

ART OF THE DEAL: GOLD RUSH

When Argonaut Gold went shopping for a gold mine, Castle Gold looked ideal. It was a perfect marriage, which just needed the lawyers to paper the deal — except for the fact that Castle was already considering transactions with dozens of parties

By Marzena Czarnecka



In the fall of 2009, as most of the world was quietly and fearfully observing the one-year anniversary of the mother of all financial meltdowns, Peter Dougherty was buying a pot of gold.

Dougherty has had some practice in following rainbows others couldn't see to a shiny payoff. As the Vice President of Finance and CFO of Meridian Gold Inc., he was part of the dream management team that built Meridian from a collection of assets that no one else wanted into a mega-success story. Meridian was subsequently bought by Yamana Gold Inc. for a cool \$3.5 billion in 2007.

Immaculate timing. And it just got better: while the world was coming to an end in 2008, Dougherty and his fellow ex-Meridians were all sidelined by non-compete clauses that formed part of the Yamana Gold deal. But by 2009, as the markets were showing signs of life – and the price of gold, arguably the least hammered of the commodities, was climbing back into record-setting highs – Dougherty was ready to get back into the game.

His vehicle? Argonaut Gold Inc., a private company where he serves as President and CEO, backed by several Meridian alumni, including Edgar Smith, who had been Meridian's Vice President of Operations and Brian Kennedy, Meridian's former CEO. Out of the gate, Argonaut had a stellar management team with a history of working well together for more than two decades. And creating exceptional value for shareholders. What it didn't have was, well, a gold mine.

Enter Castle Gold Inc. Castle had the very promising El Castillo gold mine in Mexico, a 50-per-cent interest in the El Sastre gold mine in Guatemala, and a gold-silver-copper project in La Fortuna, Mexico. Moreover, it was actively shopping around for a suitor.

It was a no-brainer: a marriage made in heaven, in which the only thing the lawyers would have to do was paper the deal. Except, of course, it wasn't. Because by the time Argonaut started eyeing Castle, the company was in the middle of a strategic review in which it was considering transactions with some 38 parties. "The problem with junior mining companies is that you don't really get value or recognition for what you have," says Mark James Plaxton, the 42-year-old founder, CEO and Chairman of the INTAC Group of Companies, a private wealth management firm.

In 2002, INTAC started investing in microcap Canadian mining companies, and by 2009 it was the largest shareholder of Castle Gold, with Plaxton serving as the company's Chairman of the Board, and, later in the deal process, as its interim President. And he was determined to maximize Castle's value. "We embarked on a very proactive strategic review," Plaxton says. With, he says, no clock ticking in the background. "To

sell a company that's valued at about \$100 million, you don't do that in three months," says Plaxton. Castle gave itself 12 to 24 months to find a buyer — or targets worth acquiring so that it could move on to the next level. "Everything was on the table."

And when he says everything, he means it. "We probably started with a hundred companies that we looked at as potential acquirers, targets or merger partners," he says. The independent committee of the board, represented by Michael Amm of Torys LLP, culled that list to 38 possibilities, then 15. Then five.

Argonaut wasn't on the list because, when the process started, Argonaut didn't exist. But the company was making lists and evaluations of its own, and its management team decided Castle Gold was going to be its new platform.

"When we looked at the sector, what we were looking for is someplace where we could really create value, and do so in the short term," says Dougherty. "With gold at an all-time high, it is not a five-year game. You can't wait several years for something to happen. I saw real value in these junior microcap companies." And exceptional value in El Castillo: under-explored, but with high potential for a comparatively modest capital investment. "We saw a great exploration upside in this project," he says. "It really hit all our investment criteria."

They just had to convince Plaxton. And he was, by his own admission, a hard man to please, as his exhaustive strategic review process underscored. "By the end of the process a lot of the lawyers thought I was a little paranoid," he admits. "I'm about dotting every i and crossing every t." And he made them do it. Over and over again.

Enter the lawyers. "By the time the Argonaut deal came to the table, Castle had been trying to get married for about a year," says Cameron Mingay, a partner with Cassels Brock & Blackwell LLP.

That prolonged dance with multiple parties had some positives – a stellar data room and a board well-versed in deal tactics – but also some drawbacks. "When you spend too many months negotiating, you can get tired of each other," says Mingay. And if you happen to be a desirable target – and Castle's properties made it such – "it's easy to fall prey to 'the other, cuter girl syndrome,'" as Mingay puts it. In other words, to be reluctant to close even the best deal, because an even better one might be just around the corner.

Argonaut's lawyers were sure they were bringing the best possible deal to the table. But then, the Argonaut team at Fraser Milner Casgrain LLP has been doing work for Dougherty and co. for years, and they're fans — and not just because the firm gets to work on exciting deals like the hard-fought sale of Meridian to Yamana. The relationship dates back to the earliest days of



Cameron Mingay; Cassels Brock & Blackwell LLP

Meridian. Dougherty and now-FMC partner John Sabine first met when Sabine was still at Fasken Campbell Godfrey (the predecessor firm to Fasken Martineau). As Sabine moved to Bennett Jones LLP, then to Donahue Ernst & Young LLP and then to FMC, Dougherty and the Meridian work followed.

“John’s a great guy in this industry, with a long history of doing mining acquisitions and a long history of knowing what’s going on,” says Dougherty. “But what’s more important than the reputation of your counsel is your relationship with them: you need time to build that rapport and trust, and we clearly have that with John.”

And, by extension, with the team that has grown around him at FMC, it’s a rapport and trust that’s reciprocated. Just ask Sander Grieve – who ran this deal for Argonaut as National Chair of FMC’s Mining Group – what he thinks of his clients. (See “In Argonaut’s Corner” on page XX for FMC’s team.) “These are very straight-up, their-word-is-their-bond type of guys to work with,” says Grieve.

Alas, Plaxton did not have that kind of 20-plus-year relationship of trust with the Argonaut principals. But he did have the advantage of having Mingay and the team from Cassels, which included Gregory Hogan and Angela Chu. And, after watching – sometimes from the sidelines, sometimes the centre of the battlefield – Castle’s strategic review process and negotiations for more than a year, Mingay had a pretty good notion of what it would take to find a deal that would work for Plaxton — and Argonaut’s first proposal wasn’t it.

Not that it wasn’t a terribly clever proposal. It was damn clever — too clever. Argonaut was a private company taking a run at a public company, a fairly unusual procedure, but not unheard of in the junior mining world. Argonaut, however, had no intention of staying private, and the obvious way to take Castle and go public in one fell swoop would be to do the deal as a plan of arrangement.

As Mingay saw it, a plan of arrangement was a great way to work most deals. But it wasn’t going to cut it in this deal. “It would require shareholder approval, it would require us to go court, it would require prolonged negotiations over terms,” he says. “It would introduce extra levels of complexity” to what already was a complex situation.

Mingay’s alternative was simple: he wanted a straight take-over bid. By eliminating shareholder votes and court dates, it minimized the risk for his client. Grieve liked what he heard — it would also make his client’s financing efforts easier. And as both sides were seriously interested in a done deal, it was to their mutual advantage to get it baked as quickly as possible.

“All the stuff that makes a deal more interesting to a lawyer – arguing about representations and warranties and all that arcane stuff – makes it less viable on the Street. The Street doesn’t care about all this stuff; it just wants to see the deal done,” says Mingay. “So let’s do this quick, because when we’re out there less, fewer things can go wrong.”

When he said “quick,” Grieve and Argonaut moved. By October 27, 2009, Argonaut and Castle had a support agreement in place. And it wasn’t your run-of-the-mill support agreement, either. “We had extraordinary lock-ups in this deal,” says Mingay. “A higher level of lock-up I’ve never seen. We had break fees and reverse break fees — anything that we could do to ensure deal certainty, it was there.”

There was even a little ratchet tied to the price of gold: because gold kept going up throughout the deal negotiations, Plaxton was worried about closing the deal at effectively yesterday’s economics. Argonaut agreed to an increase in the base price of the deal if gold kept on going up post-deal. Of course, that meant that the deal’s price tag was a moving target somewhere south of \$102 million (ultimately, it came in at \$112 million). Still, as far as Argonaut was concerned, even the high price was a fair price: Dougherty and co. were also betting that the price of gold was going to continue to rise.

It looked like they had a deal. The only thing missing was the money. “What we had on October 27 was essentially an unfinanced take-over agreement,” says Grieve. Dougherty and the ex-Meridians had some skin in the game, but not quite the \$100 million-plus that it would take to

buy Castle. And in the support agreement, they undertook to have the deal financed by November 24. In cash.

The cash aspect of the deal was a huge selling point for Plaxton. "There's a big premium for cash," he says. "Liquidity is a huge issue for shareholders, and it meant that every shareholder could do what they wanted with the proceeds." Like invest in one of the gold companies that Castle didn't end up marrying. "A cash deal gave power to the shareholders." So long as Argonaut could find the cash.

Mingay was sanguine: it was an ex-Meridian team. They would do it. Grieve, however, was a little more anxious. This was, after all, the fall of 2009, a mere 12 months since Lehman Brothers died and dozens of other formerly unassailable financial houses scrambled to survive. Dougherty, well, he was just going to get it done. And he did, closing the deal on November 20, with four days to spare.

The hero was GMP Securities LP, represented in the transaction by a team from Wildeboer Dellelce LLP that included Derek Sigel and Al Wiens. GMP enabled Argonaut to complete a private placement of 50 million subscription receipts, at \$3 per receipt, for a grand total of \$150 million, comfortably bypassing Argonaut's minimum target of \$130 million — the \$112 million purchase price of Castle, plus a few million extra in working capital to ramp up production and exploration. Sweet.

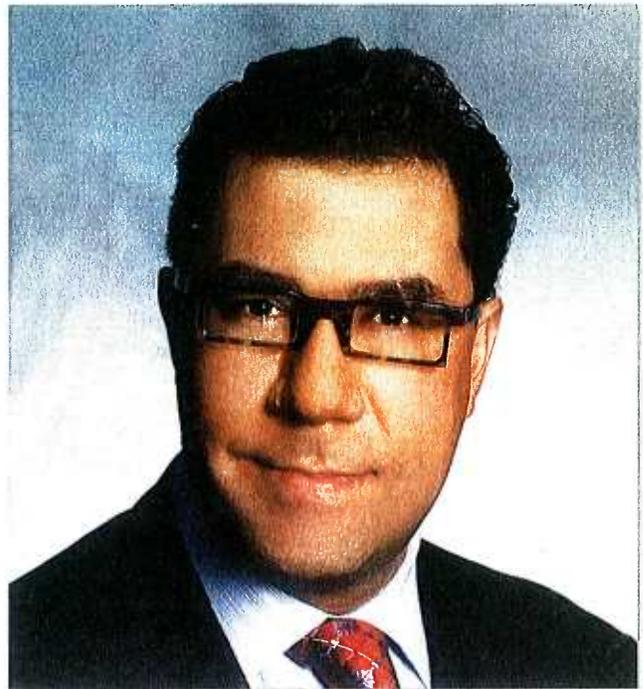
"We've never used GMP before — we've been a BMO firm," says Dougherty. "Now that doesn't mean a lot" — in other words, if there's a deal in Argonaut's future that appeals to BMO, he wants to work with the bank — "it just means that for this particular deal, because of the parties involved, GMP was the one that would work out."

It was a pretty straightforward financing, with your standard escrow release requirement that the acquisition of Castle be completed. Oh, and a liquidity condition that would cause a 10-per-cent increase in the conversion ratio if Argonaut wasn't public by December 31, 2009 — something that would cause some scrambling on the Argonaut side later on.

For Grieve, closing the private placement on November 20 was a huge relief: "With the capital markets being what they've been, even though everyone was gung-ho and everyone was saying these are the kinds of guys everyone wants to finance, to get \$150 million committed to get this deal to happen was a pretty extraordinary accomplishment."

Dougherty agrees. "It wasn't exactly easy," he says. "A lot of it was built on our past, but the past doesn't guarantee you're going to have a home run the next time."

Still, if you had to raise money in the fall of 2009, the sector to do it in was mining, and if you could do it in gold, you were laughing. While the downturn of late 2008 affected gold prices



Sander Grieve; Fraser Milner Casgrain LLP

too, they recovered faster than other commodities. By 2009 they were again touching US\$1,000 per ounce (albeit helped by the weak US dollar), and on a fairly steady upward trajectory.

"That certainly makes gold different from the other commodities from the capital markets' perspective in its ability to raise money and ability to make transactions," says John Nyholt, a partner with PricewaterhouseCoopers LLP in Toronto and the firm's National Leader of Transaction Services.

Argonaut had the money. The deal was as good as done. Wildeboer and GMP turned their attention to other matters. Mingay's team at Cassels took a breather: their client was as good as married. But for Grieve and the team at FMC, the rollercoaster ride continued. To get the money, they had to close the deal, and to get the money on the best terms, they had to take Argonaut public before year's end.

Meanwhile, they also had to make sure the shareholders tendered. And while the deal was sweetened with a nice premium, there were one or two little difficulties. Despite the sizeable chunk of shares held by Plaxton's INTAC and a 40-per-cent lockup in the support agreement, most of Castle's shares were spread across a dispersed base of retail shareholders. And it was Christmas.

Enter the proxy solicitors. "It was a great, very easy, no-problem file that turned out to be like herding cats," recalls Wes Hall, President and CEO of Kingsdale Shareholder Services Inc. "When you have people owning 10, 15, 20 per cent of the



Lonnie Kirsh; Kutkevicius Kirsh LLP

stock of a company, they pay attention to headlines and to stuff they get in the mail. When you have a deal that's not a huge deal, and people who have 100 or maybe even just 20 shares, and who will just make \$2,000, \$5,000 on the transaction — well, they're not going to drop everything else they're doing just to tender their shares before the bid expires."

Or are they? On December 29, the bid expired — and 91.25 per cent of Castle's shareholders had tendered. Grieve and Dougherty each let out a big whoop. "That put us into compulsory acquisition territory, which was great," says Grieve.

Dougherty is even more emphatic. "If you told me you were doing an all-cash deal in a rising-gold-price environment with a retail shareholder base, and you were going to get more than a 90-per-cent tender first round over the Christmas holidays, I wouldn't believe you," he says. "It's unheard of."

Hall, who doesn't typically engage in false modesty, says he was pretty pleased as well. The management team at Castle co-operated, and as they had been in "strategic review mode" for months, they had all the required shareholder information at their fingertips. But ultimately, he says, the massive tender was the result of ... shareholder fatigue. "We called them and called them and called them again, until people got fatigued and went to their brokers in the hope that if they did so, we'd stop calling," he quips.

While Kingsdale worked the phones, Grieve was working with Lonnie Kirsh of Kutkevicius Kirsh LLP, who was representing Intuitivo Capital Corporation in the last leg of the

transaction. "We were running three deal teams simultaneous at this point; it was very exciting," recalls Grieve.

Intuitivo was a capital pool company (CPC) listed on the TSX Venture Exchange and, like all CPCs, a company in search of a transaction. Under the TSX's rules, CPCs are created solely to invest in and raise money for private companies that want to be publicly listed and traded. In other words, just what Argonaut needed, as the \$150 million it was getting from GMP was contingent upon the company taking itself public.

GMP put Intuitivo on Argonaut's radar during their negotiations. "As we explored the various scenarios, we ran into a situation where, on December 31, we may not have a tradeable share," recalls Dougherty. A situation that would cause no end of angst — if Argonaut, in whatever form, wasn't publicly traded by December 31, the liquidity condition in its deal with GMP wouldn't be met. Argonaut would be on the hook for the 10 per cent bump, and GMP, says Grieve, "would presumably be unhappy, as they sought an interest in a public company."

The Toronto Stock Exchange came to the rescue, working with GMP and Argonaut on workable alternatives, the best of which all parties decided was a qualifying transaction via a CPC. Intuitivo hopped out of the wings, and on November 24 Grieve and Kirsh came to terms with what on the face of it would be an Intuitivo acquisition of Argonaut after its acquisition of Castle. Intuitivo put the deal to its shareholders as a qualifying transaction. It was, everyone assumed, a rubber-stamp type of transaction: still, Grieve heaved another big sigh of relief when the Intuitivo shareholder meeting, set for December 22, gave the deal a thumbs up. On December 29, the Castle bid expired, and on December 30, the deal with Intuitivo closed. Argonaut amalgamated with a wholly owned subsidiary of Intuitivo, which was then renamed Argonaut Gold.

"It was a very efficient transaction," notes Kirsh. "Most of these CPC qualifying transactions take months — five to six months. This one had a very short time fuse, and took about four weeks." And at 5:01 p.m. on December 30, 2009, Argonaut became listed on the TSX under the symbol AR.

Done. For the lawyers, that is. For Dougherty and the the Meridian team, the adventure is just beginning. "When I look at this company, I look back to what we looked like when we started Meridian," says Dougherty. The company was formed out of assets competitors weren't interested in. "We shopped it around — at least 16 guys looked at us, and nobody saw value. We saw greater value than others did. So we spun out Meridian and went public. We went to Chile. Nobody was willing to make an investment in us. Well, we saw value where others didn't, and



Kevin Thomson; Davies Ward Phillips & Vineberg LLP

that's how you succeed in this industry. You have to be able to see value where others don't. We see that same potential here."

At FMC, Grieve and the Argonaut legal team see more potential deals too. "It's a well-worn story in the mining industry," says Nyholt. "People who start with nothing, get some capital behind them, do a couple of well-organized acquisitions, do some development – frankly, get lucky – and then watch the market take off." And, ultimately, sell to the big guys. "The Barricks and Yamanas of the gold world are always looking for strong mid-tier companies to add to their fold."

And the cycle starts again. "It's one of the wonderful things about the Canadian mining space," says Kevin Thomson, a partner with Davies Ward Phillips & Vineberg LLP in Toronto, whose mining mandates include, among others, Canadian giant Barrick Gold Corporation. "It's filled with entrepreneurial, hungry people who love the mining industry and who just keep on starting new ventures." Along the way, he says, the successful ones collect "a very loyal following of shareholders who see their ability to create value and who will follow them anywhere."

That's priceless – that's what got Argonaut \$150 million in three weeks in 2009 – and that's why the success stories "are very careful not to burn their reputations by not asking their investors to follow them into sketchy ventures. The last thing they want to do is chase a rainbow," says Thomson. Well, unless they're damn sure there is a pot of gold at the end. ☪

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In ARGONAUT'S Corner

AT CRUNCH TIME, Fraser Milner Casgrain LLP was effectively running three deal teams for Argonaut, led by Sander Grieve, with Argonaut relationship partner John Sabine in the background as "senior statesman." Grieve and Linda Missetich led the Castle bid team. Missetich additionally headed up the private-placement team. Abbas Ali Khan headed up the CPC/amalgamation team. Zahra Nurmohamed led the tax team involved in each of the three transactions. Additional brainpower came from Brian Abraham, QC, and Ralph Shay; key associates on the file included Eric Foster, Peter Danner and Liz Fraser. US counsel was provided by a team from DLA Piper, led by Daniel Goldberg.

