

SOLITARIO EXPLORATION & ROYALTY CORP.
Form 10-Q
August 11, 2015

UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-Q

(Mark One)

QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the quarterly period ended June 30, 2015

OR

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from _____ to _____

Commission File Number. 001-39278

SOLITARIO EXPLORATION & ROYALTY CORP.

(Exact name of registrant as specified in its charter)

Colorado

(State or other jurisdiction of incorporation or organization)

4251 Kipling St. Suite 390, Wheat Ridge, CO

(Address of principal executive offices)

(303) 534-1030

(Registrant's telephone number, including area code)

84-1285791

(I.R.S. Employer Identification No.)

80033

(Zip Code)

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Indicate by checkmark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.

YES NO

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every

Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

YES NO

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act.

		Non-accelerated filer	
Large accelerated filer	Accelerated filer	(do not check if a smaller reporting company)	Smaller reporting company

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

YES NO

There were 39,314,189 shares of \$0.01 par value common stock outstanding as of August 10, 2015.

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PART I - FINANCIAL INFORMATIONItem 1. Financial Statements

SOLITARIO EXPLORATION & ROYALTY CORP.

CONSOLIDATED BALANCE SHEETS

(in thousands of U.S. dollars, except share and per share amounts)	June 30, 2015 (unaudited)	December 31, 2014
Assets		
Current assets:		
Cash and cash equivalents	\$ 64	\$ 869
Investments in marketable equity securities, at fair value	1,125	2,308
Prepaid expenses and other	49	40
Total current assets	1,238	3,217
Mineral properties	15,685	14,660
Other assets	1,156	1,163
Total assets	\$ 18,079	\$ 19,040
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable	\$ 450	\$ 343
Current portion long-term debt, net of discount	4,969	4,861
Other	1	—
Total current liabilities	5,420	5,204
Deferred gain on sale of mineral property	7,000	7,000
Warrant liability	34	55
Commitments and contingencies		
Equity:		
Shareholders' equity:		
Preferred stock, \$0.01 par value, authorized 10,000,000 shares (none issued and outstanding at June 30, 2015 and December 31, 2014)	—	—
Common stock, \$0.01 par value, authorized 100,000,000 shares (39,314,189 and 39,347,689, respectively, shares issued and outstanding at June 30, 2015 and December 31, 2014)	393	393
Additional paid-in capital	54,876	54,512
Accumulated deficit	(47,154)	(46,563)
Accumulated other comprehensive loss	(2,147)	(1,120)
Total Solitario shareholders' equity	5,968	7,222
Noncontrolling interest	(343)	(441)

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Total shareholders' equity	5,625	6,781
Total liabilities and shareholders' equity	\$ 18,079	\$ 19,040

See Notes to Unaudited Condensed Consolidated Financial Statements

SOLITARIO EXPLORATION & ROYALTY CORP.

CONSOLIDATED STATEMENTS OF OPERATIONS

(Unaudited)

(in thousands of U.S. dollars)	Three months ended June 30		Six months ended June 30	
	2015	2014	2015	2014
Costs, expenses and other:				
Exploration expense	\$7	\$136	\$32	\$184
Depreciation and amortization	2	5	5	8
General and administrative	478	404	1,032	935
Gain on derivative instruments	(1)	(7)	(83)	(39)
Property abandonment and impairment	—	20	—	20
Interest income	(1)	(1)	(1)	(1)
Total costs, expenses and other	485	557	985	1,107
Other income (expense)				
Gain on sale of marketable equity securities	364	103	364	403
Gain on sale of other assets	7	—	7	—
Gain (loss) on warrant liability	(28)	41	21	(219)
Net loss of equity method investment	—	(28)	—	(153)
Total other income (expense)	343	116	392	31
Loss before income tax	(142)	(441)	(593)	(1,076)
Income tax expense	—	(100)	—	—
Net loss	(142)	(541)	(593)	(1,076)
Less net loss attributable to noncontrolling interest	1	2	2	5
Net loss attributable to Solitario shareholders	\$(141)	\$(539)	\$(591)	\$(1,071)
Loss per common share attributable to Solitario shareholders:				
Basic and diluted	\$(0.00)	\$(0.01)	\$(0.02)	\$(0.03)
Weighted average shares outstanding:				
Basic and diluted	39,273	39,228	39,260	38,616

See Notes to Unaudited Condensed Consolidated Financial Statements

SOLITARIO EXPLORATION & ROYALTY CORP.

CONSOLIDATED STATEMENTS OF COMPREHENSIVE INCOME (LOSS)

(Unaudited)

(in thousands of U.S. dollars)	Three months ended		Six months ended	
	June 30		June 30	
	2015	2014	2015	2014
Net loss attributable to Solitario shareholders, before other comprehensive loss	\$(142)	\$(541)	\$(593)	\$(1,076)
Other comprehensive income (loss)				
Unrealized loss on marketable equity securities, net of deferred taxes	(429)	(368)	(1,027)	(182)
Comprehensive loss	(571)	(909)	(1,620)	(1,258)
Loss attributable to noncontrolling interests	1	2	2	5
Comprehensive loss attributable to Solitario shareholders	\$(570)	\$(907)	\$(1,618)	\$(1,253)

See Notes to Unaudited Condensed Consolidated Financial Statements

SOLITARIO EXPLORATION & ROYALTY CORP.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Unaudited)

(in thousands of U.S. dollars)	Six months ended June 30, 2015 2014	
Operating activities:		
Net loss	\$(593)	\$(1,076)
Adjustments to reconcile net loss to net cash used in operating activities:		
Unrealized gain on derivative instruments	(83)	(39)
Depreciation and amortization	5	8
Loss on equity method investment	—	153
(Gain) loss on warrant liability	(21)	219
Employee stock option expense	313	111
Accrued interest income	(2)	—
Property abandonment and impairment	—	20
Gain on equity security and asset sales	(371)	(403)
Changes in operating assets and liabilities:		
Prepaid expenses and other current assets	(9)	85
Accounts payable and other current liabilities	108	(42)
Net cash used in operating activities	(653)	(964)
Investing activities:		
Additions to mineral properties	(763)	(999)
Sale of derivative instruments	84	36
Proceeds from sale of marketable equity securities	519	473
Other assets, net	8	10
Net cash used in investing activities	(152)	(480)
Financing activities:		
Proceeds from issuance of common stock	—	1,630
Short-term borrowing (net)	—	(802)
Payment to noncontrolling interest	—	(250)
Net cash provided by financing activities	—	578
Net decrease in cash and cash equivalents	(805)	(866)
Cash and cash equivalents, beginning of period	869	2,092
Cash and cash equivalents, end of period	\$64	\$1,226
Supplemental disclosure of cash flow information:		
Cash paid for interest, capitalized to mineral property	\$133	\$96
Supplemental disclosure of non-cash activities:		
Capitalized non-cash interest	\$206	\$206
Loan to non-controlling interest	\$100	\$—
Issuance of stock to noncontrolling interest	\$—	\$76
Issuance of stock for mineral property	\$51	\$38

Issuance of stock to settle severance liability	\$—	\$45
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See Notes to Unaudited Condensed Consolidated Financial Statements

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NOTES TO UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(Unaudited)

1. Business and Significant Accounting Policies

Recent Developments

On June 10, 2015 Solitario Exploration & Royalty Corp. (“Solitario” or the “Company”), along with DHI Minerals (U.S.) Ltd. (“DHI”), entered into a definitive agreement (the “Agreement”) to sell their combined interests in the Mt. Hamilton gold project (“Mt. Hamilton”) to Waterton Nevada Splitter, LLC, a wholly-owned subsidiary of Waterton Precious Metals Fund II Cayman, LP (collectively, “Waterton”), for total cash proceeds of US\$30 million (the “Transaction”). Under the terms of the Transaction, Solitario will sell its 80% interest in Mt. Hamilton LLC (“MH-LLC”), a limited liability company which holds 100% of the Mt. Hamilton project assets, and DHI will sell its 20% interest in MH-LLC. DHI is a wholly-owned subsidiary of Ely Gold and Minerals, Inc. (“Ely”). As a result, on closing of the Transaction, Solitario would be entitled to gross cash proceeds of US\$24 million and Ely would be entitled to gross cash proceeds of US\$6 million. Costs and fees related to the Transaction, including any income taxes, broker fees and professional service fees, will reduce the net amount received by Solitario and DHI. The Transaction is structured as the sale of Solitario’s and DHI’s combined membership interests in MH-LLC. Completion of the Transaction is subject to the satisfaction of various conditions precedent, including the approval of the holders of a majority of Solitario’s outstanding shares of common stock, as well as customary closing conditions, including regulatory approvals. Solitario’s shareholder meeting is scheduled for August 14, 2015, with the closing of the Transaction, assuming it is approved by Solitario shareholders, and assuming all closing conditions of the Agreement are met, is expected to occur as soon as practical after Solitario’s shareholder meeting.

As explained in more detail in Note 5, “Short-term Debt,” Solitario entered into a facility agreement (the “Facility Agreement”) with RMB Australia Holdings Limited (“RMBAH”) and RMB Resources, Inc., a Delaware corporation (“RMBR”) whereby Solitario has borrowed \$5,000,000 from RMBAH (with any amounts outstanding collectively being the “RMB Loan”). Concurrent with the execution of the Agreement, Waterton and Solitario entered into a letter agreement whereby Waterton has committed to provide Solitario, at Solitario’s request, with a loan through a standby debt facility (the “Standby Debt Facility”) in an amount necessary to repay the RMB Loan due on September 30, 2015. If Solitario elects to enter into the facility, completion of the Standby Debt Facility is conditional on Solitario being in compliance with all terms of the Agreement, providing security over Solitario’s assets which is substantially similar to the security provided under the Facility Agreement, and completion of necessary documentation. The indebtedness would be secured by Solitario’s interest in MH-LLC as well as other corporate assets, have a six-month term and earn interest at 8% per annum. Waterton will also be entitled to a 2% structuring fee should Solitario exercise its right to enter into the Standby Debt Facility.

On August 5, 2015, Solitario entered into an agreement with RMBAH to extend the maturity date of the RMB Loan from August 21, 2015 to September 30, 2015 (the "RMB Loan Extension"). In consideration for entering into the RMB Loan Extension, Solitario paid RMBAH an extension fee of \$50,000 and agreed to extend the terms of warrants issued to RMBAH to acquire 1,624,748 shares of Solitario common stock from August 21, 2015 to August 21, 2016. All other terms of the Facility Agreement, the RMB Loan and warrants remained the same.

Business and company formation

Solitario is a development stage company at June 30, 2015 under Industry Guide 7, as issued by the United States Securities and Exchange Commission ("SEC"), with a recent focus on the Mt. Hamilton gold project located in Nevada. Solitario was incorporated in the state of Colorado on November 15, 1984 as a wholly-owned subsidiary of Crown Resources Corporation ("Crown"). In July 1994, Solitario became a publicly traded company on the Toronto Stock Exchange (the "TSX") through its Initial Public Offering. Solitario has been actively involved in mineral exploration since 1993. In December 2010 Solitario signed the Limited Liability Company Operating Agreement of Mt. Hamilton LLC (the "MH Agreement") with DHI and formed MH-LLC, the owner of the Mt. Hamilton project. Prior to entering into the Agreement, Solitario was primarily focused on the development of the Mt. Hamilton project. However, Solitario has never developed a mineral property and the development of the Mt. Hamilton project would require a significant amount of outside capital. In addition to its activities at Mt. Hamilton, including the proposed Transaction, Solitario also acquires and holds a portfolio of exploration properties for future sale or joint venture or to create a royalty prior to the establishment of proven and probable reserves.

However, if the proposed Transaction is approved by Solitario shareholders and the Transaction closes, Solitario intends to shift its primary focus from the development of the Mt. Hamilton project to the furtherance of its other assets and to Solitario's historical focus of the acquisition of precious and base metal properties with exploration potential and the development or purchase of royalty interests. However there can be no assurance that the Transaction will close.

Solitario has recorded revenue in the past from the sale of mineral property and joint venture property payments and the sale of a royalty on its Mt. Hamilton property. Revenues from the sale or joint venture of properties have not been a significant source of revenue and would occur, if at all, on an infrequent basis in the future.

The accompanying interim condensed consolidated financial statements of Solitario for the three and six months ended June 30, 2015 and 2014 are unaudited and are prepared in accordance with accounting principles generally accepted in the United States of America. They do not include all disclosures required by generally accepted accounting principles for annual financial statements, but in the opinion of management, include all adjustments, consisting only of normal recurring items, necessary for a fair presentation. Interim results are not necessarily indicative of results, which may be achieved in the future or for the full year ending December 31, 2015.

These financial statements should be read in conjunction with the financial statements and notes thereto which are included in Solitario's Annual Report on Form 10-K for the year ended December 31, 2014. The accounting policies set forth in those annual financial statements are the same as the accounting policies utilized in the preparation of these financial statements, except as modified for appropriate interim financial statement presentation.

Basis of Presentation

The accompanying financial statements have been prepared assuming Solitario will continue as a going concern. As of June 30, 2015 Solitario has a working capital deficit of \$4,182,000. The RMB Loan is due on September 30, 2015. Solitario currently does not have sufficient liquidity to repay the RMB Loan when due raising substantial doubt about its ability to continue as a going concern. Pursuant to the Agreement, if the Transaction closes, Solitario expects to use a portion of the funds from the Transaction to repay the RMB Loan. In the event the Transaction is delayed, Solitario may enter into negotiations for the Standby Debt Facility, however there can be no assurance that the Transaction will close or that funds will be available from Standby Debt Facility in time to repay RMB Loan. If the Transaction does not close and Solitario does not obtain adequate funds from the Standby Debt Facility there can be no assurance that Solitario will be able to raise sufficient outside funds on acceptable terms in order to repay the RMB Loan. The accompanying financial statements do not include any adjustments that might result from the outcome of this uncertainty. Under the terms of the RMB Loan, Solitario will be in default if it is unable to repay the RMB loan when it is due on September 30, 2015. Should Solitario be in default, RMBAH has, among other rights, the right to foreclose on its security interest in certain assets of Solitario to satisfy its obligation.

Financial reporting

The consolidated financial statements include the accounts of Solitario and its wholly-owned subsidiaries, controlled non-wholly-owned subsidiaries. All significant intercompany accounts and transactions have been eliminated in consolidation. The consolidated financial statements are prepared in accordance with accounting principles generally accepted in the United States of America ("generally accepted accounting principles"), and are expressed in US dollars.

Revenue recognition

Solitario records delay rental payments as revenue in the period received. Any payments received for the sale of property interests are recorded as a reduction of the related property's capitalized cost. Proceeds which exceed the capitalized cost of the property without reserves are recognized as revenue. Payments received on the sale of properties with reserves are recognized as revenue to the extent the proceeds exceed the proportionate basis in the assets sold. Gain on the sale of a mineral property revenue stream is deferred to the extent there is a guarantee for the future revenue stream until such time as the potential funding obligation for the guarantee is reduced or released.

Use of estimates

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates. Some of the more significant estimates included in the preparation of Solitario's financial statements pertain to: (i) the recoverability of mineral properties, with significant emphasis on Mt. Hamilton and the recoverability of its investment as well as the recoverability of mineral exploration properties and their future exploration potential; (ii) the fair value of Solitario's stock option grants to employees; (iii) the fair value of Solitario's investment in marketable equity securities; (iv) the fair value of Solitario's liability for warrants Solitario issued to RMBAH upon entering into the Facility Agreement

In performing its activities, Solitario has incurred certain costs for mineral properties. The recovery of these costs is ultimately dependent upon the sale of mineral property interests or the development of economically recoverable ore reserves and the ability of Solitario to obtain the necessary permits and financing to successfully place the properties into production, and upon future profitable operations, none of which is assured.

Cash equivalents

Cash equivalents include investments in highly liquid money-market securities with original maturities of three months or less when purchased.

Mineral properties

Solitario expenses all exploration costs incurred on its mineral properties prior to the establishment of proven and probable reserves through the completion of a feasibility study. Initial acquisition costs of its mineral properties are capitalized. Solitario began capitalizing all of its development expenditures on its Mt. Hamilton project, subsequent to the completion of a feasibility study in 2012. Solitario regularly performs evaluations of its investment in mineral properties to assess the recoverability and/or the residual value of its investments in these assets. All long-lived assets are reviewed for impairment whenever events or circumstances change which indicate the carrying amount of an asset may not be recoverable, utilizing established guidelines based upon undiscounted future net cash flows from the asset or upon the determination that certain exploration properties do not have sufficient potential for economic mineralization.

Derivative instruments

Solitario accounts for its derivative instruments in accordance with ASC 815 "Accounting for Derivative Instruments and Hedging Activities" ("ASC 815"). Solitario has not designated its covered calls as hedging instruments and any changes in the fair value of the covered calls and the RMB Warrants are recognized in the statement of operations in the period of the change.

Fair value

FASB ASC 820, "Fair Value Measurements and Disclosures" ("ASC 820") establishes a framework for measuring fair value and requires enhanced disclosures about fair value measurements. ASC 820 clarifies that fair value is an exit price, representing the amount that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants. For certain of Solitario's financial instruments, including cash and cash equivalents, short-term margin loans and accounts payable, the carrying amounts approximate fair value due to their short-term maturities. Solitario's marketable equity securities and the Kinross Gold Corporation ("Kinross") calls are carried at their estimated fair value based on quoted market prices. See Note 7, "Fair Value" below.

Marketable equity securities

Solitario's investments in marketable equity securities are classified as available-for-sale and are carried at fair value, which is based upon quoted prices of the securities owned. Solitario records investments in marketable equity securities as available-for-sale for investments in publicly traded marketable equity securities for which it does not exercise significant control and where Solitario has no representation on the Board of Directors of those companies and exercises no control over the management of those companies. The cost of marketable equity securities sold is determined by the specific identification method. Changes fair values are recorded in accumulated other comprehensive income within shareholders' equity, unless a decline in fair value is considered other than temporary, in which case the decline is recognized as a loss in the consolidated statements of operations.

Foreign exchange

The United States dollar is the functional currency for all of Solitario's foreign subsidiaries. Although Solitario's South American exploration activities have been conducted primarily in Brazil, Peru and Mexico, a portion of the payments under the land, leasehold and exploration agreements of Solitario are denominated in United States dollars. Foreign currency gains and losses are included in the results of operations in the period in which they occur.

Income taxes

Solitario accounts for income taxes in accordance with ASC 740, "Accounting for Income Taxes." Under ASC 740, income taxes are provided for the tax effects of transactions reported in the financial statements and consist of taxes currently due plus deferred taxes related to certain income and expenses recognized in different periods for financial and income tax reporting purposes. Deferred tax assets and liabilities represent the future tax return consequences of those differences, which will either be taxable or deductible when the assets and liabilities are recovered or settled. Deferred taxes are also recognized for operating losses and tax credits that are available to offset future taxable income and income taxes, respectively. A valuation allowance is provided if it is more likely than not that some portion or all of the deferred tax assets will not be realized.

Accounting for uncertainty in income taxes

ASC 740 clarifies the accounting for uncertainty in income taxes recognized in a company's financial statements. ASC 740 prescribes a recognition threshold and measurement attribute for the financial statement recognition and measurement of a tax position taken or expected to be taken in a tax return. ASC 740 also provides guidance on derecognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. ASC 740

provides that a company's tax position will be considered settled if the taxing authority has completed its examination, the company does not plan to appeal, and it is remote that the taxing authority would reexamine the tax position in the future. These provisions of ASC 740 had no effect on Solitario's financial position or results of operations. See Note 8, "Income Taxes" below.

Earnings per share

The calculation of basic and diluted loss per share is based on the weighted average number of shares of common stock outstanding during the three and six months ended June 30, 2015 and 2014. Potentially dilutive shares related to outstanding common stock options of 3,748,000 and 1,758,000 for the three and six months June 30, 2015 and 2014, respectively, and warrants issued to RMBAH to acquire 1,624,748 shares of common stock for the three and six months ended June 30, 2015 and 2014 were excluded from the calculation of diluted loss per share because the effects were anti-dilutive.

Employee stock compensation and incentive plans

Solitario classifies all of its stock options as equity options in accordance with the provisions of ASC 718 "Compensation – Stock Compensation."

Recent accounting pronouncements

In August 2014, the FASB issued ASU 2014-15, “*Presentation of Financial Statements—Going Concern: Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern*”. The standard requires an entity's management to evaluate whether there are conditions or events that raise substantial doubt about the entity's ability to continue as a going concern within one year after the date that the financial statements are issued. Public entities are required to apply the standard for annual reporting periods ending after December 15, 2016, and interim periods thereafter. Early application is permitted. The adoption of this guidance is not expected to impact the Company’s consolidated financial position, results of operations, or cash flows. If any event occurs in future periods that could affect the Company’s ability to continue as going concern, the Company will provide appropriate disclosures as required by ASU 2014-15.

2. Mineral Property

The following table details Solitario’s investment in Mineral Property:

(in thousands)	June 30, 2015	December 31, 2014
Development (United States)		
Mt. Hamilton	\$ 15,666	\$ 14,641
Exploration		
La Promesa (Peru)	5	5
Norcan (Mexico)	6	6
Aconchi (Mexico)	5	5
Canta Colorado (Peru)	3	3
Total exploration	19	19