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Canadian Government Blocks Foreign Acquisition of Canadian Gold Miner on National Security Grounds

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The Canadian government has exercised its authority under the national security provisions of the *Investment Canada Act* (ICA) to prohibit Shandong Gold Mining Co., Ltd. (Shandong), a Chinese state-owned enterprise (SOE), from acquiring Canadian gold producer TMAC Resources Inc. (TMAC). This decision serves as yet another reminder to foreign investors of the need to consider the potential application of the ICA's national security provisions when planning investments in Canadian businesses.

Following the announcement of the government's decision, a Canadian gold miner, Agnico Eagle Mines Limited (Agnico), announced that it had entered into agreements to purchase TMAC in place of Shandong.[1]

The Decision

On May 8, 2020, Shandong announced that it had entered into an agreement to acquire all of the outstanding shares of TMAC for approximately $207 million. TMAC is listed on the Toronto Stock Exchange and holds a 100% interest in the Hope Bay property, a gold mining property located in the Canadian Territory of Nunavut in Canada's far north.

The transaction required approval under the ICA's "net benefit to Canada" review process, which typically takes into account the impact of the transaction on factors such as employment levels and capital investment in Canada. To this end, Shandong had announced various types of commitments that it was willing to offer to secure such approval under the ICA, including continuing to grow employment and skills training for TMAC's Inuit employees and ensuring "the continued commercial orientation and standards of corporate governance practiced by TMAC."

The proposed transaction was also the subject of a formal national security review under the ICA (as announced by TMAC on October 25, 2020). The ICA's national security review process authorizes the government to block a transaction or impose remedies when it determines that an investment (of any size) would be "injurious" to Canadian national security interests. These measures range from prohibiting or unwinding the investment to orders imposing conditions to "mitigate" the perceived jeopardy to Canada's national security interests in order for the investment to proceed.

The national security review of Shandong's proposed acquisition of TMAC was extended by up to an additional 45 days on November 27, 2020. Subsequently, the Canadian government advised the parties that the federal Cabinet had issued an order on December 18, 2020 directing Shandong not to implement its proposed acquisition of TMAC.

The fact that the proposed transaction came under national security scrutiny was not necessarily surprising, particularly since the deal was signed shortly after the Canadian government had issued a policy statement in April 2020 announcing its intention to apply "enhanced scrutiny" under the ICA to certain categories of foreign investments, including all investments by SOEs.

One of the hallmarks of the Canadian national security review process is its lack of transparency. The Shandong/TMAC case is no exception. As of the date of writing, the Canadian government has not issued any statement announcing its decision, let alone providing any explanation for it. The only step the government has taken so far is to permit a spokesperson to verify to the press that the decision had been made to block the proposed transaction. However, the spokesperson declined to give specific reasons for the decision.

It is quite possible that the government's negative decision was influenced by tensions in Canadian-Chinese relations, including those arising from China's arrest and detention of two Canadians for alleged espionage following Canada's arrest in 2018 of Meng Wanzhou, Huawei Technologies Co. Ltd.'s Chief Financial Officer, on a U.S. extradition warrant. The current Liberal government, which was initially positively disposed toward China, is said to be conducting a review of its position in relation to China at least in part due to these tensions.

According to news reports, however, the Canadian military may have raised concerns about the proposed transaction's impact on the ongoing effort to promote and protect Canadian sovereignty in the Arctic. In particular, reports pointed to the fact that TMAC's Doris mine is located approximately 100 kilometres from a North American Aerospace Defense Command (NORAD) radar station in Cambridge Bay, Nunavut, which is part of a chain of installations in the Arctic that gather and transmit information to NORAD's military operation centres. Other reports have also noted that the Doris mine is located close to a narrow point of the Northwest Passage, a strategic shipping route connecting the Atlantic Ocean to the Pacific Ocean.

If these reports are correct, this would not be the first time that concerns about the impact on Canadian sovereignty in the North have led to the demise of a proposed foreign investment in Canada. In 2008, even before the ICA's separate national security review process was enacted, the Canadian government blocked a proposal by a U.S. investor to acquire a Canadian satellite company because of concerns about the loss of Canadian control over satellite technology developed by the company (with government financial support) that was used for surveillance of Canada's northern territories.

Similarly, this also would not be the first time that the Canadian government has denied permission for a Chinese investment because of concerns that the transaction would position a Chinese SOE's operations in close proximity to a strategically sensitive installation or location. In 2015, it was reported that the government blocked Beida Jade Bird, a Chinese SOE software and computer solutions company, from establishing a new Canadian business – a fire and smoke alarm systems manufacturing facility in Saint-Bruno, Québec – because the site was located less than two kilometres from facilities operated by the Canadian Space Agency. Beida Jade Bird was reported to have plans to build fire alarm systems for the Chinese market. Interestingly, the Québec government had given Beida Jade Bird $3 million in loans and a $1 million grant for the project. However, this Québec support did not prevent the federal government from blocking the investment on national security grounds.

Subsequent Developments

Shortly following the Canadian government's decision to block Shandong's proposed acquisition of TMAC, Agnico, a Canadian headquartered and managed gold mining company, announced that it had entered into agreements to acquire all of the outstanding shares of TMAC in place of Shandong and at a higher price than Shandong had offered. (The proposed Agnico acquisition is being effected by way of assignment to Agnico of the May 8, 2020, Shandong agreement.)

Although the Canadian government has not commented publicly on Agnico's stepping into Shandong's shoes to acquire TMAC, it may view this as a way of demonstrating that the national security review process does not necessarily inhibit deal-making in Canada or harm Canadian shareholders of potential target companies.

Implications

The vast majority of foreign investments in Canada do not raise any national security concerns – including transactions involving Chinese investors. That said, the Shandong/TMAC transaction reinforces the need for a risk assessment to be conducted in each specific instance, especially while the Canadian government's policy of enhanced scrutiny remains in force (and there is no indication this policy will be repealed or relaxed any time soon).

As always, key considerations will include where the purchaser is based, the identity of any major investors in the purchaser, whether the purchaser is an SOE, the type of Canadian business being acquired, and whether the Canadian business is already foreign controlled.

The Shandong/TMAC experience also highlights the importance of investigating if there are sensitive government facilities in proximity to the target Canadian business or other geographic sensitivities relating to its location. As a reflection of this type of concern, the Committee on Foreign Investment in the United States (CFIUS), which conducts similar national security reviews in that country, has published a geographic reference tool that allows parties to identify whether a particular address is located in close proximity to U.S.

military installations (and thus whether a particular transaction may be subject to CFIUS review on that basis). However, no such tool is available in Canada.

Finally, although not apparently an issue in the Shandong/TMAC case, it also should be noted that the latest frontier in national security reviews – both in Canada and abroad – involves the potential uses (and misuses) by foreign investors of personal data possessed by target businesses. This burgeoning area of concern has led authorities (including in Canada) to question, block or unwind transactions involving businesses engaged in activities such as dating services, video games, social media platforms, mortgage insurance and money transfers. It is doubtful that any of these businesses would have been regarded as possible national security concerns even a few years ago.

[1] Davies is acting for Agnico on this transaction.

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