERNATIONAL ACCOUNTING STANDARDS DEVELOPMENT

The International Accounting Standards Committee (IASC), the predecessor of IASB, was formed in 1973 and headquartered in London. Its objective was "*harmonising the accounting principles which are used by businesses and other organisations for financial reporting around the world.*" Harmonisation would allow companies to provide financial reports to securities exchanges in a number of countries with-

1. In the U.S., the term *appraisal* is used for a *valuation* assignment and a formal *Valuation* report. A *valuation* under U.S. usage is typically a less stringent undertaking than an *appraisal*, especially when Real Property is involved. Similarly, a professional *valuer* or *valuator* is called an *appraiser* in the U.S. For the South African audience, valuation and valuer are generally substituted for the U.S. equivalent terms throughout this paper.
2. The South African minerals industry is confronted by a special situation related to the requirement for valuations for capital gains tax purposes to be carried out by 30 September 2003. It would be very difficult for SAIMM to quickly adopt any standard that requires modification, in time to provide a useful time span of governance of its members prior to that date. Therefore, the author recommends that SAIMM give serious consideration to immediate adoption of the IVSC's International Valuation Standards. Quick modification and adoption of the recently released Canadian Draft CIMVal Standards also might be attempted, and if successful could be used as a supplement to IVS (CIM, 2002).

out modification due to variation in accounting rules. Harmonisation meant that countries could adopt the IAS developed by IASC, or modify their existing standards to include the same accounting principles.

By the time IASB took over the IASC's role at the end of 2000, its membership consisted of 153 professional accounting bodies in 112 countries. Though much of its management and standards development work was done on a volunteer basis, it was quite successful and well respected internationally. IASC developed close relationships with all major international financial and economic bodies.

Although the U.S. has been among the slowest countries in progressing with harmonisation, largely due to the scale and complexity of its economy, it has been one of the strongest supporters of IASC and its goals. From 1983, the U.S. Securities and Exchange Commission (SEC) was having formal meetings with IASC. In 1988 the U.S. Financial Accounting Standards Board (FASB) joined the IASC's consultative group in a supporting role. The U.S. Congress passed the National Capital Markets Efficiency Act in 1996, which contains paragraphs encouraging rapid establishment of high quality international accounting standards and requiring the SEC to report to it on progress made towards allowing unadjusted IAS-based financial disclosures (Section 509). Many high level U.S. regulatory personnel on their retirement took positions in IASC and now IASB. An example is Paul Volcker, former Chairman, Board of Governors, U.S. Federal Reserve Bank, who is now Chairman of the IASC Foundation, and another example is the former Chairman of the SEC, Arthur Levitts.

In 1987, IASC published its first bound volume of International Accounting Standards (IAS). In the same year, the International Organization of Securities Commissions (IOSCO) joined the IASC's consultative group in a supporting role. In 1998, IASC completed the major components of the core set of Standards, as identified in an agreement with IOSCO in July 1995. The core standards provide a comprehensive basis of accounting, covering all the major areas of importance to general businesses. They will result in transparency and comparability and they provide for full disclosure.

In May 2000, IOSCO recommended that its members endorse the use of IAS by companies with cross-border offerings and listings. However, the extractive industries and some other economic sectors were excluded from this approval, because they have specialized reporting practices falling outside of the scope of the 30 standards approved by IOSCO resulting from the IAS core standards work program.

Many countries have already adopted IAS as their own, some with minor changes. Some others, such as Australia, have been modifying their standards to match or harmonise with IAS. In June 2000, the European Commission announced that all European Union companies listed on the securities markets should prepare their accounts using IAS by 2005, and is considering advancing that deadline. Although U.S., Canada and Japan are the slowest to adopt IAS, that adoption is accelerating rapidly. The U.S. and Canada have been working under a policy of first attempting to rapidly converge their Generally Accepted Accounting Principles (GAAP) systems of accounting to effectively merge into one system, then modifying GAAP to harmonise with IAS. The timescale for completion appears to remain a few years. The Canadian Securities Administrators (CSA), based on responses it received to a March 2001 discussion paper, is giving serious consideration to abandoning the GAAP convergence project with the U.S., to accelerate adoption of the IAS accounting principles (CSA, 2001). South Africa has modified its GAAP system to allow South African companies to provide IAS compliant reports, but foreign IAS reports are not yet accepted without adjustment to GAAP.

IASB AND INTERNATIONAL FINANCIAL REPORTING STANDARDS DEVELOPMENT

In December 2000 to March 2001, IASC physically underwent a major restructuring, and the IASC organisation was dissolved and replaced by IASB. A determination had been made by IASC in cooperation with governments and the international financial community that the time had come to transition the primary focus from IAS development to global implementation. The SEC and FASB heavily influenced the determination and its outcome (Volcker, 2002). The volunteer board has been replaced by a paid board of primarily full time members, with heavy U.S. and European representation. This new organisation, IASB, relies largely on government rather than private funding. The U.S. will be funding a substantial portion of the IASB's expanded annual budget of approximately £15 million (approximately $20 million).

The IASB's statement of objectives is:

> *The Board is committed to developing, in the public interest, a single set of high quality, understandable and enforceable global accounting standards that require transparent and comparable information in general purpose financial statements. In addition, the Board cooperates with national accounting standard setters to achieve* ***convergence*** *in accounting standards around the world.* (Emphasis added)

The goal of "convergence" in replacing that of "harmonisation" of accounting standards around the world has resulted in the IASB starting the development of a new set of standards. Sir David Tweedie, Chairman, IASB, in describing the goal for the new International Financial Reporting Standards (IFRS), said, 'we plan to build a set of financial reporting standards that are the "gold standard"' (Tweedie, 2002). The ultimate goal is to have only one high quality set of accounting standards used globally in private sector financial reporting, these being the IFRS.

The convergence process in developing the IFRS is being conducted by representatives of the financially advanced countries of the world working directly together, these being from France, Germany, United Kingdom, Japan, Canada, United States and Australia. The process involves reviewing existing national standards and IAS rule by rule to select the best rules for inclusion in IFRS. The spectacular imploding and bankruptcy in late 2001 of the $60+ billion Enron Corporation, and some other recent major financial reporting disasters in the U.S. and Europe have added emphasis to the importance of the convergence process. The Extractive Industries Standard when completed will be an IFRS.

Current Value Reporting

The reporting of the value of assets is one of the areas of most important difference between the IFRS and the older style GAAP systems of accounting still employed in the U.S. and Canada. GAAP dictates reporting of asset value based on their historic cost. Each year the value of the asset is adjusted downward by depreciation, amortization or depletion. Addition of asset value to the accounts requires that an expenditure be capitalized. GAAP can provide accuracy to the cent in reporting to shareholders the depreciated value of a high rise New York or Toronto office building that a company has held for 20 years. It is an extremely precise accounting system. But, GAAP's accuracy is horrible. While the value of the office building is now reported in the accounts to stockholders at less than half its purchase price, the building's market value may have increased 5-fold. With a 10-fold inaccuracy in the value reported, the company is a takeover target. IFRS solves this serious problem by allowing current value *(fair value)* reporting for assets in the primary financial accounts of companies. Many companies in Europe that have adopted IFRS obtain fresh valuations of their major assets, particularly real estate, every two or three years. Those current asset values are entered into the accounts, then depreciation and amortization begin again.

IFRS allows companies to retain historic cost accounting if they prefer. However, once companies adjust their accounting systems to IFRS, it will in general benefit them to move to current value reporting for assets. In addition to providing the shareholder and financial community with a much more accurate statement of company assets, it will generally benefit companies by reporting much higher values for their appreciated assets. This will tend to elevate the price of their shares and aid fund raising.

We hope that the proposed Extractive Industries IFRS will provide similar current value reporting opportunities for mineral and petroleum deposits. However, the tentative views expressed in the IASC's Extractive Industries Issues Paper published in November 2000, and the content of responding submissions, provide cause for concern as discussed below (IASC, 2000).

IVSC AND INTERNATIONAL VALUATION STANDARDS DEVELOPMENT

The International Valuation Standards Committee also is based in London. It was founded in Melbourne, Australia in 1981. The objectives of IVSC are stated as follows:

> *The principal IVSC objective is to formulate and publish, in the public interest, valuation Standards and procedural guidance for the valuation of assets for use in financial statements, and to promote their worldwide acceptance and observance.*
>
> *The second objective is to harmonize Standards among the world's states, and to make disclosures of differences in standards statements and/or applications of Standards as they occur.*
>
> *It is a particular goal of IVSC that international valuation Standards be recognised in statements of international accounting and other reporting standards, and that Valuers recognise what is needed from them under the standards of other professional disciplines.* (IVSC's website www.ivsc.org)

From the perspective of the application of the IFRS, IVSC can be viewed as an important small sister to IASB. IVSC is developing the standards for valuation of assets that are reported at *fair (market) value* under IFRS. The Investment Property Standard recently released by IASB, references and quotes from IVS in its instructions for determination of *fair value*. However, the intended applications for the IVSC standards cover the broader spectrum of uses for formal valuations.

IVSC published the first edition of the IVS in 1985. By the 1997 edition a useful core set of standards was available, and the IVS was now recognised throughout the world and had already been incorporated into the domestic Standards of many nations. In recent years the pace of development has accelerated. The 2001 edition, which the author estimated as being approximately three times the size of the 1997 edition, is a very comprehensive, well organised, 458 page book (IVSC, 2001a). It is written in a relatively easy to read style, considering the nature of its content. The 2000 edition is available in a number of languages, as will be the 2002 edition. It contains guidelines for valuation of the four generally recognised Property Types (categories of assets), these being Real Property, Personal Property, Businesses, and Financial Interests (Intangible Property). It also includes a Code of Ethics and Competency Provisions for the Valuer, though IVSC and IASB have no enforcement mechanism of their own (Ellis, 2001). Ten Guidance Notes sections address specific valuation topics, and work is in progress towards developing additional sections.

The development of the International Valuation Standards (IVS) has been guided by three principal objectives:

> *To facilitate cross-border transactions and contribute to the viability of international property markets by promoting transparency in financial reporting as well as the reliability of valuations performed to secure loans and mortgages, for transactions involving transfers of ownership, and for settlements in litigation or tax matters;*
>
> *To serve as a professional benchmark, or beacon, for Valuers around the world, thereby enabling them to respond to the demands of international property markets for reliable valuations and to meet the financial reporting requirements of the global business community; and*
>
> *To provide Standards of valuation and financial reporting that meet the needs of emerging and newly industrialised countries*. (IVSC, 2001, p. 15).

National valuation associations from 35 countries maintain full IVSC membership, and another 11 countries have observer status representation. IVSC is a Non-Governmental Organisation member of the United Nations, and like IASB works closely with many influential international bodies, such as the World Bank, the Organisation of Economic Cooperation and Development, the International Monetary Fund and the World Trade Organisation.

IVSC's EXTRACTIVE INDUSTRIES INITIATIVE TO ASSIST IASB's PROJECT

IASC Extractive Industries Issues Paper

The IASC in April 1998 appointed a 12 person Extractive Industries Steering Committee to investigate the development of one or more accounting standards for use by mining and petroleum industry enterprises. Development of the Extractive Industries Accounting Standard(s) is occurring at the specific request of the International Organization of Securities Commissions. After 30 months of research, in November 2000 the Steering Committee released a 412 page Issues Paper containing a wide variety of discussion to consider and about 100 questions (IASC, 2000). Submissions in response were sought by 30 June 2001.

The author found that the tentative views expressed by the Steering Committee have a disconcerting *deja vu* resemblance to the U.S. Securities and Exchange Commission's perspective expressed in its highly restrictive *Industry Guide 7* (SEC, 1992). The Steering Committee's tentative recommendation is that primary accounts of extractive industries companies must be reported on an historic cost basis only. Disclosure of the current value of Reserves would be restricted to a supplemental information section and likely be based on a specified method for calculation of a pseudo value as is done now for U.S. petroleum industry reporting. The question of whether to allow quantitative reporting of Resources that are not Reserves, as supplemental information, was only barely included, despite this being an item of great importance for the mining industry. The possibility of reporting an estimate of the current value of any category of such Resources was not included (Ellis, 2001a-b).

If the Extractive Industries Accounting Standard is finalized with this perspective, the restriction to an historic cost accounting basis for Reserves and Resources will greatly handicap the financial abilities of the mining and petroleum industries relative to all other industries that will be allowed current value accounting of their assets (Ellis, 2001b). Research reviewed in the Issues Paper, partially based on the Australian experience, shows that investors react very favorably to current value reporting of reserves in the primary financial accounts of extractive industries corporations, resulting in "a significant effect on the value that the market places on an enterprise's shares" compared to disclosure of the current values in the supplemental information.

IVSC's Extractive Industries Submission to IASB

In late January 2001, the author was contacted by the IVSC to assist it in developing its response to the Issues Paper. Due the long, close relationship with the IASB, the IVSC's input can be expected to receive careful consideration. An IVSC representative has often been appointed to IASC committees that develop standards.

With the author's assistance, the following volunteer Task Force of independent expert minerals valuers was quickly assembled:

Trevor Ellis as the U.S. representative and Task Force leader. President, American Institute of Minerals Appraisers.

Michael Lawrence as the Australasian representative. Chairman, AusIMM's VALMIN Code Committee.

William Roscoe as the Canadian representative (Ross Lawrence, alternate). Co-Chair, CIM's Special Committee on Valuation.

Roger Sawyers as the U.K. representative. Chartered member, Royal Institute of Chartered Surveyors.

Raymond Westwood, Retired Valuer-General, Tasmania, Australia, provided enormous assistance and advice as Technical Editor, having a strong knowledge of the applications and interaction of IVS and IAS.

The response document drafted by the Task Force addressed issues pertaining to the nature of mineral deposits and their valuation. It did not respond to questions about some of the more esoteric areas of accounting. The response document was submitted by the IVSC to the IASB in June 2001 (IVSC, 2001b). Through this, the Task Force hopes to influence the IASB Steering Committee to modify the outcome to an appropriate current value accounting standard for the extractive industries, based on an international minerals valuation standard.

The IVSC has allocated some financial sponsorship for international travel expenses to the Task Force to assist it in composing on a timely basis an Extractive Industries addition to IVS, and for providing additional support to the IASB as may be requested. IVSC is seeking minerals and petroleum industry financial support to provide the Task Force with additional sponsorship for this very time consuming undertaking (but no support had been received at the time of this writing in late February, 2002). An expanded IVSC Task Force should begin drafting the Extractive Industries addition soon after the IASB announces the results of its review and consideration of the submissions, which is expected by May 2002.

In the review of mining and petroleum industry practice in the IASB Issue Paper, Steering Committee members expressed considerable concern about the lack of tight industry standards for the inputs into reserve and resource estimates, particularly economic inputs. Confusion by the Steering Committee is apparent in the document over what, if any, similarities might be drawn between the petroleum industry's reserve definitions (developed by the Society of Petroleum Engineers and World Petroleum Congresses) and the mining industry's Reserve and Resource reporting Standard (the Australasian JORC Code, adopted internationally through the Council of Mining and Metallurgical Institutions and incorporated in United Nations' definitions) (JORC, 1999; Miskelly, 2001). In addition to the lack of "quality" that Steering Committee members perceive in reserve and resource estimates, they express concern about the difficulties and inconsistencies in valuation of those reserves and resources. The petroleum industry has much more distance to cover in addressing these concerns than the mining industry. The petroleum industry's reserve definitions are looser than those of the mining industry; the petroleum industry lacks an equivalent of the Reserve-Resource reporting Standard of the mining industry based on defined Competent Person requirements; and no equivalent of the Australian mining industry's VALMIN Code is present for petroleum (AusIMM, 1998). In drafting the submission, considerable effort was directed at explaining and demonstrating those differences and attempting to remove the confusion.

The following, directly quoted, are the main recommendations made in the IVSC submission:

- There should be a single reporting Standard for the extractive industries with differences between the mining and petroleum industries covered by individual rules.
- The *fair value* of Proved and Probable Mineral Reserves and proved petroleum reserves should be the preferential reporting definition in the primary financial accounts, with *historic cost* reporting for these reserves as an option. No reporting of value of probable or possible reserves for petroleum, or any Mineral Resource categories should be allowed in the primary accounts.
- For mining industry enterprises, quantitative and qualitative information should be included in the supplemental statements for all Mineral Reserve and Mineral Resource categories.
- For petroleum industry enterprises, quantitative information should be included in the supplemental statements for all proved and probable reserves. No reporting for possible petroleum reserves should be allowed, nor should such for any petroleum resource category. The IVSC Task Force has concluded that the content of the petroleum possible reserves category is much too speculative for public disclosure as reserves, while the potential for profitable extraction from the contents of the resource classes within a reasonably foreseeable timeframe is too low for public disclosure.
- For mining industry enterprises, reporting of the *fair value* of Measured and Indicated Resources should be encouraged in the supplemental notes, with mandatory *historic cost* reporting required as the alternative. *Fair value* reporting for Inferred Mineral Resources and exploration properties lacking defined Mineral Resources should also be allowed, subject to careful review for reasonableness, and only if such value does not compose a large portion of the value of the company, with *historic cost* basis being the alternative.
- *Fair value* disclosure for probable petroleum reserves should be allowed in the supplementary notes. Such disclosure should also be allowed for exploration properties lacking proved or probable reserves, subject to careful review for reasonableness, and only if such value does not compose a large portion of the value of the company. In both cases, *historic cost* basis disclosure should be the alternative.
- The IASB standard should specify that reports of Mineral Resource and Mineral Reserve estimates must be developed and reported in compliance with one of the CMMI-based standards. A Competent Person similar to that specified in the CMMI-based standard must take responsibility for the report. Reports of petroleum reserve estimates should comply with the SPE/WPC definitions. IASB should encourage the petroleum industry to develop a petroleum reserve reporting standard containing a competent person provision similar to that in the JORC Code.
- *Fair value* valuation of all mineral and petroleum properties should be performed by defined Competent Persons and the name and qualifications of such persons should be disclosed by notation in the supplemental statements. Guidance by a comprehensive internationally respected mineral and petroleum valuation standard should be specified. Presently the Australasian VALMIN Code is the only standard available that meets those criteria. However, the Task Force does not view it as suitable for direct application to meet such wide ranging needs. Development by IVSC of the Extractive Industries guidance section of the International Valuation Standards using VALMIN and CIMVal as a base will allow a truly international extractive industries standard suitable for all jurisdictions to be referenced by the IASB Standard.
- The proposed IASB Standard must allow changes in the value of mineral and petroleum assets to be made in the financial statements without being reflected in the profit and loss statements. A requirement to reflect such changes in the profit and loss statement will discourage reporting of negative corrections, while positive changes could frequently mask operating results.
- *Fair value* revaluation of mineral and petroleum properties should only be expected at four or five yearly intervals for inclusion in the primary accounts and supplemental disclosures or when major quantitative changes in reserves or resources occur that are not due to production.
- Any enhancements to the petroleum industry's resources and reserve reporting definitions which IASB determines are needed, or possible future development of a reserve reporting standard, should be coordinated through SPE/WPC or a successor international body representative of the petroleum industry as may exist at the time.
- Any enhancements to the mining industry Mineral Resource and Mineral Reserve reporting Standards which IASB determines are needed must be made through CMMI or its successor.
- The proposed Standard should clearly differentiate the current valuation requirements for *fair value* and *value in use*, the former being entirely market related and the latter being entity specific. *Value in use* should conform to existing IASB definitions to take account of account trading connections, contractual arrangements and management attributes and be related to identifiable cash flow units. *Value in use* calculations should not include internally generated goodwill in the cash flows.

Industry Support Needed

The negative attitude of the IASB Steering Committee expressed in the IASC Issues Paper towards disclosure of current value estimates and resource estimates for mineral deposits has considerable momentum. If not reversed, this negative attitude will result in the Extractive Industries IFRS being drafted to allow only historic cost accounting in the primary financial accounts and preventing quantitative disclosure of Resources and other non-Reserve mineralization. Discouragingly, it presently appears that the large majority of submissions received by IASB recommended limiting the extractive industries to historic cost accounting. Even Australasia's Joint Ore Reserve Committee (JORC) has campaigned for only historic cost accounting, which appears to have resulted from a lack of understanding of the relevant accounting and valuation goals, principles and practice (JORC, 2001).

For this negative momentum to be reversed so as to result in a favorable current value accounting outcome based on fair value reporting of Reserves in the primary financial accounts, there will need to be a great increase in interest and involvement from the mining industry, and particularly the petroleum industry at this late date. This must be reflected in moral and financial support for the IVSC's Extractive Industries Task Force's development of an Extractive Industries Guidance section for incorporation in the IVS, their meeting with IASB Steering Committee members during the drafting of the IFRS, and their critiquing of the IASB drafts of the standard(s) when it is published. The author has already made tentative arrangements with the IASB's lead person on this project to meet in London once the results of the analysis of the submissions is available.

A positive outcome from these efforts will provide immense financial benefits for the mining and petroleum industries internationally, especially when compared to the financially depressing alternative. In essentially one coordinated action, this can put in place Reserve-Resource reporting standards, Valuation Standards, and Competent Person requirements, for the mining and petroleum industries, for financial reporting for the securities markets worldwide, and similarly standards for valuations for private and public sector purposes unrelated to company financial reporting.

CONTENT OF THE IVS EXTRACTIVE INDUSTRIES ADDITION

The IVS and IFRS are nonprescriptive standards. They provide principles, concepts and general direction, then expect good judgment, honesty and professionalism in determining how to accomplish the goals. They provide few rules and little in the way of detailed guidance or benchmarks. Selection of this route to developing standards has been a very important philosophical decision regarding how to write the IVS and IFRS.

By comparison, the U.S. GAAP accounting standards are detailed and specific, because U.S. companies and auditors prefer them that way. This prescriptive accounting approach of the U S. GAAP is viewed by some experts as a reason behind some of the recent spectacular accounting disasters such as the collapse of Enron Corporation. In contrasting the two standards development policies, Sir David Tweedie, Chairman, IASB, recently told the U.S. Senate Banking Committee:

> "Companies want detailed guidance because those details eliminate uncertainties about how transactions should be structured. Auditors want specificity because those specific requirements limit the number of difficult disputes with clients and may provide a defence in litigation. Securities regulators want detailed guidance because those details are thought to be easier to enforce.
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> "The IASB has concluded that a body of detailed guidance (sometimes referred to as *bright lines*) encourages a rule-book mentality of "where does it say I can't do this?" We take the view that this is counter-productive and helps those who are intent on finding ways around standards more than it helps those seeking to apply standards in a way that gives useful information. Put simply, adding the detailed guidance may obscure, rather than highlight, the underlying principle. The emphasis tends to be on compliance with the letter of the rule rather than on the spirit of the accounting standard.
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> "We favour an approach that requires the company and its auditor to take a step back and consider whether the accounting suggested is consistent with the underlying principle. This is not a soft option. Our approach requires both companies and their auditors to exercise professional judgement in the public interest. .... There will be more individual transactions and structures that are not explicitly addressed. We hope that a clear statement of the underlying principles will allow companies and auditors to deal with those situations without resorting to detailed rules." (Tweedie, 2002).

In drafting the extractive industries addition to the IVS, the Task Force will have to maintain the same nonprescriptive philosophy, instead including principles, concepts, general direction and goals. Specific instruction, recommendations and examples pertaining to analysis and methods should be kept out of the draft. If the valuer doesn't know what verification, analysis or methods his peers would consider appropriate, he needs to get appropriate experience or education elsewhere. We may look to the CMMI or national mining institutes to provide valuers with more detailed guidance.

The CIMVal Committee has done very good work in laying out the Draft CIMVal Standards so that the document reads easily, embodies the Generally Accepted Valuation Principles and the "Fundamental Principles" from the VALMIN Code, provides the necessary links to the relevant regulations, and ends with a useful "Recommended Table of Contents" for a valuation report. However, it will be difficult to take much material directly from the Draft CIMVal Standards since much is based on Canadian specific definitions and regulations; the Recommended Table of Contents fails the prescriptiveness test; and all other paragraphs would need to be reviewed to assure that they are not too prescriptive.

The Extractive Industries Guidance addition will also need to be structured very differently to the structure used in Draft CIMVal Standards document, though this does not cause any significant change in the application of the valuation principles. The layout will need to follow the same heading structure and style as the other IVS Guidance sections while also fitting within about a 20 page length. Thankfully the CIMVal Committee has already shown us how to keep the document concise. Also, general valuation definitions and concepts are provided elsewhere in IVS and will not be repeated in this section.

Important definitions and rules pertaining to mineral and petroleum properties, such as concise Mineral Resources and Petroleum Reserve definitions and general mineral industry valuation concepts and principles must be included. In particular, the important Competent Person concept for Mineral Reserve and Mineral Resource estimation must be included. Mineral Reserve and Mineral Resource category definitions and the Competent Person definition must be written in such a way that they are not country or mineral institute specific. Rather than including the various comprehensive definitions and tables pertaining to reserves, resources and exploration properties of SPE-WPC and CMMI-UNFC, it seems that they should be listed as important references. However, a review of the IVS shows that IVSC practice is to exclude such comprehensive material entirely. References to such external documents are not used.

Some guidelines should be included to aid the valuer in correctly classifying mineral and petroleum properties into the appropriate Property Types prior to valuation. Mineral and petroleum property holdings are generally real property, while certain interests in them will be considered financial or intangible. An operating mining business or mining company may need to be divided into its real property, personal property and intangible property components before valuation.

Similarly, once the draft extractive industries IFRS becomes available, it will be necessary to provide guidelines within IVS on how to conduct and report valuations to the requirements of that IFRS. It may prove appropriate to incorporate such guidance in the International Valuation Applications, where IVA 1 already covers financial reporting. It may be found that definitions and instructions within that IFRS conflict with or override the equivalent definitions within IVS. For example, the Extractive Industries IFRS could include a more stringent definition of the qualification and experience requirements of a valuator for mineral or petroleum properties.

CONCLUSIONS

Mineral industry institutes in countries such as the U.S. and South Africa should cease their initiatives to develop national valuation standards for mineral properties. Instead they should support the efforts of the International Accounting Standards Board and the International Valuation Standards Committee to develop extractive industries standards for inclusion with their existing standards. The IASB's International Financial Reporting Standards and the IVSC's International Valuation Standards are rapidly achieving complete global coverage and will likely make national valuation standards largely irrelevant within just a few years.

Based on tentative views expressed against resource reporting and current value accounting in the IASC Extractive Industries Issues Paper, and that a majority of submissions received favored historic cost accounting, it is likely that the IASB's Extractive Industries Steering Committee is disinclined to allow current value accounting in the Extractive Industries with fair value reporting for mineral and petroleum reserves. Due to this, the mining and petroleum industry companies will be handicapped relative to almost all other financial sectors, due to their stock prices being relatively depressed because of the historic cost accounting rules.

Mining and petroleum companies have not yet provided IVSC with any sponsorship for its Extractive Industries Task Force's effort to develop the IVS Extractive Industries Standard and the submissions to the International Accounting Standards Board on the development of the Extractive Industries International Financial Reporting Standard. Mining and petroleum industry companies should financially support the IVSC and its Extractive Industries Task Force to help assure a favorable outcome for the industry from these standards development initiatives. The author is hopeful that through IVSC's cooperation with the IASB's Extractive Industries Steering Committee, the outcome will be a favorable current value Extractive Industries International Financial Reporting Standard.

The author has provided his initial suggestions regarding the appropriate content for the IVS Extractive Industries Guidance addition. He has also proposed that the Council of Mining and Metallurgical Institutions and the World Petroleum Congresses develop supplemental valuation guidelines to support the IVS. National mining institutes should adopt the IVS and develop disciplinary procedures for members who violate the Standards. National mining and petroleum institutes or national regulatory bodies may find it beneficial to develop supplemental guidelines for application of the extractive industries valuation standards in their country.

Problems have arisen within South Africa due to the impending cutoff of 30 September 2003 on Valuation of mineral properties for capital gains tax purposes. The problem is due to the lack of an enforceable mineral property valuation standard within the country. The author suggests that SAIMM consider immediately adopting IVSC's International Valuation Standards and making it binding on its membership. Despite the fact that IVS does not yet contain specific instructions for extractive industries valuation, the author expects that most mineral property valuations can satisfactorily be performed under the existing Real Property Valuation provisions. The instructions for the other Property Types should also be found satisfactory. The author expects the existing IVS will be found superior for this purpose to the Uniform Standards of Professional Appraisal Practice that he has applied to mineral property valuation in the U.S. for many years, which also has no specific instructions for the extractive industries.

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