

HARD MINERALS DUE DILIGENCE

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Due diligence is more than simply checking land titles. A due diligence investigation is the objective evaluation of a number of legal, land and other areas of a property or business targeted for acquisition, merger or other business arrangement. The examination is performed by a task force composed of attorneys, landmen and other specialists. What is investigated and the detail of the investigation is a function of the particular characteristics of the transaction for which the due diligence is being conducted. The primary duty of the task force is to identify existing and potential problems and the means by which the target business can be more efficient and therefore more profitable. All task force members should advise member attorneys of every possible legal problem they discover.

Quite often, the practical matter of how much time is available determines how the due diligence will be performed. Generally, the less time the examiner has to conduct his due diligence, the more important it is to prioritize the conduct of the investigation with respect to certain parcels of land. Every effort should be made to thoroughly research each parcel of land, but the plain fact that time is short may require the due diligence effort be focused on the most important lands.

Regardless of the time element, frequent communication with other members of the due diligence task force and one's team members is essential. Good communication among task force members is necessary for a thorough, balanced due diligence evaluation. Above all, an investigator should know what is important to his client/employer. The investigator's objective is to address the client's concerns and evaluate all aspects of the target business so the client can make a well informed decision regarding the merits of completing the transaction.

The client/employer relies on the good judgment of the due diligence examiners and expects every examiner to provide an accurate assessment of his area of responsibility. The examiner must always advise the client/employer of any circumstance or condition that prevents or substantially hinders the examiner from adequately performing his investigation. The due diligence examiner also owes the client and the seller/owner of the property or business the obligation to treat all information he obtains during his investigation in a confidential manner. Attorneys' ethics are governed by state law and bar associations, and the American Association of Professional Landmen (AAPL), Denver Association of Petroleum Landmen, Nevada Landman's Association and Rocky Mountain Association of Mineral Landmen all have by laws requiring their members to practice good ethics. The examiner should also become familiar with the meaning of terms that convey title in the state in which the lands are located before beginning his review of deeds. He should also know the state's title standards. Finally, the name "Due Diligence" is very appropriate. Attorneys, landmen and the other members of the task force owe their client/employer the duty of diligently pursuing the investigation, identifying deficient areas, and promptly notifying the client of any material problem.

The due diligence examiner should:

1. Verify Title Chains. All real property title records should be reviewed. Besides public records in the courthouse, federal and state agencies, landman and attorneys should identify the

location of all land records and review any abstracts, title insurance policies, title reports and other title information regarding the subject lands and other real property. The exceptions listed in title insurance policies should be closely reviewed. The landowner's landmen, property records staff and attorneys should be interviewed. They usually know the various locations of the land records and title information and may know valuable information about a property that is not described in any record. Pay particular attention to reservations of all types contained in deeds. Reservations of minerals, water, easements, rights of way and royalties must be identified. In practice, it is usually not advisable to rely entirely on title insurance policies regarding mineral matters. The title to patented lands with the highest mineral potential should, therefore, be independently verified. If time is short, this verification can be limited to a "spot check" of the information in the policies. This will indicate the degree of the title company's familiarity with mineral titles, accuracy of its mineral title information, and whether additional individual title verification is necessary.

2. Review Agreements. All recorded and unrecorded agreements in the title chain should be closely reviewed. Are releases recorded for all prior recorded lease agreements? If a property is subject to an existing contract for its purchase and sale, the seller should be interviewed regarding real or perceived problems to identify possible or probable conditions of default and other contractual issues.

3. Identify Problems and Areas Where Improvement is Possible. Be aware of any problem or condition that affects activities on the mine properties. The current status of the title to lands, easements, rights of way, contracts, existing permits, the need for new permits, transportation of the mine product, organization and utilization of the mine's work force, contracts for the mine's power supply and water rights must all be evaluated. Any problem or recommendation to improve efficiency in any area should be reported.

4. Be Sensitive to Environmental Problems. Landmen are often the first ones on a property. Therefore, while not environmental specialists, they should be able to recognize conditions that may be hazardous or require future remediation. The possibility of any such condition should be immediately reported to the leader of the task force's environmental team.

5. Communication and Organization. A due diligence investigation is an exercise of good judgment and interfacing with members of the task force and one's team. As soon as possible, all members of the task force should be given specific times to complete assignments. This schedule may include intermediate times for the completion of phases of the due diligence investigation. The task force should be well organized and have a clear chain of command with one individual in charge, usually an officer of the client/employer. It typically consists of number of teams, with each team having a specific area of responsibility. Common areas evaluated by the task force are:

- Environmental
- Finance - Corporate Accounting
 - Tax considerations for structuring the transaction
- Geology
- Human Resources
- Hydrology
- Land - Identify all encumbrances
 - Easements and Rights of Way
 - Conditional uses contained in contracts and permits

Reservations
Severed surface and mineral estates
Other encumbrances

- Legal
 - Labor law
 - Liabilities of any type
 - Contracts
 - Corporate Matters
 - Titles - Land, water, fixtures, vehicles and other Personal Property
- Mining engineering - Mine Plan, Mine Operations and Mill
- Other areas of Technical Expertise
- Permits – Are there any foreseeable permitting problems?

Every task force member should clearly understand his or her individual responsibilities and communicate facts during the investigation that he or she believes may be useful to his team members and his team leader. Periodic meetings of team leaders, and sometimes all team members, is necessary to ensure the investigation is well coordinated and completed on schedule. Weekly meetings are common, but the frequency of meetings are determined by the particular characteristics of each transaction. Near the end of the investigation, team members should submit individual reports of their findings to their respective team leader, who in turn furnishes a report to his immediate task force supervisor. It is the author's opinion that it is best for the client/employer to have one comprehensive due diligence report presented by the task force leader to management. One final report facilitates decision-making. The report may be either an executive summary prepared by the task force leader with the team reports attached, or a new report prepared by the task force leader that is a compilation of information in the team reports.

Typical areas that are investigated during a due diligence investigation are attached at the end of this paper. There is a lot to check and verify. Therefore, these lists are only guides. It will not be necessary to review all the areas for every due diligence exercise, and areas that are not listed may require examination under certain circumstances. It is important to remember that every due diligence exercise is unique, and the decision of exactly what to investigate must be determined on a case-by-case basis.

SELECTED MINING DUE DILIGENCE REFERENCES

Generally, all manuals for the Mineral Title Examination Special Institutes, I through III, by the Rocky Mtn. Min. L. Fdn., 1977, 1982 and 1991, respectively, are excellent references to numerous issues and problems the attorney and landman will encounter while performing due diligence. The primary reference regarding mining due diligence is:

Dean R. Massey, Due Diligence in Modern Mining Deals: How to Protect Your Client from Buying a Pig in a Poke, 33 Rocky Mtn. Min. L. Inst., 33-1 (1985).

Other specific references are listed below:

DUE DILIGENCE

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Sitzman, Sylvia J., Utilization of Bureau of Land Management Records, Natural Resources for Legal Assistants and Land Support Personnel Special Institute Manual, Rocky Mtn. Min. L. Fdn., NRLA-9 (1979).

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HARD MINERALS DUE DILIGENCE

GENERAL CHECKLIST FOR LAND AND MINING CLAIMS

RECORDS CHECKED: Company _____ County _____ State _____ Federal _____

OWNERSHIP

Record Owner vs. Title Owner: - Are all necessary instruments recorded?
Mineral Reservations.
Royalties: Primary and Overriding.

EASEMENTS AND RIGHTS OF WAYS

Identify all existing easements and rights of way across private and public lands, including, but not limited to those for roads, electrical transmission lines and water pipelines. Note any rights that terminate at the end of a definite term or upon the cessation of use.

TAXES

Are all real and personal property taxes current?
Are there any tax liens of record?

LIENS

Are there any mechanic's and materialman's liens of record?

LEASES / ENCUMBRANCES

Are there any unreleased leases, rights, or other agreements encumbering the property?

MORTGAGES / LOANS

Are there any unreleased mortgages, loans, promissory notes or other monetary obligations?

LITIGATION, LIS PENDENS, JUDGMENTS

Are there any existing or pending legal actions against the landowner filed in county or federal courts? Are there any judgments of record?

SECRETARY OF STATE

The Secretary of State's office in states where property is located, and states where corporate landowners are incorporated and doing business, must be checked for service of process and corporate status. Are corporate landowners in good standing?

BANKRUPTCY COURT

Bankruptcy courts for the regions where the landowner is located and doing business should be checked to confirm the landowner is not bankrupt.

WATER RIGHTS

Are all water rights valid?

Is registration or similar state statutory requirement?

Contact the state agency responsible for water rights.

Search appropriate state and county records to verify rights and identify any prior, superior rights.

UNPATENTED MINING CLAIMS

Was the public domain land open for location when the claims were located?

Identify the locator(s) of the claim(s).

Do the forms of the Location Certificates and Affidavits of Labor comply with U.S. and state law?

Were the Location Certificate and Affidavits of Labor recorded in the county and filed with the BLM in a timely manner?

Was good assessment work performed? Does it satisfy statutory requirements?

If applicable, has the \$100 claim Holding Fee in lieu of Assessment Work been paid?

If the \$100/claim holding fee was paid, was it paid to the BLM on or before August 31, 1993, or as subsequently required by later law?

What conflicts, if any, exist with third party claims?

Are there any multiple uses or limitations of activities on U.S. lands such as grazing permits or wildlife considerations that will interfere with activities on the subject properties?

FIELD INSPECTION

A field inspection of the subject property is a necessity. The status on the ground of unpatented lode mining claim monumentation and actual location, plus the existence of recently located conflicting third party claims is particularly important. The inspector should note any condition of concern to the client/employer, such as noncompliance with applicable reclamation laws, existence of wetlands, evidence of hazardous substances not being handled properly, or any situation that could involve groundwater contamination. Any of the foregoing circumstances should be immediately reported to the proper team leader or leaders.

ACKNOWLEDGMENTS

Are the acknowledgments on all agreements, affidavits of labor and other instruments legally correct, considering the state in which the property or properties are located and the actual jurisdiction in which the instrument was signed?

PERMITS, LAND USE & ZONING

Are all permits current, including those for mine plans, rights of way, easements, and environmental concerns?

Are there any restrictions or zoning requirements that may inhibit operations?

Does the local government pose any threat to the operation?