

FROM THE CAPITAL

Bad habits hurt disclosure practices

Hit and miss regulation makes it tough for investors to reserve judgement

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Up and coming lithium miner Pilbara Minerals was pulled up by the Australian Securities Exchange for a disclosure lapse in one of the exchange's pet areas, while more serious gaps remained in the sometimes patchy oversight of ASX company reporting.

On June 2, Pilbara Minerals announced a 32% increase to 23.83Mt in its Pilgangoora tantalum-lithium resource in Western Australia. The following day the company was forced to acknowledge that its earlier release had not conformed to the requirements of the exchange.

As always, in these circumstances, interest lies in what amendments the regulator had required and, from that, how the company might have misled readers of the original release.

In this case the apparently offending material had referred to the company's exploration target. An upgraded target of 50Mt-60Mt, the company said on the first page of its initial filing, was enough to demonstrate that "it is on track to delineate a globally significant hard-rock lithium-tantalum deposit".

Later in the announcement, the company did detail the basis on which the exploration target had been adjusted. The problem would have arisen because the statement on the first page of the 36-page announcement was not directly accompanied by any supporting information about the nature of the exploration effort justifying the conclusion. Nor was there a warning about the risks of relying on an exploration target.

In this instance, investors would have little reason to recast conclusions they might have drawn from the first version of the announcement. The exploration target was retained as originally quantified.

The assertion by the company's chief executive that the exploration target "gives investors a good indication of its potential as one of the world's largest and highest-grade hard rock lithium deposits" remains intact in both versions on the public record.

Ironically, the only benefit from the lapse and subsequent intervention seems to have accrued to the company. It was able to make the same announcement heralding its exploration success twice while its share price rose 30% between June 2 and 5.

A closer look at the Pilbara Minerals releases over these few days suggests the



regulator could have paid attention to matters with a greater potential effect on investment decisions.

One of the documents the company had to amend and reissue referred to its Tabba Tabba tantalum project, where production is due to start imminently.

The company now claims the project will generate an EBITDA of A\$18 million (US\$14 million) in its first year. That is a big leap from prior references to the anticipated financial performance of the project based on a February 2014 feasibility study.

The study outlined a mine life of 19 months to deliver a total EBITDA of A\$16 million. There has been no explanation by the company as to how the profit rate has been able to increase by 75%. New numbers have simply been substituted for the old numbers in a presentation.

The company continues to refer prominently to having a five-year offtake agreement. Doubtlessly such an agreement exists, but the Pilbara Minerals has a sufficient mining reserve for only 18 months of production. Most recently, the company has referred to "its excellent potential to increase project reserves to at least a five-year mine life".

The squeamishness of the ASX over unsupported statements about exploration targets has not extended to these even more nebulous and less well documented statements about reserves critical to the company's financial outcomes.

There are other examples in reporting practices of companies defining their own disclosure paths.

The 2012 JORC code, to which ASX requires adherence, asks companies publishing reserve estimates to explain the source and confidence of the economic inputs going to produce a net present value. It also calls for companies to disclose the ranges and sensitivity of the NPV to variations in the signifi-

cant assumptions and inputs.

South Boulder Mines (recently renamed Danakali Limited) released its maiden ore reserve estimate for the Colluli potash project in Eritrea on May 19, 2015. The South Boulder personnel completing the submission explicitly addressed the requirements of the JORC Code requiring information about the economic analysis underpinning the reserve calculation.

The company referred to the impact of differing tax regimes on the valuation and the expected effect on the NPV of changes to a range of factors to which the project valuation is most sensitive.

The South Boulder approach contrasted with the way Northern Minerals reported its ore reserve for the Browns Range rare-earth project in Western Australia on March 2, 2015.

The company did not provide any sensitivity analysis. Nor did it even qualitatively identify any of the inputs to its valuation.

On the same day, Northern Minerals released a document in which it claimed a 24% increase in the NPV of the project.

The company attributed the improvement to an extended mine life and lower costs. There was no mention among the cited reasons for the valuation increase that the company had used a materially different exchange rate assumption, which could have accounted for the entire increase in the declared value of the project.

The precise impact of the exchange rate change is unclear because the company has not disclosed the sensitivity of the valuation to changes in the exchange rate despite being required to do so in order to be compliant with the JORC code.

The South Boulder and Northern Minerals disclosure approaches are so different it is hard to imagine them being a response to the same guidelines.

The same quality control is not policed across the full range of disclosure requirements.

Financial constraints will compel regulators to make choices about the disclosure rules policed most actively. One consequence of having to make these choices is the rising risk of bad habits proliferating where less rigorous surveillance is the norm.

Ideally, the choice of where to shine a light should match where investors are most likely to be misled or where the likely costs are greatest. ▼