



**MEDUSA MINING LIMITED**

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13 October 2016

**Chris Bailey**

Adviser

ASX Listings Compliance (Perth)

ASX Compliance Pty Limited

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Dear Chris

**Medusa Mining Limited (ASX Code: MML) (Medusa or the Company): 2016 annual report and qualified audit opinion**

We refer to your letter dated 5 October 2016 regarding the Company's 2016 annual report lodged with the Australian Securities Exchange (**ASX**) on 2 October 2016 (**Annual Report**) and the qualified opinion provided by the Company's auditor on page 118 of the Annual Report (**Qualified Opinion**). A copy of your letter is **enclosed**.

Our responses to the questions set out in your letter are as follows:

1. ***Commenting specifically on the Qualified Opinion and the Updated Resources and Reserves Statement, can the Company confirm that in the Directors' opinion the Annual Report:***

***(a) complies with the relevant Accounting Standards; and***

***(b) gives a true and fair view of the financial performance and financial position of the Company?***

The Company confirms that, in the opinion of the directors of the Company (**Directors**), the consolidated financial reports contained in the Annual Report:

(a) comply with the relevant Accounting Standards; and

(b) give a true and fair view of the financial performance and financial position of the Company as at 30 June 2016,

despite the Qualified Opinion.

## 1.1 The Qualified Opinion and the auditor's reasons for it

As you know, for the purposes of your letter, the nature of the Qualified Opinion relates to the receipt of the "Annual Mineral Resources and Ore Reserves Update Statement", received by the Company and lodged with ASX on 28 September 2016 (**Updated Resources and Reserves Statement**), and the Company's independent auditor stating that they were not provided with "sufficient appropriate audit evidence" or "sufficient time to assess the impact" of the Updated Resources and Reserves Statement on the carrying value/recoverable amount of certain assets.

The Directors maintain their opinion that the financial statements in the Annual Report both complied with the relevant Accounting Standards and gave a true and fair view of the financial performance and financial position of the Company as at 30 June 2016 (and set out above) for the following reasons:

- (a) The carrying value of the asset was correctly recorded using the requirements of the applicable Australian accounting standard (AASB 136 *Impairment of assets*) The Company had in the prior year adopted a very conservative approach to determining the asset's recoverable amount, since that date the outlook for the company's operation has improved with the successful roll out of the E15 improvements that will see greater efficiencies and faster production, and the improvement in the gold price. The recoverable amount has been determined using the "worst case" case mine plan, and includes no expected upside arising from extending the mines life from the discovery of future resource.

The updated resource statement did not provide any information that contradicted the mine plan or the director's determination of the assets recoverable amount determined in accordance with AASB 136 using VIU (value in use). The resource statement largely was a simple calculation of information reducing the original reserve by the known mined amounts and the result of not replenishing the resource following on from our delayed infill drill program

- (b) The receipt of the Updated Resources and Reserves Statement does not constitute a "an event after the reporting date" for the purposes of Australian Accounting Standard AASB 110 "Events after the Reporting Period" (**AASB 110**). This means that even if the auditor had "sufficient appropriate audit evidence" in relation to, or "sufficient time to assess the impact" of, the Updated Resources and Reserves Statement, that would have **no impact on the validity of the value ascribed to the Company's property and assets as at 30 June 2016**.
- (c) Even if the Company were to accept that receipt of the Updated Resources and Reserves Statement is in fact a "an adjusting event after the reporting period" under AASB 110 (which, as noted above, it does not), the information contained in that statement does not represent an impairment trigger under Australian Accounting Standard AASB 136 "Impairment of Assets" (**AASB 136**). This means that no further impairment testing is required flowing from the information in the Updated Resources and Reserves Statement and again, there is **no impact on the validity of the value ascribed to the Company's property and assets as at 30 June 2016**.

The Company will address these reasons in more detail below.

## 1.2 No impact on the determination of the mine's recoverable amount

The Company has received external, independent accounting advice that the receipt of the Updated Resources and Reserves Statement has no impact on determining the mines recoverable amount under AASB 136. Accordingly, from an Australian Accounting Standards perspective, the Updated Resources and Reserves Statement **has no impact on the validity of the value ascribed to the Company's property and assets as at 30 June 2016 applying AASB 136**.

In order to be a "subsequent event" for AASB 110 purposes, the Updated Resources and Reserves Statement must represent an event that gives further information (either favourable or unfavourable) about Medusa's assets.

It is the Directors' opinion that the Updated Resources and Reserves Statement does not represent new or further information (received after the 30 June balance date) as to the applicable assets (and the Company's estimated life of mine plan (**LOM Plan**) or budgets). The Updated Resources and Reserves Statement reflects the impact of the mined quantities of ore and the impact of not completing its infill drill program, both of which were known to Directors as at 30 June 2016. Accordingly, for the purposes of AASB 110, the Updated Resources and Reserves Statement is neither:

- (a) an "adjusting event after the reporting period"; nor
- (b) a "non-adjusting event after the reporting period",

as it does not represent further information not already known to Directors as at 30 June 2016, when the financial accounts were being prepared.

### 1.3 **No impairment trigger or impact in any event**

Even if it was accepted that the Updated Resources and Reserves Statement constituted an "adjusting event after the reporting period" (and the Directors do not think this is so, see section 1.2), the information contained in that statement does not represent "negative information". As such, it does not give rise to an impairment trigger under AASB 136 and no further impairment testing is required.

The Company and its independent advisers have formed this view, having regard to the further work done by Medusa as described below at paragraphs 1.3(a) to 1.3(e). In short, this further work suggests that the Updated Resources and Reserves Statement does not lead management to believe that there would be a change to the LOM Plan. In addition, the Directors consider that further impairment write-downs of the assets related to the Co-O Mine are **not** appropriate.

To explain in more detail:

- (a) The Directors confirm that the Company's property and assets, as at 30 June 2016, have been measured according to the requirements of AASB 136 and that its recoverable amount as at 30 June 2016 was determined in accordance with its value-in-use impairment model (**VIU Model**), using the LOM Plan.
- (b) The Company has adopted a conservative approach with its current LOM Plan on which the VIU Model has been based. This VIU Model is considered by management to be a "base case" model. In addition, an asset impairment write-down was recorded by the Company for the year ended 30 June 2015, which was done following adoption of what the Company considered to be a conservative impairment testing methodology and approach.
- (c) Due to:
  - (i) a downward trend in the Company's all-in sustaining costs (see pages 4 and 100 of the Annual Report, by way of example), attributable in part to the completion of the expansion program on the E15 Project to sink a new access shaft (**E15 Project**); and
  - (ii) sustained (and rising) gold prices during 2016,

management prepared a high level VIU Model to ensure that no further impairment in the assets of the Co-O mining operation (**Co-O Mine**) were required under AASB 136 at the time of preparing the 30 June 2016 Annual Report and for the purposes of the audit.

- (d) Since the release of the Annual Report, the Directors have obtained independent accounting advice that the recoverable amount using the VIU Model is best derived from the most conservative option under the LOM Plan, with certain adjustments to be made consistent with the requirements of AASB 136 (this revised VIU Model, including these adjustments, is the **AASB 136 VIU Model**), principally to reflect the finite life of the mine, the consumption of stores and the sale of the mill and to use a more conservative discount rate. The adjustments contemplated by the AASB 136 VIU Model, to calculate the mines' recoverable amount (using the value-in-use method), were to reflect a finite life of mine and the utilisation of a more conservative discount rate, among other things.
- (e) The Company, with assistance from the independent accountants, has considered the carrying value/recoverable amount of assets using the revised AASB 136 VIU Model, the applicable carrying values reported in the Annual Report and information contained in the Updated Resources and Reserves Statement.

Following this review, and taking into consideration the conservative approach adopted with respect to the 2015 impairment charge (described above in paragraph 1.3(b)), we do not consider any further impairment write-downs of the assets related to the Co-O Mine are appropriate.

After considering the matters set out in paragraphs 1.2 and 1.3 above, the carrying value of assets in the Annual Report were **correctly determined in accordance with Australian Accounting Standards**, and are also **true and fair**.

2. ***Given the Qualified Opinion relates to the Auditor's inability to obtain sufficient appropriate audit evidence to assess the impact of the Updated Resources and Reserves Statement on the recoverable amount of a number of the Company's assets, what steps does the Company intend to take to obtain an unqualified audit/review report for future financial periods?***

The Company confirms that the Qualified Opinion was given by reason of late receipt of the Updated Resources and Reserves Statement. The Company considers this to be an anomalous occurrence, so it believes that it will be able to obtain an unqualified audit/review report in future periods.

The Company is committed to timely and fulsome disclosure, in compliance with its obligations under the ASX Listing Rules and *Corporations Act 2001* (Cth) (**Corporations Act**). Accordingly, following the issuance of a Qualified Opinion, the Company has already undertaken the following:

- (a) (**reconciliation**) A detailed reconciliation of the VIU Model to its latest LOM Plan This reconciliation exercise provides a comprehensive basis for allowing an auditor to test all assumptions underlying the VIU Model and therefore will, in the Directors' opinion, represent sufficient and appropriate audit evidence upon which an auditor will be able to issue an unqualified report going forward.
- (b) (**LOM Plan update**) The Company has engaged a third party expert to assist with updating its LOM Plan for the latest Updated Resources and Reserves Statement. This updated LOM Plan will be provided to our auditors.
- (c) (**updated information received**) The Company notes that the Updated Resources and Reserves Statement has now been received and the reconciliation referred to above has been done, so the Company is well placed to be able to provide its auditors with sufficient and appropriate audit evidence to receive an unqualified audit/review report in the coming year. To that end, the Directors believe that the Company is well positioned to have its information processes in place to receive unqualified audit/review reports going forward;
- (d) (**independent advice**) As mentioned above, Medusa has also engaged an independent accounting firm to assist with the review of its internal processes, to ensure adequate and

appropriate information is available on a timely basis to allow for future unqualified audit/review reports.

In particular, Medusa has obtained advice in relation to preparing the AASB 136 VIU Impairment Model and the Company intends to prepare its annual impairment model for the purposes of meeting the requirements of AASB 136 on this basis for future reporting periods.

The Company notes that, to its knowledge, this is the first time the Company has received a qualified audit opinion in the nature of the Qualified Opinion. The Company has also had discussions with its competent persons, so as to ensure the timely receipt of future update resources and reserves statements.

The Company considers that these steps are adequate to minimise the risk of future qualified audit/review reports.

3. ***How has the Company satisfied itself as to the recoverable amount of the Company's assets referred to in the Updated Resources and Reserves Statement?***

As mentioned above, the Company has engaged an independent accounting firm, following receipt of the Qualified Opinion, to assist with assessing the appropriateness of its impairment model (that is, the VIU Model) for the Co-O Mine assets. Among other things, this will assist with determining the impact of the disclosures in the Updated Resources and Reserves Statement on the carrying value/recoverable amount of its asset, namely:

- (a) the decrease in Mineral Resources at the Company's Co-O Mine from:
  - (i) 3.50 million tonnes at a grade of 10.2g/t for a total of 1.15 million ounces contained gold as at 30 June 2015; to
  - (ii) 2.77 million tonnes at a grade of 10.8g/t for a total of 0.96 million ounces contained gold, as disclosed as at 30 June 2016; and
- (b) the 12% decrease in Probable Ore Reserves at the Company's Co-O Mine as at 30 June 2016, when compared to 30 June 2015.

To that end, the Company notes that:

- (a) as described above, the fall in Reserves referred to in ASX's letter are almost entirely due to the mining of ore in 2016 and the delays in completing the Company's infill drill program, which resulted from the Company focusing its efforts on the E15 Project, including sinking a new shaft intended to improve efficiency of the mining operation by up to 30%. The E15 Project meant that the drill campaign did not commence until April 2016, and was not finalised at 30 June 2016 so as to be included in the Updated Resource and Reserves Statement.

The Company has previously disclosed its progress with the E15 service shaft, and any delays associated with this, in an ASX announcement dated 9 April 2015, its Quarterly Activities Reports for the periods ended 31 March 2016 and 30 June 2016 and its 2015/2016 financial results released on 30 August 2016, among others.

- (b) Over the 10 year operation of the mine, Medusa has a continued track record of both converting Inferred to Measured Resources and extending the mine life through the replenishment of the resource from infill drilling. At this stage the Updated Resources and Reserves Statement has not lead to any material change in the LOM Plan.

In terms of satisfying itself as to the recoverable amount of the Company's assets, following receipt of the Updated Resources and Reserves Statement:

- (a) As is normal practice, and as mentioned in paragraph 2(b) above, management is in the process of entering the revised information from the Updated Resources and Reserves Statement into the LOM Plan. At this stage, management have no concerns that this will have a significant impact on the LOM Plan.
- (b) As mentioned in paragraph 1.3(d) above, the Company, with assistance from the independent accountants, has considered the carrying value/recoverable amount of assets using the AASB 136 VIU Model and information contained in the Updated Resources and Reserves Statement and does not consider any further impairment write-downs of the assets related to the Co-O Mine are appropriate.

Even after considering the Updated Resources and Reserves Statement, the carrying values/recoverable amounts set out in the Annual Report remain appropriate.

4. ***Does the Company consider that its level of operations is sufficient to warrant continued quotation of its securities on ASX in accordance with the requirements of listing rule 12.1? In answering this question, please also explain the basis for this conclusion.***

Yes. Medusa has been admitted to the official list of ASX since 23 December 2003 and has actively continued its mineral exploration and development and gold mining/production operations since that time.

Listing Rule 12.1 provides that the level of Medusa's operations must, in ASX's opinion, be sufficient to warrant the continued quotation of Medusa's securities and its continued listing.

To elaborate, and by way of example:

- (a) **(continued operational activity)** As disclosed in the Annual Report:
  - (i) the Company continues to increase production, and produced 108,578 ounces of gold for the year ended 30 June 2016 (compared to 98,359 ounces from the previous corresponding period) at an average recovered grade of 6.40 g/t gold;
  - (ii) the Company's exploration activities continue, with exploration expenditure, inclusive of underground diamond drilling, at US\$9.3 million; and
  - (iii) there have been a number of management changes resulting in strengthened leadership of the Company, including the appointment of Mr Boyd Timler as Chief Executive Officer on 21 March 2016 and Mr Roy Daniel as Non-Executive Director on 25 November 2015.
- (b) **(continued revenue growth)** Following on from the sustained operational activity noted above, the Company's revenues continue to grow, achieving revenues of US\$128.1 million for the year ended 30 June 2016, compared to US\$123.0 million for the previous corresponding period.
- (c) **(increased profit)** The Company also made a net profit (attributable to members) of approximately US\$43,792,000, compared to a loss for the previous corresponding period.

Also as disclosed in the Annual Report, the financial year ended 30 June 2016 was a year in which the Company positioned itself for future growth, having completed an operational review, and progressed mine infrastructure projects to increase production.

The Company believes that its level of operations will satisfy Listing Rule 12.1 requirements.

5. ***Is the Company of the view that the financial condition of the Company would be sufficient to warrant continued listing on ASX in accordance with the requirements of listing rule 12.2?***

Yes. See reasons set out in our response to questions 4 and 6.

6. ***If the answer to questions 4 or 5 is "Yes", please explain the basis on which the Company has formed the conclusion that the financial condition of the Company is sufficient to warrant continued listing on ASX in accordance with the requirements of listing rules 12.2. Specifically, the Company should submit the reasons (including any previous disclosures made to the market) it considers relevant given the matters outlined in the Independent Auditor's Review Report resulting in the Qualified Opinion.***

Listing Rule 12.2 states that Medusa's financial condition (including operating results) must, in ASX's opinion, be adequate to warrant the continued quotation of its securities and its continued listing.

The nature of the Qualified Opinion was directly in terms of the auditor being able to obtain sufficient and appropriate audit evidence as to property, plant and equipment of US\$53.06m and development expenditure of US\$108.61m. It does not strictly relate to whether the Company is a going concern. This is consistent with the consolidated financial statements to which the Qualified Opinion relates, which made no indication as to going concern issues.

The Directors' maintain the opinion expressed in the Directors' declaration on page 117 of the Annual Report, where they confirmed that "there are reasonable grounds to believe that the Company will be able to pay its debts as and when they become due and payable".

7. ***If the answer to question 4 or 5 is "No", please explain what steps the Company has taken, or proposes to take, to warrant continued listing on ASX in accordance with the requirements of listing rules 12.1 and 12.2.***

Not applicable.

8. ***Please confirm that the Company is in compliance with the listing rules and, in particular, listing rules 3.1 and 12.2.***

The Company confirms that it is in compliance with the Listing Rules, in particular, Listing Rules 3.1 and 12.2.

Yours faithfully



**Peter Alphonso**  
Company Secretary



5 October 2016

Mr Peter Alphonso  
Medusa Mining Limited  
Suite 10, 100 Mill Point Road  
South Perth WA 6151

*By Email*

Dear Mr Alphonso

**Medusa Mining Limited (the “Company”)**

ASX Limited (“ASX”) refers to the following:

1. The Company’s announcement titled “Annual Mineral Resources and Ore Reserves Update Statement” lodged with ASX on 28 September 2016 (“Updated Resources and Reserves Statement”) which discloses, inter alia, the following:

*“Total Indicated and Inferred Mineral Resources for the Co-O Mine are now estimated at 2.77 million tonnes at a grade of 10.8 g/t gold for a total 0.96 million ounces contained gold, compared to the 30 June 2015 estimate of 3.50 million tonnes at a grade of 10.2 g/t gold for a total 1.15 million ounces contained gold (Table I)” (at page 1); and*

*“A comparison between the current Ore Reserves and that stated for 30 June 2015 shows a net decrease in Probable Ore Reserves of 12% or 51,000 ounces contained gold” (at page 2).*

2. The Company’s Annual Report for the year ended 30 June 2016, lodged with ASX on 2 October 2016 (the “Annual Report.”)
3. The Independent Auditor’s Report set out on pages 118 to 120 of the Annual Report which contains a Qualified Opinion (the “Qualified Opinion”), stating the following:

***Basis for Qualified Opinion***

*Carrying value of property, plant and equipment and development expenditure:*

*The Company originally released its audited financial accounts on 30 August 2016. The Company has reported a total carrying value of property, plant and equipment of US\$53.06m (Note 11) and development expenditure of US\$108.61m (Note 12) as at 30 June 2016. Australian Accounting Standard AASB 136 Impairment of Assets requires an asset to be carried at no more than its*



*recoverable amount. The audit report included an emphasis of matter relating to the disclosures included in Notes 1(x) and Note 13 which outlined that the Company estimates its ore reserves and mineral resources based on information compiled by Competent Persons in the Annual Mineral Resources and Ore Reserves Update Statement (the “Statement”) and that the last Statement was released in September 2015. The determination of ore reserves and remaining mine life affects the estimate of the recoverable amount of a number of the Company’s assets including the deferred mining costs. At the date of our original audit report, an updated Statement had not been completed.*

*On 28 September 2016, subsequent to the signing of the original financial accounts, the Company released its updated Competent Persons Statement to the market. The updated Statement includes a 12% decrease in probable ore reserves and 16% decrease in total resources. On 30 September 2016 the Company has provided a revised value in use model to assess recoverable amount which includes these updated reserve and resource amounts and other changes in assumptions. As at the date of this report we have not been provided with sufficient appropriate audit evidence nor had sufficient time to assess the impact of these updates on the estimate of the recoverable amount. In the event that the carrying value of these assets exceeds their recoverable amounts, it would be necessary for the assets to be written down to their recoverable amounts.*

## **Relevant listing rules and guidance**

ASX also refers to the following:

- Listing rule 3.1, which requires an entity, once it becomes aware of any information concerning it that a reasonable person would expect to have a material effect on the price or value of the entity’s securities, to immediately tell ASX that information.
- Listing rule 12.2, which states that an entity’s financial condition (including operating results) must, in ASX’s opinion, be adequate to warrant the continued quotation of its securities and its continued listing.
- Listing rule 19.11A, which requires accounts given to ASX under the requirements of the listing rules, to be prepared to Australian accounting standards and if the entity is a foreign entity, the accounts may be prepared to other standards agreed by ASX.
- Listing rule 3.1A sets out an exception from the requirement to make immediate disclosure, provided that each of the following are satisfied.

*“3.1A.1 A reasonable person would not expect the information to be disclosed.*

*3.1A.2 The information is confidential and ASX has not formed the view that the information has ceased to be confidential.*

*3.1A.3 One or more of the following applies.*

- *It would be a breach of a law to disclose the information.*

- *The information concerns an incomplete proposal or negotiation.*
- *The information comprises matters of supposition or is insufficiently definite to warrant disclosure.*
- *The information is generated for the internal management purposes of the entity.*
- *The information is a trade secret.”*

### Questions for response

In light of the information contained in the Annual Report, and referring to the listing rules above, we ask that you answer the following questions in a format suitable for release to the market in accordance with Listing Rule 18.7A.

1. Commenting specifically on the Qualified Opinion and the Updated Resources and Reserves Statement, can the Company confirm that in the Directors’ opinion the Annual Report:
  - (a) complies with the relevant Accounting Standards; and
  - (b) give a true and fair view of the financial performance and financial position of the Company?
2. Given the Qualified Opinion relates to the Auditor’s inability to obtain sufficient appropriate audit evidence to assess the impact of the Updated Resources and Reserves Statement on the recoverable amount of a number of the Company’s assets, what steps does the Company intend to take to obtain an unqualified audit/review report for future financial periods?
3. How has the Company satisfied itself as to the recoverable amount of the Company’s assets referred to in the Updated Resources and Reserves Statement?
4. Does the Company consider that its level of operations is sufficient to warrant continued quotation of its securities on ASX in accordance with the requirements of listing rule 12.1? In answering this question, please also explain the basis for this conclusion.
5. Is the Company of the view that the financial condition of the Company would be sufficient to warrant continued listing on ASX in accordance with the requirements of listing rule 12.2?
6. If the answer to questions 4 or 5 is “Yes”, please explain the basis on which the Company has formed the conclusion that the financial condition of the Company is sufficient to warrant continued listing on ASX in accordance with the requirements of listing rules 12.2. Specifically, the Company should submit the reasons (including any previous disclosures made to the market) it considers relevant given the matters outlined in the Independent Auditor’s Review Report resulting in the Qualified Opinion.

7. If the answer to question 4 or 5 is “No”, please explain what steps the Company has taken, or proposes to take, to warrant continued listing on ASX in accordance with the requirements of listing rules 12.1 and 12.2.
8. Please confirm that the Company is in compliance with the listing rules and, in particular, listing rules 3.1 and 12.2.

### **When and where to send your response**

This request is made under, and in accordance with, Listing Rule 18.7. Your response is required as soon as reasonably possible and, in any event, **by not later than 12:00 pm AWST on Monday 10 October 2016**. If we do not have your response by then, ASX will have no choice but to consider suspending trading in the Entity’s securities under Listing Rule 17.3. Your response should be sent to me by return e-mail, copying [tradinghaltspert@asx.com.au](mailto:tradinghaltspert@asx.com.au). It should not be sent to the Market Announcements Office.

You should note that if the information requested by this letter is information required to be given to ASX under Listing Rule 3.1 and it does not fall within the exceptions mentioned in Listing Rule 3.1A, the Entity’s obligation is to disclose the information “immediately”. This may require the information to be disclosed before the deadline set out in the previous.

Please note that ASX reserves the right, under listing rule 18.7A, to release this letter and the Company’s response to the market. Accordingly, please prepare your response in a form suitable for release to the market.

If you have any queries regarding any of the above, please call me.

Yours sincerely,

*[sent electronically without signature]*

Chris Bailey

**Adviser, Listings Compliance (Perth)**