COVID-19’s impact on mining

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The mining industry has been significantly affected by the COVID-19 pandemic. From senior producers being forced to put their cornerstone assets on temporary care and maintenance to junior explorers being unable to access or conduct operations on their mineral tenures, the fallout has been widespread. Governments, regulatory bodies and industry groups in the key Canadian mining jurisdictions have generally been prompt to respond with measures and proposals aimed at assisting industry participants. Surging precious metal prices also indicate that a resumption of deal activity in the sector may be in store in the not too distant future. Below we discuss a number of considerations relating to the COVID-19 pandemic for participants in the mining industry.

SHUTDOWNS AND ESSENTIAL SERVICES

In response to the COVID-19 pandemic, provinces across Canada have imposed varying levels of restrictions on operations, limiting activities in many cases to “essential services.” In general, mining activities have been permitted to continue. Below we briefly summarize the applicable restrictions in key mining jurisdictions.

- **British Columbia**: Mineral production and mineral exploration/development are explicitly designated as essential services, so businesses may maintain ongoing operations so long as they can adapt their workplaces to ensure compliance with the orders and recommendations of British Columbia’s public health officer.
- **Alberta**: Neither mineral production nor mineral exploration has been designated as an essential service by the provincial government. However, they are not among the class of businesses that have been ordered to close, so activities in Alberta may continue so long as businesses can adapt their workplaces to ensure compliance with the orders and recommendations of Alberta’s chief medical officer.
- **Ontario**: Businesses that provide and ensure the domestic and global continuity of the supply of resources, including mining, are classified as essential services. Initially, the Ontario list made clear...
that exploration was permitted; however, the essential workplace list is now more generic. Mining businesses have been permitted to continue full operations (subject to compliance with health and safety orders and recommendations) but many have voluntarily shuttered operations to protect employees.

- **Québec**: The government of Québec initially declared aluminum production to be an essential service and required that all other mining issuers scale down operations to a minimum in its initial directive on March 23, 2020. However, on April 13, 2020, the provincial government reversed course and allowed mining operations in the province to resume, subject to compliance with health and safety orders and recommendations.

**MINERAL TENURE UPKEEP CONSIDERATIONS**

In most jurisdictions, minimum annual investments are required to be made on projects in order to keep the constituent mineral claims in good standing. Government-mandated shutdowns and other measures in response to COVID-19, as well as employee safety considerations, present meaningful challenges for businesses that will affect their ability to complete necessary project expenditures. Additionally, due to persistent challenging market conditions, it has been difficult for many juniors to raise the capital needed to fund their planned exploration programs.

In certain jurisdictions, mining industry regulators have announced relief measures for claim holders. On March 27, 2020, the Chief Gold Commissioner of British Columbia issued an order extending to December 31, 2021, the deadline for the filing of a statement of exploration and development or making payment in lieu on any mineral or coal claim coming due in 2020 or 2021, giving mineral and coal claim holders in British Columbia until the end of next year to incur the required expenditures or make payment in lieu. In Ontario, the Ministry of Energy, Northern Development and Mines (MNMD) recently announced that it will be granting exclusion orders to any claim holders with claim anniversary dates on or prior to December 31, 2020. Pursuant to MNMD’s existing Exclusion of Time policy, an exclusion order relieves the claim holder from the obligation to satisfy its annual assessment work for a period of time. Note that, unlike in B.C., a claimholder must make application (by email to pro.ndm@ontario.ca) no earlier than the 30th day before the anniversary date of the claim and no later than 4:30 p.m. ET on the date of the relevant mineral claim anniversaries to receive an exclusion order.

It will be interesting to see if governing bodies in other jurisdictions with significant mining activities grant similar relief if mineral exploration activities are curtailed throughout 2020. Impacted mineral tenure holders should follow the situation closely and may wish to consider engaging with the relevant governing bodies to see if relief is available.

**FLOW-THROUGH SHARE ISSUES**

As the uncertainty around businesses continues due to COVID-19, it is important for issuers planning exploration programs in the summer field season to plan ahead and be prepared for any eventualities. This is even more important for companies with outstanding flow-through obligations that must incur Canadian Exploration Expenses (CEE) and Canadian Development Expenditures (CDE) (each as defined in the *Income Tax Act* (Canada)(the Tax Act)) on their mineral projects by December 31, 2020, or that are contemplating potential issuances of flow-through shares to fund proposed exploration or development programs. As noted above, in jurisdictions where mineral exploration and development have been declared essential businesses, it may be possible to conduct some work, but even then companies should make sure that suppliers and service providers are able to support their proposed programs. Remote
projects and those in harsh climatic conditions may be subject to even further delay. It is also unclear how one might practice physical distancing on a drill rig.

Certain industry organizations, notably the Association for Mineral Exploration in British Columbia and the Prospectors and Developers Association of Canada, have announced advocacy efforts to seek accommodation from Canadian and provincial tax authorities to extend the deadlines by which CEE or CDE must be incurred, and to broaden the scope of what constitutes CEE to include desktop studies that can be safely performed in the current environment. It is not yet clear what, if any, relief will be granted for flow-through shares, but issuers are advised to plan ahead and address any current or anticipated difficulties as early as possible and be sure they understand their commitments and obligations.

Subscription agreements for flow-through shares will contain commitments from the issuer to the investors as to the type of expenses (CEE or CDE) it will incur and the timing for the renunciation of those expenses to the investors. Under the tax legislation, issuers generally have two years to incur and renounce the exploration or development expenses to the investors. Sometimes the period for incurring expenses is shortened contractually to increase the marketability and pricing of the financing. Furthermore, the expenditure period is shortened where the flow-through shares are issued under the “look-back rule.” Under this rule, issuers can renounce certain expenses effective as of December 31 of the year of the share issuance but have until December 31 of the following year to incur the required expenses.

Issuers that are considering flow-through share financings should take into account the continuing (and potentially new) business and operational disruptions due to the COVID-19 pandemic in determining the timing for launching a flow-through share financing and in setting the expenditure and renunciation terms. In particular, issuers should consider whether shortening the two-year expenditure period (whether contractually or applying the “look-back rule”) will heighten the risk of the issuer not being able to meet its commitments.

There are both contractual and tax implications to consider if an issuer fails to meet its flow-through share commitments. Subscription agreements generally contain an indemnity from the issuer to the investors for additional taxes payable by the investor as a result of the issuer failing to meet its commitments. If a company has issued shares under the “look-back rule,” it may also be subject to additional taxes and/or penalties under the Tax Act a result of a delay or failure to meet its flow-through share obligations.

If a company has concerns that, as a result of the current circumstances, it may not be able to meet commitments to its flow-through share investors, it should proactively consider mitigation strategies.

**M&A AND CAPITAL MARKETS CONSIDERATIONS**

The COVID-19 pandemic has undeniably affected both M&A activity and capital raising as significant market declines, physical distancing and a persistent state of volatility have created an environment that is not conducive to deal-making.

At the same time, the price of gold continues to rise and gold company shares have recently had some significant market support. Market sentiment suggests that when conditions improve there will be a flurry of M&A and financing activity. In anticipation of that market window and likely first-mover advantages for companies that are prepared for it, we have set out below some suggestions for steps that issuers should take now while considering potential M&A activity or potentially access to the capital.
projects that may be available in the current opportunistic market environment — our colleagues have written about a variety of matters that public issuers should think about, including shareholder engagement and legal protections such as shareholder rights plans. Consider protections that may be available in the current opportunistic market environment — our colleagues have written about a variety of matters that public issuers should think about, including shareholder engagement and legal protections such as shareholder rights plans.

- Develop or update an electronic data room if one is not current — it is far easier to maintain an existing data room on a periodic basis than it is to update a stale (or non-existent) data room; having a current data room will allow counterparties (M&A counterparties, underwriters or lenders) to conduct their due diligence quickly, efficiently and, most importantly, remotely.

- Review the disclosure of peer companies and of the majors to assess best practices, see current trends and consider ways to enhance your own disclosure record — consider the impact of the pandemic on applicable disclosure requirements (see our update on Q1 disclosure considerations for some ideas).

- Use downtime to conduct “desktop diligence” on potential counterparties or issuers with projects near yours in order to assess the viability of potential peers in an M&A transaction (either as a merger partner, target or buyer) — although site visits will ultimately be required (with some uncertainty as to timing), desktop diligence and virtual data rooms can cover off critical path decision questions.

- Connect with peer companies, financial advisors and legal counsel for transaction ideas and to build relationships.

On the financing side, equity financing may be required (as soon as volatility in the markets settles) for many issuers. While many in the gold sector may have the luxury of a strong gold price to bolster interest, others may not be so fortunate and may need to consider emergency financing. A brief reminder that after the financial crisis of 2008 (at a time when many issuers were taking advantage of the financial hardship exemptions from both the TSX Company Manual and the related party transaction rules under MI 61-101), the TSX issued a staff notice imposing additional hurdles on the use of the financial hardship exemption.

**PROJECT AGREEMENTS**

Much has been written about the importance of reviewing and understanding force majeure provisions of contracts to determine their application as a result of the COVID-19 pandemic. See our materials on the Osler COVID-19 page. However, there may be limitations for invoking force majeure provisions in certain relational agreements for mining projects, like earn-in agreements and joint venture agreements.

Force majeure provisions often carve out payment obligations and lack of funds as a trigger, so even if obligations requiring exploration expenditures or the attainment of project milestones may be suspended due to force majeure, parties may still be required to make cash payments to vendors. Typically, such contracts are structured to enable parties to complete exploration and development work to justify making the next payment based on results. In addition, a unilateral declaration of force majeure may be opposed by a counterparty leading to potential dispute. It may instead be advisable to review possible amendments to earn-in and joint venture agreements to determine if mutually beneficial amendments might achieve a better long-term result for the parties. Examples of the types of amendments that we are seeing under consideration include the following:

- extension of the time period for the incurrence of exploration expenditures, cash payments or attainment of project milestones (i.e., production decision, resource estimate, advanced project study like a feasibility study);
revision to the quantum of exploration expenditures or payments to reduce costs during the current COVID-19 environment while increasing costs at later dates; expansion of the area of interest around the project to potentially capture a larger project area; and rationalizing property interests to vest royalty interests without waiting for dilution events.

Every agreement is unique so there may be other provisions that would benefit from amendment. It is often easier to align parties’ interests for amendments during periods of disruption and uncertainty, so the COVID-19 pandemic may offer some opportunities for property relational agreements.

CONCLUSION

While a return to normalcy may yet be several months away, we encourage industry participants to proactively move now to best position themselves for the next wave of deal activity and consider how rapidly evolving governmental policy will affect their businesses in 2020.
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